



Update on Public Service workforce forecasts

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| | Actions Sought | Due Date |
|--|---|------------------|
| Hon Chris Hipkins, Minister for the Public Service | Refer this paper to the Minister of Finance | 15 December 2022 |

Enclosure: Yes/No

Executive Summary

- 1 This report updates you on latest estimates for the size of the Public Service in terms of both FTE and contractor and consultant spend.
- 2 In August, agencies provided us with forecasts that indicated FTE growth of 4.7% for 2022/23. This is consistent with projected workforce investment of approximately 2900 FTE from Budget 22. However, from June 2022 to September 2022 the Public Service workforce has grown 0.3%. This is significantly below the forecast workforce growth.
- 3 If Public Service workforce growth for 2022/23 does not occur, this may impact on delivery of Government priorities, and may result in an increased reliance on contractors and consultants.
- 4 At the same time, contractor and consultant operating expenditure for 22/23 was previously forecast by agencies to drop around 15% or \$140 million compared to 2021/22. Quarter 1 spend indicates that this forecast decrease may not be achieved. If spending at 2022 September levels continues, we project that operating expenditure could be closer to \$890 million in financial year 2022/23 (compared to \$927 million in 21/22).
- 5 We expect the tight labour market to also impact pay. Over the first quarter the average Public Service salary increased 2.3 percent to \$92,900. We anticipate annual wage growth to 30 June 2023 will be significantly higher than 2.3 percent if increases result from the Public Sector Pay Adjustment process occur.
- 6 The next iteration of this survey will ask agencies for updated FTE numbers as at 31 December 2022, and for a refined workforce forecast for 30 June 2023. Data will be received in early February 2023, and we will provide you with an update at the next available meeting of MOGGSER following this.
- 7 As with any forecasts, changing circumstances and decisions may affect the accuracy of estimates in this paper. In particular, these forecasts are expected to be affected by decisions made by Ministers as part of the Budget 23 process, including initiatives which would require additional staffing, the impact of the Public Service Pay Adjustment on budget reallocation within existing baselines, and any reprioritisation of initiatives across agencies and the Public Service.
- 8 The Treasury have also been scrutinising the underspends and expense transfers, including from the Covid Relief and Recovery Fund where underspends have been returned through the October Baseline Update process.

Recommended Action

We recommend that you:

- a **note** that workforce growth between June and September 2022 has been 0.3%, substantially below agencies' forecast growth
- b **note** that agencies have forecast around \$785 million in contractor and consultant spending, a drop of around 15% compared to 2021/22
- c **note** that results from Quarter 1 of 2022/23 indicate that operating expenditure on contractors and consultants is likely to be closer to \$890 million

- d **note** that as at 30 September 2022 the average salary in the Public Service is \$92,900, an increase of 2.3% since June, but we anticipate that wage growth for the 2022/23 financial year will be significantly above this rate
- e **note** that we are working with Treasury to manage the risks associated with changes to workforce numbers and spending on contractors and consultants, in particular we will:
- i. continue to survey agencies on workforce matters, including workforce size and forecasts, pay, recruitment, and retention, and expect to provide our next update to MOGGSER Ministers in February 2023
 - ii. continue to work with Treasury to improve wage and workforce data quality in Budget 23, allowing Ministers to make more informed decisions
- as part of the Budget 23 process, update Ministers and agencies on work to tighten the use of departmental underspends in future financial years, to help ensure that priorities are reviewed so that a tight-labour market in one year does not translate into significant workforce growth when that market
- f **refer** this paper to the Minister of Finance
- Refer/not referred.*
- g **agree** that Te Kawa Mataaho release this briefing in full once it has been considered by you.
- Agree/disagree*

Hon Chris Hipkins
Minister for the Public Service

Te Kawa Mataaho Report: Update on forecast Public Service workforce and associated risks

Purpose of Report

- 9 This report outlines current forecast and first quarter reporting of the public service workforce. The paper also updates Ministers on active work with, and by, Treasury to return CRRF money to the Crown, address the carry-over of workforce related underspends, and provide Ministers with better information about workforce implications through the Budget 23 process.

Background

- 10 In March this year we provided MOGSSER with our assessment of the trends that have affected public service workforce growth since 2017. These trends include population growth, increased investment in frontline services and (more recently) the response to Covid 19 (2022/0038 refers).
- 11 At the request of the Minister for the Public Service and Minister of Finance, the Commission is closely tracking further changes to the size and shape of the Public Service, providing indicative forecasts of future changes and working with the Treasury to better inform Government budget decisions.
- 12 In June this year, we provided those Ministers with a report on the outcome of Budget 22 (2022/0130 refers). That report set out the estimated increase in Public Service numbers for 2022/23 (2,900 FTE for departments and departmental agencies) and provided advice on potential levers to manage growth in the Public Service.
- 13 As at 30 June 2022:
- i. The Public Service workforce was 60,381 FTE
 - ii. The average Public Service salary was \$90,800
 - iii. Contractor spend was \$1,244.8 million, with operating expenditure representing 14.6% of total workforce spend.

Analysis

Update on workforce numbers

Agencies provided an initial forecast of workforce numbers by June 2023, indicating an increase of 2,800 FTE

- 14 In August 2022 agencies were asked to provide a forecast of their expected workforce as at 30 June 2023 accounting for their ongoing work programme, and new initiatives funded through Budget 2022. This forecast, if realised, would result in an annual increase in the Public Service workforce of approximately 2,800 FTE, or 4.7% compared to 30 June 2022.
- 15 An increase at this level would be similar to the 2,900 FTE growth supported by Ministers through Budget 2022, which was noted in the June paper.
- 16 Appendix A – Public Service Workforce Composition provides a breakdown of this forecast, by agency.
- 17 The Public Service experienced limited growth in the July 2022 to September 2022 quarter. It has grown by 174 FTE, (0.3%) compared to 30 June 2022.

The Public Service experienced limited growth in the first quarter of 2022/23

- 18 In October 2022 we asked agencies to provide an update on the number of FTE actually employed as at September 2022.
- 19 The Public Service has grown by 174 FTE, (0.3%) compared to 30 June 2022.

- 20 Figure 1 shows Public Service workforce size and growth over the last 5 years, updated for workforce growth at September 2022, and incorporating the forecast growth for June 2023, as estimated by agencies.

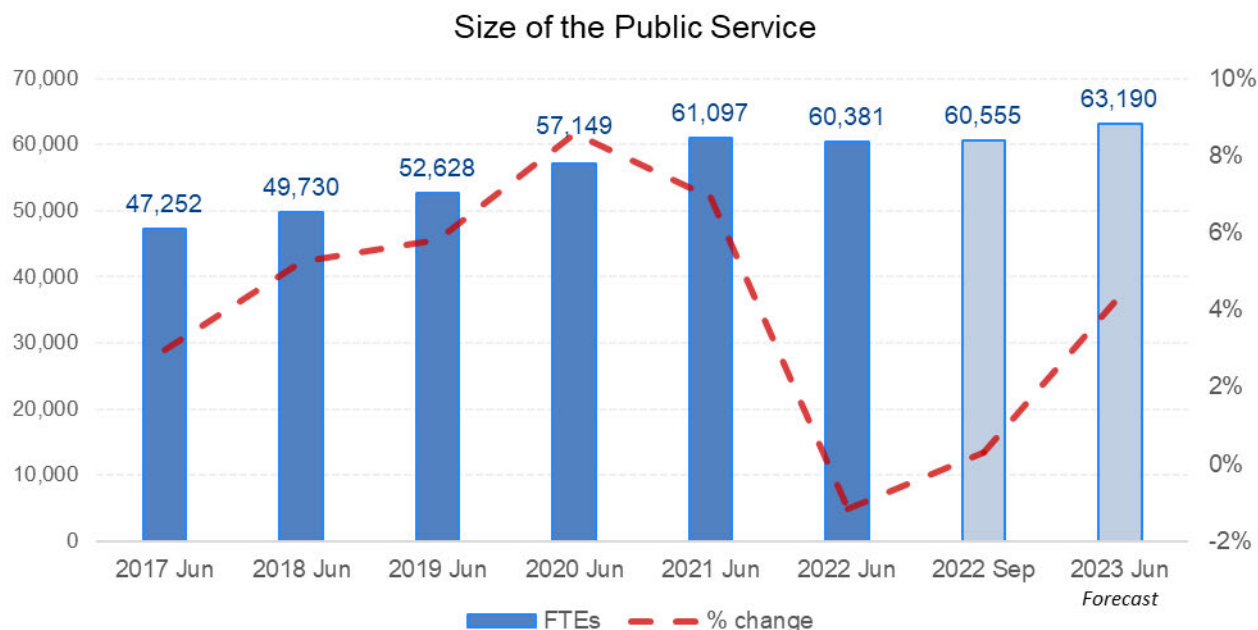


Figure 1: Public Service workforce growth, 2017 to 2022, including agency-provided updates on FTE as at September 2022, and projected growth to June 2023.

Agencies are unlikely to meet forecast workforce growth, given continued recruitment and retention pressures

- 21 In the face of continued tight labour market conditions, we consider it likely that the agency forecast overestimates the number of public servants who will be in place by June 2023. Actual growth as of September 2022 is tracking significantly below agency forecast growth for the 2022/23 year, including for a number of agencies which were forecasting growth, but which have declined in size over the last 3 months.
- 22 At current rates of workforce growth, most agencies will not grow in line with the forecast. We note that:
- i. assuming constant quarterly growth/decline, only 6 agencies will have close to the number of FTE at 30 June 2023 they estimate in the initial forecast.
 - ii. 8 agencies have indicated they expect to grow during the 2022/23 financial year but have declined in workforce between June and September 2022. Conversely, 2 agencies have indicated they expect to decline this financial year, but have, so far, experienced workforce growth.
- 23 When surveyed in August 2022 29 of 37 agencies indicated “severe” difficulty in recruiting for at least one occupational group, most typically ICT Professionals, or Policy and Other Advisors. We consider it likely that such difficulties will persist, meaning recruitment may prove more challenging than agencies anticipate.
- 24 Almost all agencies report higher rates of turnover now than in recent years. Quarterly unplanned turnover for July 2022 to September 2022 is approximately 4.3% for the Public Service, with most agencies reporting between 3.0% and 6.0% quarterly unplanned turnover.

- 25 Agencies have previously overestimated their workforce size in forecasts. Following a survey in May 2022, we briefed you on forecast Public Service workforce growth of approximately 0.5% between 2021 and 2022. However, the workforce declined by 1.2%.

As a result, agencies may struggle to deliver Government priorities or may turn to contractors and consultants

- 26 The apparent discrepancy between the forecast provided by agencies and actual FTE growth as of September 2022, combined with ongoing tight labour market conditions and high turnover, suggests that agencies looking for significant increases in FTE may find it challenging to deliver on relevant Government priorities. Alternatively, they may turn to contractors and consultants to deliver their work programmes.

Update on Contractor and Consultant expenditure

- 27 Figure 2 shows Public Service contractor and consultant spend over the last 5 years, updated for contractor and consultant spend at September 2022, and agencies' forecast spend for June 2023.
- Spending on contractors and consultants increased significantly in 2021/22 with operational expenditure up 52% from \$609.6 million in 2020/21 to \$926.9 million.
 - Agencies forecast that operating expenditure will reduce by 15%, to around \$785 million, in 2022/23
 - We project operating expenditure is more likely to be around \$890 million based on current spending on contractors and consultants for the first quarter of 2022/23.**

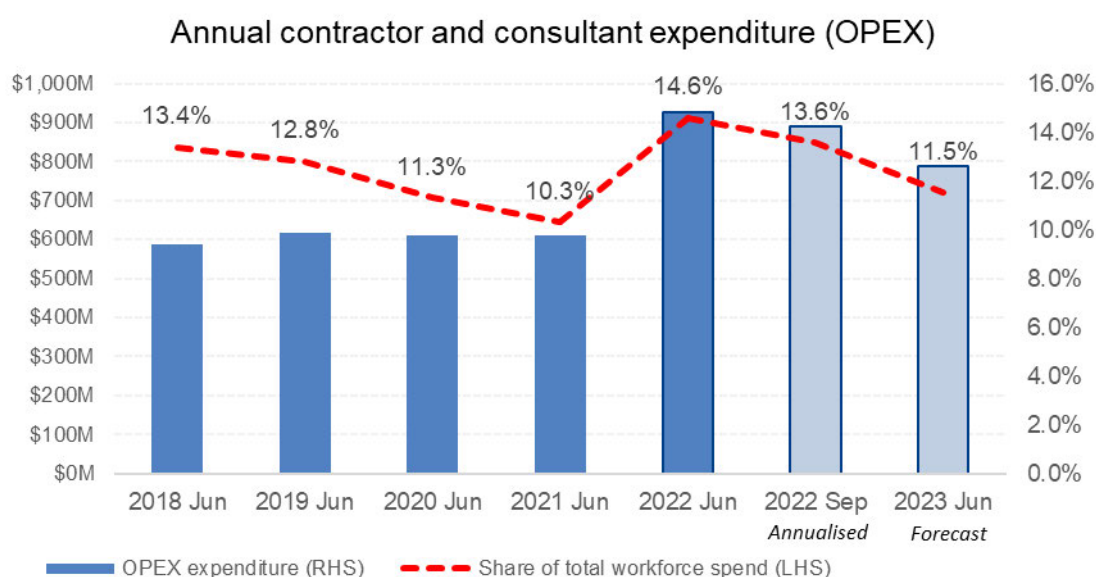


Figure 2: Public Service contractor and consultant spend, 2018 to 2022, including agency-provided updates as at September 2022, and projected spend for financial year 2022/23.

Spending on contractors and consultants increased significantly in 2021/22

- 28 In 2021/22, Public Service organisations spent a total of \$1,244.8 million on contractors and consultants. Total expenditure comprises operational expenditure of \$926.9 million (up 52% from \$609.6 million in 2020/21) and capital expenditure of \$317.9 million (down 4.1% from \$331.5 million in 2020/21).

- 29 Total spending in 2021/22 represents an increase of 32% on the 2020/21 spend of \$941.1million, with the increase mainly driven by:
- i. COVID-19, including the national vaccination rollout
 - ii. Government priorities, especially big reform work programmes such as the recent health reforms, the RMA reforms and Three Waters
 - iii. One-off IT improvement projects and upgrading systems for online access to government services, and migrating legacy systems to cloud-based, which are more secure, resilient and cost efficient in the long-term.
- 30 Other factors contributing to this year's expenditure include restarting projects that were put on hold during the pandemic and tight labour market conditions, with the country's borders not fully opening until the middle of this year.
- 31 Operating expenditure on contractors and consultants was 14.6% of total Public Service workforce spend (\$6,328.8 million), an increase from 10.4% in 2020/21, 11.3% in 2019/20, 12.8% in 2018/19 and 13.4% in 2017/18.

Agencies provided an early forecast of contractor and consultant spend for 2022/23

- 32 We asked agencies to provide a forecast of their estimated spend on contractors and consultants for the 2022/23 financial year.
- 33 Collectively, agencies project they will spend a total of around \$1,190 million on contractors and consultants for the 2022/23 financial year. Of this, operating expenditure is estimated to total around \$785 million (representing a drop of 15% or \$140 million compared to 2021/22) and capital expenditure is estimated to total around \$405 million (representing an increase of around 27% or \$87 million compared to 2021/22).

Agencies' forecast decrease to contractor and consultant spending may not happen

- 34 To help track spending, the Commission collects quarterly updates on contractor and consultant spending from all agencies. This year we have compared this to agency forecasts.
- 35 Results from Quarter 1 of 2022/23 indicate that the decrease to contractors and consultant spending projected by agencies may not happen.
- 36 If spending at Quarter 1 levels continue, the projected spending illustrated in figure 2 will be exceeded.
- 37 We estimate that operating expenditure will be around \$105 million above forecast, for a total spend closer to \$890 million in financial year 2022/23. While this would be a decrease on this year's operating expenditure of \$926.9 million, it would still be notably higher than the period from 2018 – 2021.

Update on Public Service salaries

Public Service salaries increased by 2.3% to September 2022, but wage growth to June 2023 is likely to be significantly higher

- 38 The average salary in the Public Service, as at 30 June 2022 was \$90,800. This figure is now out of date due to increases to salaries (progression, and other negotiated/provide increases) which occur from 1 July annually.
- 39 To monitor this change, we have surveyed agencies on average salaries, the number of staff earning below the 2022 Living Wage, and the number of staff earning above \$100,000.

- 40 As at 30 September 2022:
- i. the average salary in the Public Service is \$92,900, an increase of 2.3% since June.
 - ii. fewer than 85 FTE public servants earning below the current Living Wage, of \$23.65 per hour.
 - iii. one third percent of public servants (33.4%) earn above \$100,000 per annum, up from 31.3% in June. We expect a slow increase to this proportion given some staff receive progression or promotions across the \$100,000 threshold.
- 41 We anticipate that wage growth for the 2022/23 financial year will be significantly above 2.3% for two reasons:
- i. wages will increase further because of increases from new collective agreement settlements, including those which give effect to the Public Sector Pay Adjustment. The increases we have seen currently largely reflect increases in previously settled agreements.
 - ii. compositional changes, such as staff moving into new roles also affect the Public Service average salary. If current labour market and economic conditions, including inflation (as measured by the CPI) and wage growth (as measured by the LCI) continue to drive turnover and salary expectations for those moving into new roles we can expect new staff to be employed on higher salaries, which will increase the average salary.
- 42 We note that without commensurate increases to baselines, reprioritisation, or efficiencies gained, increases to average salaries may restrict the ability for agencies to invest in new personnel.
- 43 The next iteration of this survey will ask agencies for updated FTE numbers as at 31 December 2022, and for a refined workforce forecast for 30 June 2023. Data will be received in early February 2023, and we will provide you with an update at the next available meeting of MOGGSER following this.

Update on workforce management

We are continuing to monitor and improve how we manage risks

- 44 There are risks associated with significant ongoing growth in Public Service numbers. In our reports of March and June, we noted that:
- i. ongoing growth will need to be explained by reference to service or legislative programme delivery, requiring agencies to be more fine-grained in their analysis and reporting regarding workforce recruitment and deployment
 - ii. existing workforce pressures may create ongoing challenges in employing the right people
 - iii. the perception that the Public Service is out of step, or competing, with the broader New Zealand labour market, may negatively affect public trust and confidence.
- 45 There are also risks if the Public Service does not grow in line with agency estimates of the FTE required to deliver Government programmes and other services. We have noted these, above, in particular that such a situation may negatively affect agencies' ability to deliver Government programmes, or increase spending on contractors and consultants. It may also contribute to wage pressures.
- 46 Based on the information outlined in this briefing, we currently consider it likely that the Public Service will not grow at the rate estimated by agencies, and contractor and consultant spending will exceed initial estimates and Public Service wage increases will exceed 2.3%.

We are increasing the frequency of our data, and improving the information we gain from it with our next quarterly workforce survey scheduled for December 2022

- 47 We will continue to survey agencies on workforce matters, including workforce size and forecasts, pay, recruitment, and retention.
- 48 The next iteration of the survey will ask agencies for updated FTE numbers as at 31 December 2022, and for a refined workforce forecast for 30 June 2023. Data will be received in early February 2023. We will provide you with an update at the next available meeting of MOGGSER following this.
- 49 Further collections are scheduled for April 2023 for data and context as at 31 March 2023, and July 2023 for contextual information to support the Commission's regular annual workforce survey.
- 50 The data we collect supports our commitment to provide Ministers with more regular updates on measures of the Public Service workforce. It also strengthens our ongoing work with Treasury aimed at better supporting informed decisions to manage workforce numbers, especially during the upcoming Budget.

Treasury and the Commission are working to improve workforce data for Budget 23

- 51 The Budget process represents the most obvious, and best, opportunity for Ministers to make decisions that will influence the future size and composition of the Public Service.
- 52 In the context of a tight labour market, for example, funding initiatives that require additional staff may result in agencies turning to contractors or consultants or affect delivery of other initiatives.
- 53 The Budget 22 process required agencies to specify:
 - i. the total workforce required under their bid
 - ii. the breakdown between fixed-term and permanent staff, and contractors and consultants
 - iii. the general occupations of the required workforce (for example, whether they are managers, policy analysts, IT workers and so on).
- 54 Similar requirements will be in place for Budget 23. Treasury and the Commission are working together to improve wage and workforce data quality in Budget 23. This will be achieved by:
 - i. improving the wording of questions
 - ii. promoting consistent definitions and wage inflation assumptions across agencies
 - iii. asking additional questions about total personnel numbers and costs, and current vacancies.
- 55 The information gathered from agencies during the Budget 23 process will provide Ministers with more of the information they need to make informed decisions about the likely effects on workforce numbers of the decisions they make.
- 56 The information collected will also support the Commission's efforts to better forecast future workforce numbers, as we did in our June report following Budget 22 decisions.

Agencies have returned CRRF underspends through the October Baseline Update allowing for greater prioritisation of initiatives

- 57 In the June paper we noted that agencies may be better placed to manage apparent shortfalls in the FTE numbers they estimate are required to deliver Government programmes if initiatives are prioritised. This may be done, for example, through the active management of fixed term funding.
- 58 With respect to prioritisation of initiatives, MOGSSER Ministers have previously been briefed on, and engaged in, the process to review spending under the COVID-19 Response and Recovery Fund (CRRF). Under this process, several agencies that received CRRF funding are being asked to relinquish that funding. In this way, funding, and associated workforce, can be prioritised elsewhere across the Public Service.
- 59 Since the last MOGSSER meeting in June, Treasury has been scrutinising the underspends and expense transfers, including from the CRRF where \$1.2 billion of CRRF underspends in 2022/23 and outyears have been returned to the centre through the October Baseline Update process. Underspends carried forward come with additional resources requirements which may not be incorporated within forecasts and will place additional pressure on an already tight labour market.
- 60 Where underspends have been carried forward they are allocated to existing Government priorities. Ministers may choose to reprioritise underspends and existing baseline funding in Budget 2023 to support deliver of Government priorities. This could include looking at vacancies across the public sector to reprioritise funding for vacant roles to assist with remuneration pressures.
- 61 Given fiscal and delivery constraints, the tight labour market, and wage inflation pressures, this approach could help generate more fiscal headroom for wage inflation pressures, increasing the deliverability of remaining vacant roles in a tight labour market. The Commission and Treasury will work to provide agencies and Ministers further direction on this approach for Budget 2023 in coming months.

Risks

- 62 This briefing provides a forecast of workforce growth, spending on contractors and consultants and Public Service wage growth. As with any forecasts, changing circumstances and decisions may affect their accuracy. In particular, the forecasts in this paper are expected to be affected by decisions made by Ministers as part of the Budget 23 process, including initiatives which would require additional staffing, the impact of the Public Service Pay Adjustment on agency budgets, including Budget 23 cost pressure envelopes and reallocation within existing baselines, and any reprioritisation of initiatives across agencies and the Public Service.
- 63 We are working to mitigate this risk by providing more frequent information as it becomes available

Next Steps

- 64 The Commission and Treasury will continue to work together to improve the Budget 23 process and will provide further information to Ministers on this approach as it develops.
- 65 We will update MOGSSER Ministers on updated forecast FTE numbers at the next available meeting of MOGSSER Ministers once data is received in early February 2023.

Workforce growth slowed in 2021/22...

- The Public Service workforce decreased by 715 FTEs (or -1.2%) in 2022. The largest reason for change related to the Health Reforms - Ministry of Health had 769 fewer FTEs primarily due to functions moving to the new health entities outside the Public Service. Without these changes, annual growth between 2021 and 22 would have been around 0.3%.
- This is slower than the recent growth in the Public Service workforce. Contributing to this slowdown was the end of time-related projects, such as COVID, and tight labour market conditions which have made it more difficult for agencies to recruit.

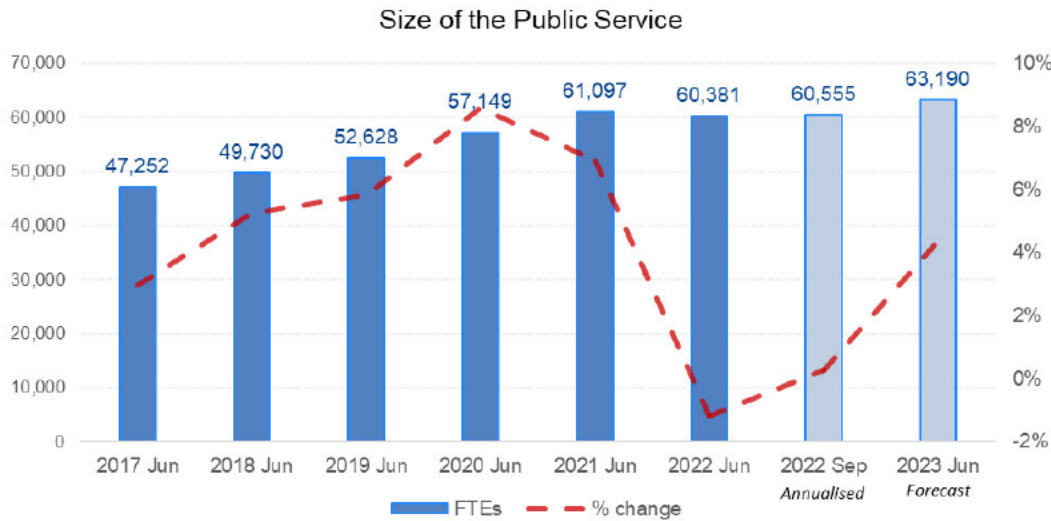
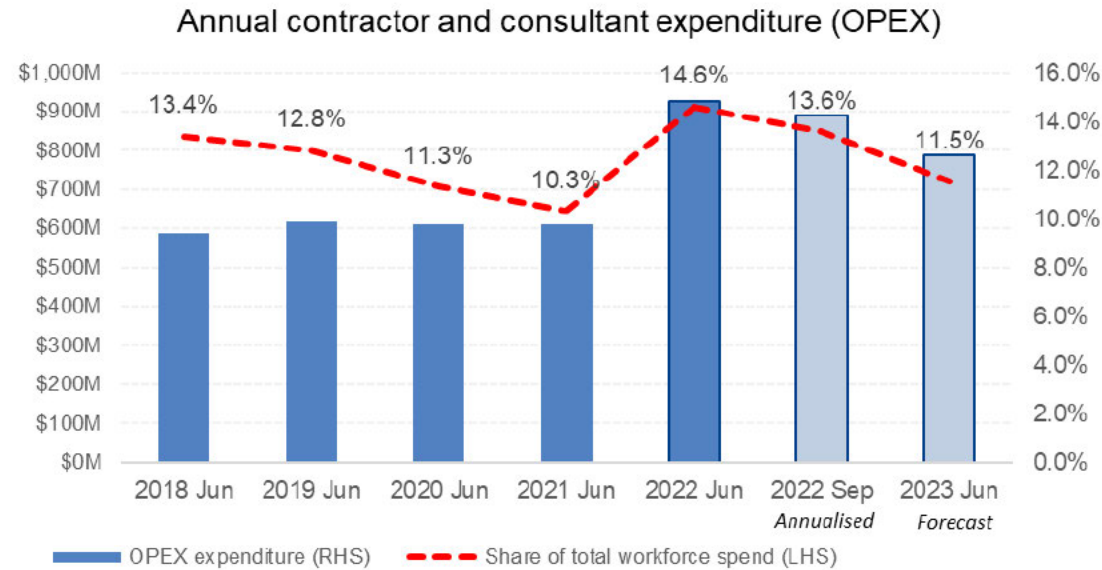
...and total expenditure on contractors and consultants increased 32%.

- This was primarily due to Covid 19 spending including the vaccine rollout, Government priorities such as water, RMA and health reform, and a larger number of one-off projects requiring specialist resource such as IT migration to cloud services.

FTEs have been forecast to increase in 2022/23

- In August, agencies forecast growth of 4.7%, an annual increase in the Public Service workforce of approximately 2,800 FTE for 2022/23.
- This is consistent with projected workforce investment of approximately 2,900 FTE from Budget 22

...while, contractor and consultant expenditure was forecast to drop 15% compared to 2021/22



However, first quarter results indicate forecasts for 22/23 may need to be adjusted

First quarter FTE growth is below expected forecast for 2022/23

- Agencies had 60,555 FTEs at 30 September 2022, a quarterly increase of 174 FTE (or 0.3%). Some agencies that had FTEs fall 2021/22 due to recruitment difficulties, such as Department of Corrections and Oranga Tamariki, continued to decrease in size in the September quarter.
- The forecast 2,800 increase, would require a 4.3% increase in the next 3 quarters. This is nearly 5 times the September growth rate. If tight labour market conditions continue, FTEs are likely to be below forecast.

Contractor and consultant spending is likely to be higher than forecast, and could be only slightly below 2021/22

- The 2021/22 increase in contractor and consultant expenditure was due to one-off projects, and spending has started to fall in September.
- Some of the 2021/22 increase was also due to recruitment difficulties. If these continue, the forecast decreases in spending for 2022/23 may not be achieved.
- Figures received from quarter 1 suggest operating expenditure will be above forecast, though will still be a decrease from 2021/22

Public Service workforce growth had been alongside unprecedented population growth, but no longer

- After record increases from 2014-19, annual population growth has reduced from 2.2% pre-COVID to 0.4% currently
- Latest Stats NZ population estimates show small pick-up in population growth but still well below pre-COVID period.

