

The SERVICE Framework: A Public-service-dominant Approach to Sustainable Public Services

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In this paper we argue that the new public management has been a flawed paradigm for public services delivery that has produced very internally efficient but externally ineffective public service organizations. Subsequently we develop the SERVICE framework for sustainable public services and public service organizations. This framework is rooted within the public-service-dominant business logic and emphasizes the need for a focus on external value creation rather than internal efficiency alone.

Building upon the call of Ashworth *et al.* (2013) for more theoretical critique and development of public management theory, the central argument of this paper is that the premises that underlie much contemporary public management theory, in its guise as the new public management (NPM), are flawed and have led to variable results in implementation. Far from creating the basis for sustainable public service organizations (PSOs) this body of theory has actually undermined their sustainability by encouraging a short-term, introspective and transactional approach to the delivery of public services (McLaughlin, Osborne and Chew, 2009; Radnor, 2007). We offer an alternative to this, based within the public-service-dominant framework for public services delivery (Osborne, Radnor and Nasi, 2013). We argue that it is essential for PSOs to move beyond the transactional approach and take a relational and public-service-dominant approach that emphasizes three elements: building relationships across the public service delivery system; understanding that sustainability derives from the transformation of user knowledge; and professional understanding of the public service delivery process which is predicated upon the inalienable co-production with service users.

Consequently this paper is in three parts. The first part develops a critique of the NPM and poses the ‘new public governance’ (NPG) as an alternative to it. The second part of the paper then offers a framework within which to situate sustainable business models for a whole range of PSOs – the SERVICE framework. The final part of the paper highlights its contribution and implications for theory and practice. Further, because this paper is a conceptual and theoretical one, the research agenda at the end of the paper details the research needed in the future to empirically test, validate and develop the framework proposed.

We emphasize that in proposing this framework we are not creating it from first principles. On the contrary, it draws upon and is embedded within an emerging strand of public management research and theory over the last decade and more (e.g. Benington and Moore, 2010; Dahler-Larsen, 2014; Gains and Stoker, 2009; Guthrie, Ball and Farneti, 2010; Klijn, 2008). What our framework does is build upon these insights and develop an integrated context within which to entrench sustainable business practice for PSOs over the next decade, and beyond.

From NPM to the NPG

Elsewhere we have charted the development of the NPM as a response to the perceived failings of public administration and the subsequent challenge to its shortcomings from the NPG (Osborne, Radnor and Nasi, 2013, Osborne *et al.* 2014). Others have also argued that the NPM was actually an ideological attempt to ‘roll back the state’ and to reconfigure the post-war European consensus on the welfare state (Dawson and Dargie, 1999; Dibben, Wood and Roper, 2004; Ferlie *et al.*, 1996). In this reading, the NPM was not solely a managerialist public service reform agenda but was rather part of an ideological confrontation on the value basis of the post-war welfare settlement across the globe (Mischra, 1984). Drawing upon public choice theory (Buchanan and Musgrave, 1999), the NPM articulated a set of neoliberal assumptions both about the inefficiencies of the state provision of public services (because of the self-serving behaviour of politicians and of government officials) and about the hegemony of the market as an antidote to these ills. Subsequently, not only would the NPM eradicate the drain of the state monopolistic provision of public services upon the economy, it would also free individuals to make their own rational decisions about responding to their welfare needs (see for example Pirie, 1988; Savas, 2000). Bevir and Rhodes (2003) have argued that this consequently led to a set of seven strands of NPM that were implemented variably across the world and that were all located within this neoliberal critique. These strands were privatization, marketization, corporate management, decentralization, regulation, political control and internal markets. An alternative line of argument has posed NPM as an aberrant departure from the political accountability concerns of ‘traditional’ public administration across Europe and called for the latter’s re-invigoration (Kickert, 1997).

The relationship between the NPM and the NPG has been examined by us in detail elsewhere (Osborne, Radnor and Nasi, 2013). We would emphasize here that the NPG is not a complete departure from the NPM. Rather it is a reintegration of the accountability concerns of public administration with the managerial focus of the NPM – but in a framework that moves beyond both to recognize the significance of service systems, as discussed below. In this paper, therefore, we focus on what we argue are the shortcomings of the NPM

that derive from five directions. First, society has been transformed profoundly since the early inception of the NPM in the 1980s. Society has become more fragmented and the processes of public service delivery have diversified – a phenomenon referred to elsewhere as the ‘hollowing out of the state’ (Haveri, 2007; Milward and Provan, 2000; Rhodes, 1994). Consequently PSOs can no longer act as if their efficiency, effectiveness and sustainability are in their own hands alone. In reality PSOs are now part of complex public service delivery systems where their mission-critical objectives require the successful negotiation of relationships within these systems – with policy makers, other PSOs, service users, citizens, and indeed a range of service system elements and stakeholders. This is discussed further below.

Significantly the NPG perspective goes beyond the network governance approach that has been articulated by, amongst others, Klijn (2008). The latter approaches acknowledge that individual PSOs can no longer act in isolation and that they require a focus upon inter-organizational policy and implementation networks (comprising a multiplicity of PSOs) to properly understand the delivery of public services. However, the thrust of the NPG is that such an inter-organizational perspective is necessary but not sufficient. Drawing upon services theory (e.g. Gronroos, 2007) it conceptualizes public services not as produced within inter-organizational networks alone but rather as produced within *public service systems*, as suggested above. It is the interaction of these complex service systems that is the core to effective public service delivery not simply the governance of networks of PSOs. The task is thus not simply the governance of networks of PSOs but the operationalization of these interactive and complex service systems.

Second, the NPG paradigm argues that PSOs are not producing technically designed and manufactured products but rather are delivering intangible services that require attention to the processes of service delivery and to relationships with service users, and not simply to service design. Gronroos (1998) has identified this search for the ‘missing product’ as a common mistake of failing service firms and this is equally relevant to PSOs as they strive to develop sustainable business models for the twenty-first century.

Third, PSOs also need to recognize that the short-termism and product-dominant basis of the

NPM is counter-productive to their survival. It assumes that their sustainability is driven by a business equation where production and consumption are treated separately – the costs of the former can be reduced without affecting the latter. This might be the case for manufactured products, but it is certainly not the case for services, including public services. In this case reducing production costs directly affects the quality of their use/consumption – and this affects their longer term viability and sustainability (Gronroos and Ojasalo, 2004; Normann, 2000). A key issue here is the role of staff in service delivery. For many service firms they are one of their most expensive costs. PSOs, in particular, have sought to limit unit costs by reducing staff costs (such as residential homes for elderly people employing less well trained staff or reducing staffing ratios). Service theory identifies this as a potentially counter-productive approach. Reducing staff costs without consideration of the delivery process can reduce the quality of the service – which ultimately undermines their sustainability in a mixed economy of care. Rather, service firms need to invest in the ‘right’ staffing to ensure and improve the quality of the service delivered, thus strengthening their market position and sustainability – what Normann (2000) calls the ‘virtuous circle’ for the profitability and sustainability of service firms.

Fourth, throughout both public administration and the NPM, the task of public service delivery has been conceptualized as something to be enacted by public service professionals and where the service user is largely passive in the process, whether considered as a ‘client’ or ‘customer’ of PSOs. There have of course been movements to bring the service user into a more active role in service delivery through ‘co-production’ (an excellent summary of this literature is provided by Alford, 2014). Important as these approaches are, though, they frequently mistake the nature of public service delivery. In reality it is impossible to deliver any service without an element of co-production (Xue and Harker, 2003). Co-production is part of the very essence of a service both because its performance is created where the users’ expectations collide with their experience of the service and because the users themselves are an active part of the service process not a passive recipient of its outputs. Consequently the task becomes not one of how to bring the user into co-production but rather how to engage actively with this already ex-

isting co-production within the public service delivery process in order both to improve the quality of existing services and to plan for future service delivery and innovation. It is important to be clear that this is different from the ‘consumerist’ movement that has dogged public services over recent decades. This movement sought to extract and objectify the ‘public service consumer’ from the overall service process and has been subject to strong critiques elsewhere (e.g. Powell *et al.*, 2010). What is proposed here is rather to understand the totality of the public service production system and the complex iterative interactions between service users and public service staff that occur within it.

Finally, the NPM appears limited in its response to the challenges to traditional public services delivery of knowledge-driven services delivery within the digital economy. Not only is the latter phenomenon transforming the nature of relationships between PSOs, politicians and service users, it is posing questions about the achievement of *public value* as the indicator of public service effectiveness rather than internal measures of public service efficiency (e.g. Bekkers *et al.*, 2011; Benington and Moore, 2010; Moore, 2002) and the governance processes required to negotiate agreement about such effectiveness (e.g. Brown and Osborne, 2013). The debate about public value is an important one. It shifts the focus of reforming public services away from internal efficiency alone and situates it rather within the context of adding value to the lives of citizens and service users – whilst also acknowledging that such ‘value’ is negotiated within the democratic polity (Gains and Stoker, 2009).

This is not to say that the NPM has had no positive impacts upon public services delivery. This would be facile. As we argue below it has been significant in addressing the prior poor design of public services in many countries (Barraza, Smith and Dahlgard-Park, 2009; Radnor, 2010); it has revealed the importance of balancing efficiency and effectiveness in delivery of public services and provided important tools to do so (Dahler-Larsen, 2014; Höglström *et al.*, 2014; McLaughlin, Osborne and Ferlie, 2002). Also the use of contractual mechanisms within an NPM framework has sharpened the focus of service delivery in many cases (Wistow *et al.*, 1994). Some have also argued that it has been an important tool of reform to drive broader societal reform in central and eastern Europe (Sorin and Pollitt, 2014). However, our

argument is that, valuable as these benefits have been, their impact has been diminished by the flaws of NPM in practice as discussed above – and particularly by the extent to which it has produced an introspective and short-term culture and strategic orientation that has diminished the ability of PSOs both to respond to external change and to deliver external effectiveness and public value.

Interim conclusion

What has been remarkable in the early responses to the global recession by governments and PSOs alike is how rooted they have been in the tenets of the ‘old’ NPM and the belief that internal cost cutting and efficiency programmes will produce sustainable PSOs for the long term (or even the middle term, for that matter) – despite the limitations outlined above. The underlying question therefore is that of the nature of sustainable business practice for PSOs within this new reality. In the next part of this paper we sketch the elements of an alternative framework of sustainable business practice for PSOs that embraces both the reality of the challenges that the NPG paradigm poses for them and the implications of a public-service-dominant logic for public services delivery.

Towards a framework for sustainable business models for PSOs

Sustainable business practice in commercial markets has traditionally been equated with a healthy ‘bottom line’ profitability that provides a return for shareholders and/or owners (Farris *et al.*, 2010). More recently however, there has also been a growing awareness that, even in commercial markets, this is not sufficient. This has led to alternative models of sustainable practice including the triple bottom line (Elkington, 1994) and social audit and social accounting based ones (Gray, 2002).

For PSOs, there has been a strong critical accounting strand over the past 20 years that has argued that ‘traditional’ bottom line measures of sustainability capture neither the complexity of the challenges that PSOs face, as outlined above (Benington and Moore, 2010; Stoker, 2006), nor their role in contributing to higher level goals of sustainable economies and societies (Ball and Osborne, 2010; Guthrie, Ball and Farneti, 2010). Osborne (2010) posed the question as to what con-

stitutes sustainability for PSOs within the NPG. Drawing upon the above we would argue that it is insufficient to define this as the sustainability of individual PSOs. This is of course essential to ensure that there are individual providers of PSOs. However, the sustainability of individual PSOs has to be integrated with an outward-facing concern with public service effectiveness (Radnor and Osborne, 2013), the creation of public value (Moore, 2002), and a balancing of individual organizational sustainability against overall service sustainability (Radnor *et al.*, 2014). Consequently we would argue that sustainability for PSOs must be assessed across four dimensions:

- the sustainability of individual PSOs,
- the sustainability of public service delivery systems and their governance mechanisms,
- the sustainability of local communities and
- environmental sustainability.

This necessitates PSOs moving beyond strategic planning, with a focus on individual survival, and towards a strategic orientation that is value based (Deshpande, Farley and Webster, 1993) and requires a ‘business model’ that is rooted in such an externally and value focused view of public services delivery.

A business model is a simplified representation of choices both about how an organizational entity, public or private, creates and distributes value amongst its stakeholders over time and how it ensures its own sustainability into the future (Zott, Amit and Massa, 2011). Business models are more than a simple descriptive narrative – they need to guide practical actions (Magretta, 2002). Nor are they unchanging recipes since successful business models will evolve with environments and opportunities: new combinations of external needs and possible solutions are constantly emerging and recombining as technology and the environment change (Baden-Fuller and Morgan, 2010).

Traditional business models in the private sector have been predicated upon the ‘single bottom line’ of organizational profitability as a measure of sustainability. However, as discussed above, this is an insufficient measure of sustainability for PSOs. Public service business models need to be more sophisticated and to be predicated upon public value rather than an organizational ‘single bottom line’.

Consequently, our approach moves beyond the narrow focus of traditional business models. Further, recent authors have argued strongly that this approach is not ‘fit for purpose’ for modern businesses, let alone PSOs. Most significantly, Lusch and Vargo (2014; see also Verma and Jayashima, 2014) have argued robustly that contemporary business requires business models embedded within a service-dominant logic – because this logic, predicated upon knowledge transformation, is the basis for value creation for any type of business. This is the approach that has been followed here. What is proposed is a framework within which to develop sustainable business models for a whole range of PSOs. The seven elements of the framework are not constant for all PSOs – the balance between these elements will be different for different PSOs or service scenarios. Moreover the elements do overlap to an extent, or approach similar issues from different directions. Consequently this framework has the potential both to steer research and evaluation upon the delivery of public services and to guide public service managers in developing sustainable business models for their own agencies.

Towards sustainable business models for PSOs: the SERVICE framework

Thus far we have argued for embracing rather than minimizing the complexity that PSOs face in achieving sustainability, as well as for clarifying what this might mean in the context of public service systems. We have argued for a value-based approach that emphasizes the relationships, governance and negotiation that is epitomized within NPG rather than the transactional focus of the NPM. At the heart of this is the public-service-dominant business logic (Osborne, Radnor and Nasi, 2013), as discussed above. Drawing together the insights from a growing community of scholars who have been exploring these relational and service-oriented aspects of public services delivery, we argue here for seven propositions to underpin a framework for sustainable business models for PSOs in the twenty-first century: the SERVICE framework. The use of such heuristics as this have been argued elsewhere to be an essential contribution to effective business process redesign – both as conceptual tools and as guides for enacting theory in practice (Reijars and Mansar, 2005).

Some of these propositions have been articulated above but they bear repetition as part of the whole. The propositions are as follows.

- Public services are systems and not just organizations, or even inter-organizational networks, and need to be governed as such, embracing all of their elements (Radnor *et al.*, 2014).
- Individual PSOs need to embrace organizational sustainability in their own right in the short term – but this is a necessary and not a sufficient condition for the long-term sustainability of PSOs and of public service systems (Booze-man, 2002; Grindle and Hilderbrand, 1995).
- Sustainable PSOs are dependent upon building long-term relationships across service systems rather than seeking short-term discrete and transactional value (McGuire, 2012; McLaughlin, Osborne and Chew, 2009).
- Consequently, such internal efficiency is necessary for individual PSOs but will not in isolation produce sustainable public service systems; rather PSOs need to be outward-focused on external effectiveness for service users and on creating sustainable public value for local communities (Radnor and Osborne, 2014; Vidal, 2013).
- PSOs need to innovate and negotiate innovation across service systems to achieve service effectiveness (Osborne and Brown, 2011).
- Co-production is at the heart of public services delivery and is the source both of effective performance and of innovation in public services (Osborne and Strokosch, 2013).
- Public service systems need to develop, capture and use the key resource of knowledge to sustain and deliver effective service experience (Lusch and Vargo, 2006, 2014).

The SERVICE framework for sustainable business models for PSOs

Proposition 1: Public services are systems not just organizations and need to be governed as such

The NPM was predicated upon the necessity of individual PSOs competing in markets and quasi-markets (Le Grand, 2007). This required them to clarify unit costs on a discrete basis and invariably ignored the transaction costs of such a business model – despite long-standing evidence

in commercial markets of the impact of such ignorance (e.g. Dyer and Chu, 2003).

Consequently PSOs, like for-profit organizations in the late twentieth century, started to explore the efficacy of inter-organizational networks as an alternative to, or modified form of, the market model (Kickert, 1997; Klijn, 2008; Provan and Milward, 2001; Rhodes, 1997), and in order to develop models of sustainability predicated upon collaborative endeavour rather than competition (Best, 1990; Phelps and Raines, 2003).

Whilst such approaches perhaps engaged more with the actuality of public services provision in the post-modern era (Havari, 2007), they nonetheless continued to mistake the nature of this provision as being something that was the domain of PSOs individually. However, a core tenet of the NPM and a public-service-dominant logic is that PSOs are only part of the systems that deliver public services. Other key elements include service users themselves, their families and significant others, local communities, for-profit and third-sector organizations, and hard and soft technologies. Sustainable PSOs must therefore embrace these service systems and learn how they interact with their other elements in order both to be sustainable within these systems and to contribute to sustainable service systems. Technologies for such systemic and process-oriented business models do exist – notably service blueprinting (e.g. Lovelock and Wirtz, 2006; Shostack, 1982). They have begun to be applied to public services delivery in discrete areas such as higher education (Baranova, Morrison and Mutton, 2010; Radnor *et al.*, 2014). However, their potential for contributing to sustainable PSOs and sustainable public services is yet to be fully realized. This service system perspective is the cornerstone of our framework of sustainable business practice for public services.

Proposition 2: PSOs need to embed organizational sustainability in their own right in the short term – this is a necessary but not a sufficient condition for long-term sustainability

As discussed above, a significant contribution of the NPM to public management was to articulate that PSOs have to address the issue of organizational sustainability if they are to continue to contribute to public service systems (and maintain their employment of staff and

managers, needless to say). A limitation of this NPM reasoning, though, was then to suppose that such sustainability derived from creating PSOs as individual service ‘silos’ responsible for their own costs and in rivalrous competition with all other PSOs (McLaughlin, Osborne and Chew, 2009). However, such a model has long been out of favour in successful for-profit service businesses due to, amongst other factors, the fact that it makes the sharing of risk in relation to innovation problematic (Best, 1990).

As this limitation of the NPM became apparent, in Europe at least, public policy and PSO managers turned to alternative strategies – including inter-organizational networks and social enterprises and entrepreneurship. Whichever alternative is adopted, however, a basic element of a framework for sustainable public services is to understand that the sustainability of individual PSOs is a precursor (albeit an essential one) to service system sustainability – which must be the ultimate goal. A key contribution of a public-service-dominant logic is to argue that organizational and service system sustainability are inextricably linked together. As Normann (2000) points out, service firms can only be successful if they embrace the overall service system, and these service systems themselves require sustainable service firms as one of their essential elements. Bringing Propositions 1 and 2 together our framework for sustainable public services argues that PSOs need to be simultaneously sustainable in their own right whilst also recognizing that service sustainability is only possible when this is embedded within sustainable public service systems.

Proposition 3: Sustainable PSOs are dependent upon building long-term relationships across service systems rather than seeking short-term transactional value

Given that we have argued in our first two propositions that PSOs cannot operate in isolation of the holistic service systems that they exist within, it follows axiomatically that the governance of relationships within these systems is a key task for their sustainability. One of the failures of public services marketing, as it has evolved over the past four decades, has been for it to become situated as a tool of the ‘marketization’ of public services as part of (often ideological) NPM-style agendas, rather than as a desirable management discipline

in its own right (Burton, 1999; Walsh, 1994). In doing so it has neglected the opportunities offered by alternative conceptualizations of marketing that take institutions and networks, rather than discrete transactions, as the central unit of analysis (Laing, 2003). McLaughlin, Osborne and Chew (2009) have argued that public services marketing practice has been dominated by precisely such transactional models of marketing which have belied the relational complexity of public service systems – and have hence contributed to their lack of sustainability. There has also been a consequent failure to explore alternative approaches to marketing that might offer a route to genuine sustainability by identifying and facilitating the enduring relationships that are essential to sustainable public services (Bovaird, 2006; Erridge and Greer, 2002; Schwartz, 2005).

The genesis of public services marketing is generally credited to the work of Philip Kotler (*inter alia* Kotler and Andreason, 1975; Kotler and Levy, 1969). Crucially, Kotler's ideas about public services marketing were rooted in classical economics and a model of exchange theory that supported a purely transactional view of marketing, with the PSO as a discrete entity operating in isolation from other organizations. This position has been criticized latterly in the broad management literature, through the concepts of 'new competition' (Best, 1990) and 'new institutionalism' (Powell and DiMaggio, 1991). Drawing upon the work of Benson (1975) on resource dependence theory and Williamson (1985) on transaction cost analysis these approaches posit the need for collaboration in order for PSOs to lever in the information, resources and capabilities necessary for sustainability. Such a model introduces new levels of complexity to exchange relationships that McLaughlin, Osborne and Chew (2009) have argued are beyond the scope and competences of traditional transactional models of marketing. The alternative, they contended, is to embrace the service-dominant model of relationship marketing (RM).

RM acknowledges that sustainable competitive advantage increasingly requires collaborative activity rather than rivalrous competition and that relationships are often the most valuable resource of an organization, public or private (Helfert, Ritter and Walter, 2002; Payne and Ballantyne, 1993; Veloutsou, Saren and Tzokas, 2002). Harker

(1999) has defined RM as an organization engaging in '...proactively creating, developing, and maintaining committed, interactive and profitable exchanges with selected customers over time' (p. 16). The core of such relationship building is *trust*.

Given the enduring emphasis in public policy upon trust as a governance mechanism within the plural state (Davis and Walker, 1997; Osborne, 2006), it is therefore surprising that RM has not yet made a significant contribution to public management. It offers a robust framework by which to fashion and guide, and when necessary terminate (Gulati, Nohria and Zaheer, 2000), inter-organizational relationships within the plural state.

This contribution is enriched further by allying it with the associated concept of 'relational capital'. Kale, Singh and Perlmutter (2000) define this as '... the level of mutual trust, respect and friendship that arises out of close interaction *at the individual level* between alliance partners' (p. 218, our emphasis). The key contribution for PSO managers here is to focus upon the import of *individuals and individual relationships*. Too often in the public administration and management field, relationships are reified to the organizational level – the neo-corporatist assumptions of the now defunct Voluntary Sector Compact in the UK are a good example of this (Osborne and McLaughlin, 2002). A focus on relational capital makes explicit that the key to effective relationship management is to locate relationships at the individual level, where the staff of a PSO interact with policy makers, the staff of other PSOs and service users. Such an approach is essential to building a sustainable business logic for PSOs.

Thus far this discussion has emphasized the contribution of RM to enhancing inter-organizational trust and relationships. However, the approach also speaks to the equally important issue of the relationships between service providers and their users – denoted 'business-to-customer' (or B2C) relationships within RM (Gummesson, 2007). As is discussed further below, the co-production of public services between PSOs and their users is essential to service system sustainability. RM has an important, and to date unrecognized, contribution to make to this debate in public management – and to a framework for sustainable public services.

Proposition 4: Internal efficiency is necessary but not sufficient for sustainable PSOs – they also need to have an outward-facing not inward-facing focus on (public) value

This proposition is a corollary of Propositions 1 and 2 – it explores their implications for managerial practice within PSOs. Perhaps one of the most disappointing failures of the NPM has been that of the application of ‘lean’ approaches to reforming and improving public services delivery (Radnor and Walley, 2008). Lean seeks to ‘design out’ inconsistency and waste in the operational processes of service delivery. It is predicated upon the need to design these processes to produce maximum value for their end-users (Holweg, 2007; Womack and Jones, 1996).

In the last decade such approaches have been seen extensively as a panacea for poor public service performance and as a significant contribution of the NPM to their reform. Indeed, their early implementation did lead to substantial improvements in the efficiency of public services delivery in a range of areas including local government, the health service and national government functions (e.g. Barraza, Smith and Dahlgaard-Park, 2009; Radnor, 2010). However, such efficiency gains did not prove to be sustainable in the longer term. There were two reasons for this (Radnor and Osborne, 2013). First, these savings came primarily from lean addressing prior design faults in PSOs rather than addressing longer term sustainability issues. Once these ‘low hanging fruit’ had gone, though, lean proved incapable of addressing the more fundamental question of a sustainable business model. Second, and most relevant here, the application of lean within PSOs mistook the nature of end-user value. It universally took an inward focus upon *internal* end-users and user value, rather than an *external* focus on service users and public value.¹ Put simply, such an approach is able to create more efficient PSOs (by improving internal efficiency) but fails to address public service effectiveness because it does not orient itself to public value as expressed by its external end-users or debated within the democratic polity. Such a mistaken approach resulted

in very efficient but *permanently failing* PSOs (Jas and Skelcher, 2005; Meyer and Zucker, 1989) in the sense that they systemically failed to address the issue of creating public value for end-users (Gains and Stoker, 2009). It is essential of course to enhance and make sense of internal efficiency and to address organizational sustainability, as discussed. But this only produces long-term sustainability, for PSOs and public service systems, when it is predicated upon an external focus that is about adding value to the external end-users of public services.

Proposition 5: Sustainability for PSOs is predicated upon innovation as a means through which to achieve service efficiency and effectiveness

NPM acknowledged innovation as essential to sustainability in public services. However, its model was derived from product-dominant approaches to innovation that situated it as a driver for competitive advantage in competitive commercial markets (e.g. Porter, 1985). Increasingly, though, the for-profit sector has come to view open, collaborative, innovation as a more effective route to commercial sustainability – and particularly in the service sector where multiple service firms can interact within a service system (Bishop *et al.*, 2008; Skalen *et al.*, 2014). Not only does it share the costs and risks of innovation, it also combines the resources and knowledge of different firms to enhance innovative potential (e.g. Chesbrough, 2003; Von Hippel, 2006).

Once more drawing upon the services management literature, we would argue that for innovation to contribute to sustainable PSOs and public service systems it needs to break free of the product-dominant constraints that have inhibited its contribution to such sustainability in the past (Djellal, Gallouj and Miles, 2013; Osborne and Brown, 2011). There are three conditions for this. First, as already articulated it needs to be externally focused to add value to the lives of service users rather than focused on internal efficiency (alone). Second, the service user and co-production are required to be at the heart of the process if innovation is to be genuinely oriented to service effectiveness (Skalen *et al.*, 2014; Verma and Jayashima, 2014). Finally, governance rather than management is the essence of innovation in intricate interactive service systems. To take but one example, Brown and Osborne (2013) have illustrated how a

¹In contrast such an external end-user focus was a core feature of the Toyota Production System that was applied to for-profit businesses, and from which the model of lean evolved (Holweg, 2007).

governance approach to risk is essential to innovation in designing and delivering public services, which requires the negotiation of innovations across such complex service systems and which makes explicit the costs and benefits of any innovation as well as where these might lie (see Kinder (2000) for an example of the impact of the avoidance of such risk governance on innovation in public services).

Innovation is an inherently risky process – the majority of innovations fail as the evidence demonstrates (Klein and Sorra, 1996). If it is to contribute to sustainable business logic for public services then an explicit engagement with these risks and their governance is essential. If such a proactive process is engaged in, innovation offers a real contribution to sustainable PSOs. This can be through their continuous development and improvement (incremental innovation), the development of new services complementary to those that a PSO currently offers (evolutionary innovation), the geographical or industry expansion of existing services to new groups of service users (expansionary innovation), and the creation of genuinely new forms of public services that address newly identified needs in novel ways (total innovation) (Osborne and Brown, 2011).

Proposition 6: Co-production is the source both of effective performance and of innovation in public services

As discussed earlier, there is a substantial and growing literature within the public management literature concerned with ‘co-production’ in the implementation of public policy and the design and delivery of public services (e.g. Alford, 2014; Bovaird and Loeffler, 2012; Fledderus, Brandsen and Honingh, 2014; Jakobsen, 2013; Pestoff, 2014; Vamstad, 2012; Van Eijk and Steen, 2014; Verschuere, Brandsen and Pestoff, 2012). Whilst this literature includes a continuum of perspectives on co-production, it has often set the co-production of public services apart as a variation on the ‘usual’ model of public service delivery where ‘public officials are exclusively charged with responsibility for designing and providing services to citizens, who in turn *only* demand, consume and evaluate them’ (Pestoff, 2006, p. 506; our emphasis). Thus it discusses the ways in which user involvement can be ‘added into’ the operational process of service delivery (Bovaird, 2007).

Such an understanding of co-production, we would argue, is derived from a product-dominant logic where production and consumption are separated as discrete processes – thus public services are conceptualized as products to be designed and produced by public policy makers and service professionals and consumed (relatively) passively by service users. Co-production can only occur at the behest of, and controlled by, service professionals. However, a central tenet of the public-service-dominant logic is that co-production is an unavoidable element of public service delivery and central to a sustainable business model for PSOs.

We would argue that co-production is an essential and intrinsic process of interaction between any service organization and its service users at the point of delivery of a service (Gummesson, 2007). From a public-service-dominant approach, therefore, there is no way to avoid the co-production of public services. The question is thus not how to ‘add-in’ co-production to public services but rather how to actively engage and work with it in order to ensure sustainable PSOs and public service systems (Osborne and Strokosch, 2013). We would also add that co-production does not always have to be a positive process. If its actuality is mishandled it can lead negative effects for external public value and public service effectiveness – as the emergent literature on ‘co-destruction’ in the services management field has begun to make explicit (Echeverri and Skalen, 2014; see also Needham, 2008).

Normann (2000) has encapsulated co-production as ‘the moment of truth’ of services delivery. Service organizations can only ‘promise’ a certain process or experience – the actuality is dependent upon such co-production. A classic example of this would be the co-produced experience of residential care by the interaction of staff and service users in a residential home for the elderly. The managers of this home may have a vision of what care they want to provide, but the actuality of it is enacted in the iterative interactions between service staff and service users.

In reality, of course, such co-production of public services is a continuum rather than a steady state. Public services such as residential care and education are clearly instances where it is high, owing to the fact that consumption and production take place at the same point in time and with direct face-to-face contact between the service

user and the service provider (in the care home or the classroom respectively). By contrast, they are rather lower for electronic public services (such as paying your local taxes through a web portal) that do not have the inter-personal immediacy of face-to-face contact between the service provider and the service user.

Conceptualizing co-production as a core element of sustainable public services reframes our understanding both of the service delivery process and of the role of public management in achieving such sustainability. To take just one issue, a public-service-dominant approach to innovation in public services puts the service user rather than the policy maker or professional at the heart of this process (e.g. Gallouj, 2002) and has profound implications for the management of the process as stated in Proposition 5 – such as in terms of how public service innovations are derived and how risk is governed in the innovation process, as discussed previously.

A core element of a public-service-dominant approach to the co-production of innovation also relates to our final Proposition 7. This is its potential to unlock the tacit or ‘sticky’ knowledge that service users possess in order to improve existing or develop new services (Von Hippel, 1994, 2006). Here, a PSO proactively seeks to uncover, understand and satisfy ‘latent (or future) needs’, rather than simply reacting to existing or currently expressed needs – as has invariably been the case with public services. This then takes the process beyond co-production alone and unlocks the potential for the co-design and co-creation of public services between service users and service professionals, both increasingly argued as vital for sustainable public services into the future (Alford, 2014; Bason, 2010). The services management literature has highlighted a range of ways in which such service user co-production of innovation can be achieved (e.g. Alam, 2006) as well as highlighting some of its drawbacks and dangers (such as over-customization and its consequent financial implications). It has also explored the way that service users can destroy as well as create value, through ‘co-destruction’, as noted above. This is a further significant debate that is absent from public management and which could enrich the discourse on public services delivery and reform, as well as contributing to sustainable public services for the future.

Proposition 7: A key resource for PSOs is knowledge and using it for delivering service experience

Two of the most common truisms about services management are that service performance is created when service user expectations collide with the reality of their service experience and that the process of service delivery is about the transformation of knowledge into such a service experience (Gebert *et al.*, 2007; Muller and Zenker, 2001). This is as true for public services as it is for other services. Despite this, public policy makers and public service managers have persisted in the search for *product*-design routes to sustainability – through the iterative restructuring of PSOs or through a focus on the technical specification of public services, in terms of professional roles, rather than upon this value-adding knowledge transformation process.

For public services the sources of such knowledge are threefold – *the technical knowledge* of public service professionals, *the ‘sticky knowledge’* (Von Hippel, 1994) of service users and *the contextual knowledge* of other key stakeholders in the public service delivery system (such as carers, family members and members of the local community). A sustainable business model of PSOs has to focus upon how to capture these varying forms of knowledge, weigh them against each other and transform them into service outcomes for their end-users. This task has been made both easier and more complex by the advent of digital technology. This offers the promise of greater access to a wider range of knowledge sources – but such access also offers a challenge in terms of sifting and weighing these information sources against each other (Dunleavy *et al.*, 2006).

Elsewhere, Lusch and Vargo (2006, 2014) have argued that such transformation of knowledge is actually the defining feature of a sustainable business model in any market, public or private, product or service based. A sustainable business model is thus not concerned with the control of the unit costs and internal efficiencies of a production process, but rather with ‘the application of specialized skills’ and where ‘knowledge is the fundamental [resource]’. In this process the service user is always the co-producer of value in that there is no extant value for a service until it is used – ‘experience and perception are essential to [service] value

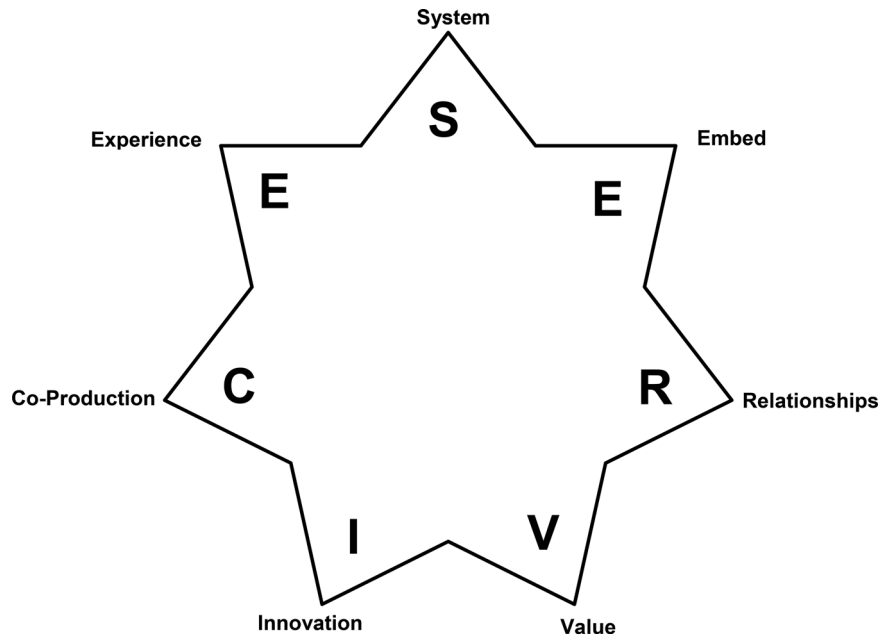


Figure 1. The seven-pointed SERVICE star of a sustainable business model for public service organizations

determination' (Lusch and Vargo, 2006, p. 44). A public-service-dominant model of sustainable business practice is thus one that places the utilization and transformation of knowledge and skills at the heart of public service delivery to achieve service experience rather than the specification of units of output and their associated costs.

Conclusions: towards sustainable PSOs and sustainable public service systems

In this paper we have argued for a public-service-dominant approach to delivering public services as the only route to long-term sustainable PSOs and sustainable public services. We have argued that the NPM, whilst containing important insights and producing some legitimate gains, was a flawed model and has had variable results in implementation. First, it sought to impose a product-dominant logic onto public services rather than understanding the fundamental differences between product and services management. Second, it has been unable to come to terms over the last decade with the emerging dominant paradigm of public services delivery –NPG (Osborne, 2010), which has recognized that public services delivery requires the governance of sophisticated public service systems rather

than individual PSOs. As an alternative we have argued for a framework for a sustainable business model for PSOs that embraces their public-service-dominant nature. Subsequently we have developed this argument into seven propositions to support a sustainable business model for PSOs and for public service systems. These are shown diagrammatically in Figure 1 in our SERVICE framework for a sustainable business model for public service organizations. This framework now requires further empirical testing to refine its components, test out their limitations and exceptions and to develop metrics to evaluate their impact.

We close with three areas requiring critical attention. First, our argument has already alluded to the development of ICT and digital technology. As for services in general (Ghosh, Surjadjaja and Antony, 2004; Surjadjaja, Ghosh and Antony, 2003), this poses important challenges to sustainable PSOs and sustainable public services, by challenging their very nature. Most public services have traditionally been based upon Normann's 'moment of truth' where service providers and service users interact in real-time. Increasingly though such moments of truth are becoming virtual and mediated by digital technology. Work has begun upon exploring the implications of this seismic innovation for public services (e.g. Margetts, 2009). The implications of this work for

sustainable PSOs and public services urgently need to be considered.

Second, it would be sophistry in the extreme to characterize all public services as part of a homogeneous whole. Inevitably there are differences between public services in different service sectors or at different points of the public service delivery chain. Whilst we would argue that the principles of sustainability identified here are germane to all PSOs and public services, their actuality and import will vary. The contingencies of such variation need to be identified and explored to deepen our understanding of truly sustainable public services.

Finally, in addressing the practical challenges of making a reality of public-service-dominant sustainability it is not necessary to reinvent the wheel. Key knowledge does exist on such topics as working with stakeholders across public service systems (Bryson, 2004; Crosby and Bryson, 2005), externally focused strategic planning and management for PSOs (Stone, 2010), inter-organizational network governance (Klijn and Koppenjan, 2000), and risk governance for public services (Brown and Osborne, 2013). This knowledge needs to be harnessed to underpin an effective approach to a public-service-dominant sustainable business model for PSOs and public services for both practice and academia. Research attention can then be focused upon the under-researched and under-theorized topics identified above. This is an essential task for the development of public management theory that is fit for purpose in the twenty-first century.

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