WHEN DOWNSIZING FAILS

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ABSTRACT

According to a 1995 survey by the AMA, more than 47 percent of the companies surveyed reported that workforce reductions were up almost 36 percent since 1990. The AMA research also shows that in companies that do downsize, profit improved in less than 50 percent of the companies and productivity improved in only 36 percent of the companies. What is the cause for the shortfall in meeting expectations? This paper examines several factors that may be contributing to these overall results.

INTRODUCTION

Downsizing in corporate America seems to be a way of life. According to a 1995 survey by the American Management Association (AMA), more than 47 percent of the companies surveyed reported that workforce reductions were up almost 36 percent since 1990 [Banham, 1995]. The reasons reported for the downsizing are typically savings in costs and improvements in productivity, leading to greater profits and higher shareholder return [Arnold & Pulich, 2003; Fagiano, 1996]. However, downsizing may not always be delivering the planned increases in profit or productivity.

As companies have executed the downsizing or restructuring efforts, they often focus on the immediate change and not on the on-going impacts on the individual employees or the organization in general [Nelson, 1997; Gustafson, 1996]. Many companies have not accounted or planned for the employee insecurities or anxieties caused by the departures of friends, managers, or direct reports. The employees are subject to what Bunker [1995] refers to as the 'layoff-survivor syndrome'. They are liable to suffer from a variety of emotions and illnesses, leading to increased absences, and increased turnover [Stoner & Hartman, 1997; Bunker, 1995; Clark & Koontz, 1995]. This change in employee behavior can also have detrimental impact on the organization. However, there are steps companies can take to minimize the negative effects of downsizing.

A brief literature review of the reasons companies choose to downsize, and the results they achieve is offered below. Also, the impact of downsizing on employees and organizations will be offered. Some of the mitigating steps a company can take to reduce the negative impact of downsizing are also offered. Finally, suggestions on future research in this area are presented.

LITERATURE REVIEW

Companies choose to downsize for several different reasons. First, there are economic factors that companies list as primary contributors to the downsizing effort. Companies may use the strategy of downsizing to boost profits, by reducing head count or restructuring the organization [Rayburn & Rayburn, 1998]. As Fagiano [1996] points out, some companies react to the expectation of building shareholder value, using downsizing as a method to improve earnings. However, as reported in "The Year of Living Cautiously" [2001], less than 25% of the company officials responding to a survey indicated that the head count reductions in their company were due to economic reasons. It was further reported that more than one third of the responding managers said their company's financial position was good, but that they had taken or were planning reductions to maintain or continue to improve company growth. This attitude toward change as a strategy to improve growth and earnings seems to be growing, and may have additional impact on employees and organizations [Rayburn, 1998; Banham, 1995].

Another reason companies downsize, in addition to saving money or boosting profits, is the technological developments that allow manufacturing companies to operate with less people. There is competitive pressure to stay current with new processes, which causes cost reductions in other areas of the business, resulting in additional downsizing in a vicious cycle [Rayburn, 1998]. This technological race does not, however, seem to be producing long-term improvements to productivity.

<u>How are the results?</u>

Wager [2001] states that the results do not match the expectations companies have about downsizing, and most companies are not realizing the planned benefits. Fagiano [1996] supports Wager's

claims with AMA research that showed productivity increased in less than 37 percent and profit improved in less than 50 percent of downsized companies. The study also showed that of the firms who downsized, more than half downsized again, some as soon as the following year [Nelson, 1997].

Fagiano [1996] also states that the focus on shareholder value seems to be detracting from the more important goal of building market share. Downsizing companies that are focused on cost reduction instead of market growth will lose market share, unless they can find a way to reduce costs at a faster rate than the competition, and even that may not be sustainable [Hyde, 2003].

Additionally, Banham [1995] compared the performance of companies that downsized with companies who did not. He found that companies who did not downsize were able to exceed the performance of others companies in the same industry, while companies that downsized either maintained or declined in their overall performance.

However, the process of downsizing really may not be the problem. One issue may be the lack of planning, training and communications about the changes that occur prior to the downsizing, including how the "new" company is going to perform work with less people and no new processes or systems [Nelson, 1997]. This issue will be addressed later in the paper. Another issue may be the low morale of the employees who remain with the company after the downsizing or restructuring is complete.

How is Life for the Surviving Employees?

The surviving employees and managers still have to deliver the company's goals and objectives. However, the workers who are left behind may no longer be motivated to do their work well, if at all [Kaye, 1998]. These surviving workers have to take on additional duties and tasks, often without the training necessary to successfully complete the work [Amundson, Borgen, Jordan, & Erlebach, 2004; Nelson, 1997]. The surviving employees may also feel badly about others losing their jobs, and have mixed feelings about keeping their own jobs.

These employees may be relieved to still have a job, but no longer think of the job as a long-term arrangement. Rather, they may think of the company as a place to obtain only a check. They may also be afraid that when the company goes through another downsizing, they may be the next to go [Stoner & Hartman, 1997; Emshoff, 1994].

In year's past, employees had an unspoken contract with their employers, with the employee believing they would remain employed, as long as they performed at or above expectations. However, with the changes that have occurred as a result of sweeping organizational changes, that emotional bond with the company is often broken [Stoner, 1997]. Rayburn and Rayburn [1998] also agree that employees can become demoralized, and start to question the company's loyalties toward them. This lack of perceived loyalty may reduce the competitive edge that businesses in America realize over their global competitors [Rayburn, 1998; Kaye, 1995].

What Can Be Done?

If the expected benefits are not being realized, employees and managers may be frustrated with the downsized organization. One has to wonder, then, what can be done to overcome these issues? Two things missing from many of these articles on the subject are the need for increased training and clear communications.

The employees need training to build skills on the work to be accomplished. Working smarter, not harder is a popular aphorism, but it can be insulting to workers. Clark and Koonce [1995] have ideas about the importance of the employee needing to fit into the new organization; so as to reduce or eliminate the feelings of insecurity and anxiety about the changing organization.

When developing a newer 'leaner' organization, with fewer employees doing the same work, it is important to redefine roles and responsibilities, and develop training programs to equip the employees with the necessary skills [Amundson, 2004; Arnold & Pulich, 2003; Clark & Koonce, 1995]. According to Gustafson [1996], an AMA study demonstrated that companies that increased their funds for training during and after downsizing showed an increase of 68 percent in profits and 44 percent in productivity. By comparison, companies that did not increase the funds for training during and after downsizing, showed only a 42 percent increase in profits and a 29 percent increase in productivity [Gustafson, 1996].

With a reduced work force, the work can be redefined to better meet the needs of the organization, and the workers can be better matched to the work needed. One way of achieving the new responsibilities is by cross-training the employees to build new skills, and to improve the productivity of the workforce, even during vacations or layoffs [Pulich, 2003; Messmer, 1992]. Cross-training can

also build the confidence of the workers. They can feel more integrated into the company, and more valued, as a result of the additional skills and knowledge [Pulich, 2003]. Employees must be willing to make the additional commitment to learning the new work, and managers must be able and willing to identify those opportunities where cross-training is appropriate and identify at what time in the process or system the training must occur [Messmer, 1992; Arnold, 2003].

Training of the managers is also needed to streamline the work and deal with the accompanying organizational changes, especially as the number of people is reduced. According Clark and Koonce [1995], managers need to build new skills that may not previously have been required, such as how to build teams and earn employee loyalty without the implied contract referred to by Stoner and Hartman [1997]. Managers also need to develop their organizational effectiveness skills in order to improve employee participation and satisfaction. Finally, they need to improve their communications skills to better identify goals and objectives, while including (or at least listening to) employee inputs [Clark & Koonce, 1995].

There also needs to be training for the HR organization, including work in organizational effectiveness, organizational development, and in training & development departments. Organizational change will only work if the change is supported by changes in the culture that each employee embraces, with clear measures for success included [Arnold, 2003].

Clear and Frequent Communications Needed!

In addition to training, the company needs to provide clear communications to employees; showing that the new organization was developed with a sense of fairness for the workers, with order in the work, and logics in the decisions [Thornhill, Saunders & Stead, 1997]. The communications should start early in the planning for the downsizing, and continue through and even after the changes have been completed [Nelson, 1997].

Improved communications can help build employee confidence and trust in the company, and more specifically in management. Employees will feel that management is concerned about them, when information is shared about the process and changes occurring [Amundson, 2004; Thornhill, Saunders, & Stead, 1997; Nelson, 1997]. Additionally, employees will feel less threatened by the changes, and the fears of job loss will be reduced [Amundson, 2004]. By building open and clear communication channels, employees will become more committed to the work and the company in general [Nelson, 1997].

SUMMARY AND RECOMMENDATIONS FOR ADDITIONAL RESEARCH

Although downsizing in corporate America has become a way of life, the execution needs much work. Throughout this paper, it has been shown that companies downsize for financial, technological and organizational reasons, but often fall short on reaching the expectations set as part of the downsizing strategy [Wager, 2001; Rayburn, 1998; Fagiano, 1996; Banham, 1995]. It is not downsizing that will increase productivity or improve profits. It is the employees of the company who will drive the success or failure of the company, and so the downsized companies must develop the strategies to take into account the impacted employees [Rayburn, 1998].

The employees in an organization represent the basis for a company's achievements, and the company should build plans to enroll the employees in the process and improve employee satisfaction along the way. It is the individual employee who produces the products and services, and who represents the company to its customers [Lewin & Johnston, 2000]. Therefore, in order to maintain a sense of loyalty to the company, more effort needs to be dedicated to developing communication plans with the employee in mind. The communications should start early in the process and continue even after the downsizing is complete [Nelson, 1997]. In addition to strong communications plans, the company needs to provide the employees with the training to accomplish their work.

The company can encourage more loyalty, better productivity, more job satisfaction, and better quality by providing the employees with proper training [Amundson, 2004; Arnold & Pulich, 2003; Gustafson, 1996; Clark & Koonce, 1995]. In addition, by building the skills of the employees, they can feel empowered to participate in the development of the company, and potentially in the next downsizing, should it occur [Amundson, 2004].

Since the validity of downsizing as a profitable strategy is still in question, additional work should be done to understand the successes and failures of these efforts. In the AMA survey previously discussed, companies that had downsized, saw profitability was up almost 50% of the time and productivity was up less than 36% of the time

[Fagiano, 1996]. While those numbers are not glowing endorsements for downsizing, they do show that there are companies that can manage their way through the downsizing and come out ahead.

The literature points out the need for planning, training and communications in such situations. Additional research could review the companies that have downsized more recently, compare their results versus their original expectations, and hopefully determine if and when downsizing is an appropriate strategy for businesses [Davis, Savage, & Stewart, 2003]. Clearly, more research needs to be conducted in this area that seems to be affecting organizations and individuals in such great numbers. The present review is a beginning effort toward this goal.

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