CAMBRIA
Consulting ▪ Coaching ▪ Assessment ▪ Interactive

Smart Downsizing: Reducing Costs while Increasing Competitiveness

Bernard J. Cullen and George O. Klemp

How to downsize in a performance-based, fair, and efficient way that also helps retain top talent for the future.

Introduction

The realities of the global economic crisis today, declining profitability, increased domestic and international competition, continued outsourcing to reduce costs, and reorganization to improve efficiency have led to dramatic reductions in the workforce at many companies. Whether one calls it "downsizing" or "rightsizing" (or, less euphemistically, "layoffs"), the harsh reality is that many companies today find themselves forced to consider significant reductions in people to compete and survive. The dilemma in doing so is how to recoup the investment in people for the long term despite short-term pressure to reduce costs, and not cut into muscle while trimming the fat.

Many of the approaches used to downsize have shown themselves to be less than effective. Offering generous severance packages as an incentive to leave voluntarily often results in the loss of many of the most experienced and talented people. Mandating businesses to cut a certain percent of employees across the board is an overly simplistic approach to a complex issue. The "last in, first out" approach, while supposedly fair, fails to take the need for critical skills into account. Waiting for natural attrition and not filling positions as people leave only works when turnover is normally high and is generally not applicable to professional or management employees. In addition, changing an employee's status to subcontractor is often just a way to move salary expenses off the balance sheet, not to mention being potentially illegal.

Despite the popularity of downsizing as a short-term cost-reduction tactic, research has shown that the long-term impacts, overall, are "decidedly negative" (Chadwick, Hunter & Wilson, 2004), including disappointing financial returns (Cascio, 2002), lowered commitment among the workers that remain (Davy, Kinicki & Scheck, 1991), and reduction in corporate productivity over time (Cappelli, 2000). Despite these outcomes, other researchers suggest that cutting jobs demonstrates that management is "in charge," often resulting in a bump in stock price, and has become almost institutionalized as a response to tough conditions (Wilkinson, 2004). Although Chadwick et al. state that downsizing is more likely to be effective in the longer term when accompanied by ongoing and extensive communication, respectful treatment of the displaced redundant employees, and attention paid to the survivors, the case for downsizing is mixed at best.

A number of organizations have also considered alternatives to downsizing. An oft-quoted article in *Workforce* magazine (Maurer, 1999) claimed that "many companies that downsize end up with less productivity or less revenue than when they started." It went on to describe thirteen alternatives, including retraining, redeployment within the organization, reduced hours, lower wages, and leaves of absence with full benefits. However, these approaches do not address the underlying problem of retaining the right talent for the future while decreasing the costs associated with keeping everyone on board.

The bottom line for most organizations today is that they do not have the luxury of time, and none of the "solutions" noted above address improving performance while reducing costs. Few organizations have had the discipline to annually prune the bottom ten percent, the poorest performers, in a systematic, reality-based way, and they are among the best prepared to meet the challenges of the future by replenishing the talent pool. For others, where downsizing is not only a matter of reducing costs but also a matter of survival, it is not too late to begin a systematic, data-based process for making the right talent decisions in a timely way. This paper presents a proven and efficient method for doing so, when time is of the essence and retaining talent needed for the future is critical.

Recommended Approach

Effective management of the necessary talent requires a high-performance approach even in the best of times. Organizations that need to downsize to meet their competitive and cost challenges would do well to follow this sequence of steps:

- Candidly evaluate the overall performance of each major work unit within the organization
- Provide a clear view of emerging challenges and expectations for each of the businesses over the next 2 or 3 years
- Take immediate action on individuals and managers known to be weak or problematic performers
- Define critical competencies for today and the future, including skills, knowledge, and behavioral requirements
- Assess each person against the criteria in the competency framework, making the process as objective, transparent, and fair as possible
- Assign people to the redesigned roles in each of the targeted organizational units

Evaluate Work Unit Performance

At a macro level, it is most important that the performance of comparable teams, work groups, and organizational units be evaluated one against the other before drilling down to assess the strengths and weaknesses of the available talent. This is because it is likely that the best performers will be found in the parts of the business that are the highest performers themselves. Take a multi-dimensional view of work unit performance, considering the most important "hard" and "soft" measures, and rank comparable work units, departments, and/or functions using the most relevant and important factors: a balanced scorecard approach is one way to do this. Factors such as the following can be used as inputs to generate a profile of comparative work unit effectiveness:

- Financial Indicators (e.g., return on capital, profit, cash flow, growth in sales, market share, cost of production, cost competitiveness against alternative suppliers)
- Activities and Processes (e.g., integrity of current operating procedures, absence of duplicated activities, quality metrics, benchmarking against best practices, safety, process alignment, process automation)
- External Relationships (e.g., delivery performance, quality performance, transaction times, complaint/quality resolution, customer satisfaction, customer retention)
- Organization and Culture (e.g., low voluntary turnover of key talent, job satisfaction, presence of critical skills training, talent development for other parts of the business)

Identify Emerging Major Business Challenges

If your organization has a strategic plan in place or a multi-year vision that defines the desired future state of your organization and the critical functions and processes that will be needed, you already have much of this work done. However, you should also take the next step and ask, specifically, what people in key roles (e.g., senior leaders, managers, key professionals) will need to do differently or at a higher level of skill than previously required. Asking the very best leaders at the top of the house — people who are known for their results and for their vision — to talk specifically about the most pressing current and emerging business challenges will put more detail into the mix, and help move from high-level strategy to understanding what it will take to execute the strategy.

Remove Weak and Problem Performers

Where a robust performance management process is in place, now is the time to make the tough calls on people who are not pulling their weight and have repeatedly under-performed or who have clearly behaved in ways that are disruptive or are counter to the values of the organization. Whether done at the outset of a downsizing effort or as part of a wider cut in the workforce is more a matter of timing and how to stage the process; nevertheless, our recommendation is that this should be done quickly and before a more systematic review of all employees is undertaken. We emphasize that this step should be based on performance (dem-onstrated results), not on skills, experience, tenure, or other personal capabilities.

Define Critical Competencies

Although many organizations have some form of competency model in place, most of them are too general and nonspecific to be used for this purpose, especially when it comes to technical and business knowledge and skills. Competency models that primarily feature behaviors and personal attributes, while helpful in communicating common expectations, generally do not prioritize the competencies in terms of importance (i.e., make or break) for a given level of management or professional role.

To be as complete but focused as possible, the framework should include the following four dimensions of competence:

- Technical or business knowledge, and the level of expertise required
- Work experiences that provide the necessary foundation for effective functioning
- Personal abilities and characteristics

- Behaviors that describe how people go about their work and interact with others

When focusing the competencies to be used as an evaluation framework, consider the following:

- Which competencies are needed at a threshold level for effective functioning
- Which competencies distinguish the best performers from others
- Which competencies are readily train-able vs. which ones are innate

Audit the Talent Pool

Once the other elements are in place, this step is the most critical and the one that has to be considered most carefully and done right. The following recommended process is at the heart of "smart downsizing" — whether performed at a work unit, department, or overall business level.

1. Start from the top of the organization and cascade downward by organizational level. This is important both symbolically and pragmatically. Symbolically, the process has to be clear to the organization that no one is exempt from the process. Pragmatically, as the assessment process cascades down the organization, assess-ment of people at lower levels should only be done by managers whose ratings are good to excellent: it makes no sense to include ratings from poorly performing managers or supervisors.
2. Organize working sessions in which all evaluations are to be shared with peers. This ensures that everyone follows a consistent process and that those doing the assessing are using the same rating criteria in the same way. Making the process open and shared allows differences of opinion to be discussed and held up to the light of direct evidence. Moreover, the openness of this process dispels the image of the "smoke-filled room" where decisions are made behind closed doors.
3. Have assessors at each level rate their direct reports before the working sessions. Ratings should be done at the same time on each performance or competency dimension (e.g., relevant performance measure, technical skill, or behavioral competency).
4. Use an external facilitator for the working sessions. Each session should be managed by an individual from outside the work group, department, or organization whose role is to ensure that assessors can justify extreme ratings, that the distribution of ratings makes sense given the overall performance of the work unit, and that different assessors use the rating scales in a consistent fashion. The facilitator should also make sure that disagreements in ratings are resolved based on evidence from past performance.
5. Have managers and supervisors collec-tively review the ratings of each individual during the working session by publicly displaying them in a large matrix and prompt a "comparative" discussion of each individual. It is especially useful to have an individual recognized by all as a "star performer" or "gold standard" serve as a point of comparison for these ratings. Once ratings for an individual are discussed and any necessary adjust-ments are made, assessors move on to the next person.
6. Have managers and supervisors discuss all ratings with their own manager after attending the open rating discussions with their peers. This step serves as an additional independent check on any

tendency of managers to over- or under-rate the performance of their direct reports. It also forces them to make sure that each rating can be justified in terms of concrete examples of accomplishments or performance issues. This step is done after the working session to limit the amount of defensive behavior when the discussion indicates that changes in ratings are needed.

7. Have managers and supervisors discuss their ratings with each individual being rated after attending the assessment sessions and before any actual personnel decisions are made. In addition to the benefits listed in the fifth step, this ensures that everyone knows where he/she stands, can raise objections, and have the opportunity to suggest changes in ratings with which he/she disagrees. (Any changes in a rating, however, should be agreed to by the manager's own manager before being finalized.)

Assign People to the New Roles

Finally comes the task of matching people to new roles and responsibilities. As the first step, the evaluations from the open rating sessions and discussions should be consolidated into a skills and capabilities database designed specifically to facilitate matching of the requirements of particular jobs and roles with the skills possessed by different individuals, with qualified individuals being presented in a list.

The organization's management team should proceed with the redesign, using the organization's strategic plan, studies of existing job families and potential redundancies in functions, activity and demand analyses, and "critical skills" positions where a shortfall of talent is expected. Managers of different teams and functions should be made responsible for rethinking the design of their individual areas. In deciding on the critical job functions and the number of people needed in each, these managers used the database to identify key job requirements and then identify those individuals with the appropriate competencies.

A Case in Point

The downsizing process described above was carried out in the Information Technology (IT) division of "Key Industries," a Fortune 200 company and a major supplier of materials to the construction industry. The sharp downturn in the housing market left the company very exposed, and declining long-term profitability, increased national and international competition, and the likelihood of an extended economic downturn demanded significant action to reduce costs. In response, Key Industries initiated a corporate-wide project to reduce costs by a dramatic 50%. This is the story of how the IT division addressed this challenging goal and the results it obtained.

Background

Within Key Industries, each organizational unit, including the IT group, was expected to reassess its activities and identify which activities added real value and which could be eliminated or redesigned. Key Industries' IT VP recognized early on that, while the 50% goal was primarily intended to get people thinking radically about the way they did business, top management clearly expected significant cost savings. For anything above 10%, she knew that cost savings meant a major reduction in the number of IT employees. She also realized that either she could wait for mandated across-the-board cuts or she could proactively begin addressing the issue of how to reduce costs and prepare her organization for the future.

At the outset, her specific concerns included the need to preserve her most technically competent personnel, systematically address existing organizational design and process issues, and avoid the organizational turmoil that had accompanied a similar reorganization undertaken five years earlier. Retaining her best talent would be more difficult if across-the-board cuts began using only seniority or other standard criteria. She decided to respond to the call for significant cost cutting by aggressively undertaking a major re-structuring within her own organization in order to ensure that critical considerations for the long-term effectiveness of the IT organization were given sufficient weight in the overall task of cutting costs.

Challenges

Within Key Industries, there was already an ongoing analysis of activities being orches-trated by an outside strategic planning group. The analysis would provide a clearer idea of the future demands that would be placed on IT and, therefore, the key organizational design and process issues. However, the analysis would not tell this VP how to address her key implementation issue: whom to let go. She was faced with a double-edged sword: her most technically competent employees worked in areas of the IT organization that were likely to be dramatically reduced in size or eliminated by the expected re-prioritization of activities, while more fundamental areas were staffed by less effective employees using obsolete technologies and procedures that should be outsourced.

The VP recognized that the key to a successful reorganization would be the ability to identify and keep the most technically current and highest performing people by reassigning them to other parts of the organization. She might have achieved this objective by using existing performance appraisal ratings. However, a quick review indicated that, as in many companies, these data were seriously flawed: 83% of the ratings were “Superior” or “Above Average,” and only six out of nearly 500 individuals were rated “Below Average.” In addition, many individual contributors did not have current evaluations, while evaluations of managers were almost entirely absent. Finally, little data existed on the level or range of technical skills possessed by each employee.

The IT VP, together with her director of human resources, determined that she had to start from scratch. In deciding to initiate an IT reorganization, she rejected easier and more typical approaches such as “last in, first out” or the elimination of entire work units. Instead, she focused her efforts on identifying and keeping the best people as part of a conscious strategy to position her IT organization for the future. She also recognized that some legal action stemming from the multiple personnel decisions was likely and wanted to make sure the approach was as transparent and as defensible as she could possibly make it.

Approach

1. Assessing work unit performance

   The first step in the process was based on a “balanced scorecard” made up of four primary components:

   - Customer satisfaction with level of service and/or quality of deliverables as measured by an annual customer survey
   - Cost competitiveness against best available alternative suppliers of the same services

- Robustness and integrity of current operating processes and procedures
- The work unit as a source of technical talent for other parts of the IT organization and the overall business

All sixteen departments within the IT organization were ranked against these four criteria by the VP of IT and her team. This simple process in itself provided a high level recognition of the location of existing talent.

2. Identifying strategic direction and major challenges

   No special effort was needed to identify emerging challenges and the role of outsourcing because these were already part of IT's strategic plan: outsourcing plans for data centers and help desks were already in place, a technology roadmap had been agreed to, as well as major high priority software development efforts and process re-engineering efforts, and each initiative had headcount implications. IT's strategic plan, however, was fine-tuned based on the recognition that some IT departments were clearly less effective than others.

3. Removing weak and problem performers

   The performance review data and discussions with HR quickly identified the individuals already known to be problem performers. The VP agreed to let these individuals go as quickly as possible in round one of the redesign effort. This helped to set a context for a more systematic review of the rest of the organization, since individuals reviewed in round two would not be lumped in with weak performers.

4. Defining critical IT competencies

   Although a general competency model existed for Key Industries, it was viewed within IT as far too generic and failed completely to identify technical capabilities. As a first step, the VP of IT asked her team of directors to quickly but system-atically identify the knowledge, skills, and abilities (KSAs) that were (1) critical given the likely future demands on IT and (2) distinguished top performers in the key job families that would be relevant going forward. The resulting KSA framework provided the basis for evaluating IT managers and technical professionals.

5. Assessing IT skills and capabilities

   The VP and her five directors agreed to adopt our recommended six-step process, beginning with a talent review at the very top of the IT organization. An outside facilitator was used to guide the process, in the presence of the VP, so that there would be no conflicts of interest and that managers at each level provided fair and accurate assessments of their direct reports. Only those managers at each organizational level who "passed" the assessment at their organizational level were invited to participate in assessing those at the next level down.

   During the cascading working sessions, managers and supervisors rated all their direct reports on each performance, skill, or competency dimension at the same time. For example, managers rated each of their direct reports on a relevant "quality metric," "database design" skills, or "results orientation" competency. Once one individual's ratings were discussed and any necessary adjustments made, they would move on to the next individual, all the while openly discussing their ratings with their peers. Since in many instances a manager's peers were also "customers" of those being assessed, these other managers or supervisors were in a position to confirm or suggest changes to the ratings of an individual under review.

As noted earlier, a most important role played by the facilitator was the resolution of disagreements in ratings made by different managers and supervisors of the same individuals. These disagreements in ratings were resolved based on evidence from past performance. For example, from our earlier work, the facilitators knew which of the sixteen departments were weakest in terms of the "balanced scorecard" metrics; they then used this information to level-set the ratings that individuals received so that there was general agreement between the average ratings received by individuals in an IT department and the overall performance of that department. In general and not surprisingly, there were relatively fewer superstars in poor-performing departments.

6. Redesigning and reassigning

The evaluation data from the open rating discussion were entered into a skills and capabilities database. The database was designed to facilitate matching of the requirements of a particular job with the skills possessed by different individuals, with qualified individuals being presented in a list.

The VP of IT and her team began the organizational redesign using IT's existing strategic plan, the results of the corporate-wide activity analysis project, insight gained from the study of the existing job families, and the data from the IT skills and capabilities assessment. The latter was particularly critical in identifying significant shortages of technical skills relevant for future initiatives.

Managers for the different areas of the IT organization were responsible for re-thinking the design of their individual areas. In deciding on the critical job functions and the number of people they would need, these managers used the database to first identify key requirements and then to identify the individuals who had the technical and non-technical skills required for each job. The database allowed managers to identify appropriate candidates for positions from areas outside of their own part of the IT organization. The database also flagged individuals who had specific skill deficiencies given the requirements of the job function being filled so that the managers understood the possible limitations of an individual's performance from day one. Those who had no assigned positions at the end of the IT organization re-staffing process had the opportunity to find positions elsewhere within Key Industries or to accept a severance package.

Results

The IT organization redesign resulted in a reduction in the number of managers and supervisors from 57 to 41 (a 28% reduction) and the number of individual contributors (programmers, analysts, etc.) from 436 to 340 (a 22% reduction). More significantly, the redesign of the IT organization was accomplished without the loss of critical technical talent in whom Key Industries had invested millions of training and development dollars. There were difficulties for a number of individuals who were not seen as strong performers or whose technical skills were no longer in demand; however, only two employment lawsuits were filed and were quickly resolved. Finally, the IT function was the only department within Key Industries to make significant progress towards meeting the company's 50% cost reduction target.

Another outcome of this systematic evaluation process was that many IT managers now had information about the performance of their direct reports as viewed by other managers, leading to the recognition of previously ignored or unknown performance problems. As a result, a number of these performance issues were addressed within a month of the evaluation session. In addition, many individuals received information on where they stood compared to their peers for the first time. For some managers, the evaluation process provided the first performance feedback they had received in years. Finally, managers realized that individuals in other parts of the IT organization were much more capable than some of their own direct reports and would in fact be "good fits" in their part of the IT organization.

Conclusion

The experience of Key Industries suggests that, when necessary, organizations can tackle major restructuring efforts in a systematic, rational, and rapid fashion, even if they do not currently have thorough evaluations of their employees' technical and non-technical skills. Such evaluations, with top management support, can be designed and developed in relatively short order, as can "open" processes that encourage candid discussions about individual performance and skills and where managers and supervisors can be held accountable for making reasonable judgments. Such processes produce evaluation data that is both credible and consistent. The credibility and consistency of the data allows management to make decisions that are both good for the long-term technical and economic health of the organization and fair in the eyes of its employees.

One final point: throughout this process, it is very important to be in constant communication with employees regarding the challenges the organization is facing and the business reasons for the downsizing. Making the evaluation criteria public and discussable, engaging employees in self-assessment of critical skills, and giving them the opportunity and latitude to develop new skills or seek other positions that fit better with their current skills and preferences will go a long way to lessen the impact of the reductions in force. Management owes it to everyone to be up front and candid throughout, so people know what they can expect and prepare for whatever eventuality may occur. In the end, it is all about putting people in greater control of their own destiny, despite unforeseen challenges.

References

Cappelli, P. (2000). Examining the incidence of downsizing and its effect on establishment performance. On the Job: Is Long-Term Employment a Thing of the Past? Neumark D (ed.). Russell Sage Foundation: New York; 463–516.

Cascio, W. (2002). Strategies for responsible restructuring. *Academy of Management Executive,* 16: 80–91.

Chadwick, C., Hunter, L. & Walston, S. (2004). Effects of downsizing practices on the performance of hospitals. *Strategic Management Journal,* 25: 405–427 (2004).

Davy, J., Kinicki, A. & Scheck, C. (1991). Developing and testing a model of survivor responses to layoffs. *Journal of Vocational Behavior,* 38: 302–317.

Maurer R. (1999). Thirteen Alternatives to Downsizing, *Workforce Magazine*, January 24.

Wilkinson, R. (2004). Downsizing, Rightsizing or Dumbsizing? Quality and Human Resources, in the Management of Sustainability. *TQM Journal*, 18 October.

About the authors

Bernard Cullen, a Partner at Cambria Consulting, co-leads Cambria's Assessment practice. Bernie has over 30 years of experience designing and implementing solutions to strategic human resources issues. He has consulted on more than 150 major projects covering the design and implementation of the full spectrum of HR systems, and helped lead the development of Cambria's competency-based HR architecture to design recruiting, performance management, workforce planning, succession planning, and promotion processes for private-sector clients.

George Klemp, a Partner at Cambria Consulting, leads Cambria's Consulting practice. George has over 30 years of experience designing and implementing solutions to strategic human resources issues. George, a widely recognized expert on building and applying competency models, has consulted on more than 200 major projects covering the design and implementation of the full spectrum of HR systems, including recruiting, succession planning, and promotion processes for private-sector clients.

He can be reached by e-mail (gklemp@cambriaconsulting.com) or by phone at (617) 523-7500.