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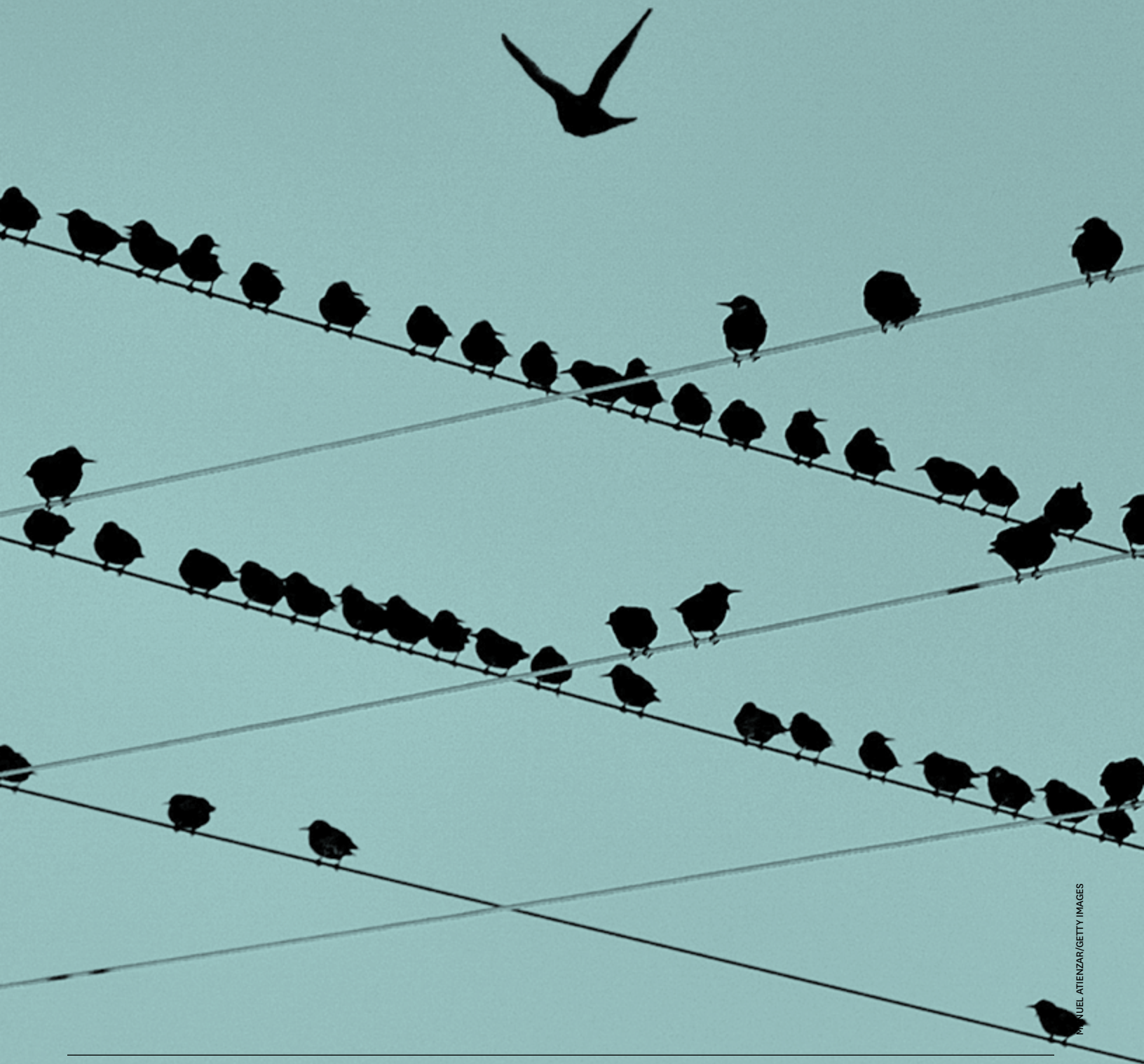
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Layoffs That Don't Break Your Company

Better approaches to workforce transitions

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LAYOFFS THAT DON'T BREAK YOUR COMPANY



BETTER APPROACHES TO WORKFORCE TRANSITIONS

BY SANDRA J. SUCHER AND SHALENE GUPTA

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Two great forces are transforming the very nature of work: automation and ever fiercer global competition. To keep up, many organizations have had to rethink their workforce strategies, often making changes that are disruptive and painful. Typically, they turn to episodic restructuring and routine layoffs, but in the long term both damage employee engagement and company profitability. Some companies, however, have realized that they need a new approach.

IN BRIEF

THE SITUATION

Automation and fierce competition are forcing many companies to resort to frequent rounds of layoffs.

THE PROBLEM

All too often, layoffs done for short-term gain damage employee engagement and actually reduce profitability.

THE BETTER WAY

Some companies have developed workforce change strategies that make sparing use of staff reductions and ensure that when they do happen, the process feels fair and the company and the affected parties are set up for success.

Consider the case of Nokia. At the beginning of 2008 senior managers at the Finnish telecom firm were celebrating a one-year 67% increase in profits. Yet competition from low-cost Asian competitors had driven Nokia's prices down by 35% over just a few years. Meanwhile, labor costs in Nokia's Bochum plant in Germany had risen by 20%. For management, the choice was clear: Bochum had to go. Juha Åkräs, Nokia's senior vice president of human resources at the time, flew in to talk about the layoff with the plant's 2,300 employees. As he addressed them, the crowd grew more and more agitated. "It was a totally hostile situation," he recalls.

The anger spread. A week later 15,000 people protested at Bochum. German government officials launched an investigation and demanded that Nokia pay back subsidies it had received for the plant. Unions called for a boycott of Nokia products. The news was filled with pictures of crying employees and protesters crushing Nokia phones. Ultimately, the shutdown cost Nokia €200 million—more than €80,000 per laid-off employee—not including the ripple effects of the boycott and bad press. The firm's market share in Germany plunged; company managers estimate that from 2008 to 2010 Nokia lost €700 million in sales and €100 million in profits there.

In 2011, when Nokia's mobile phone business tanked, its senior leaders decided they needed to restructure again. That would involve laying off 18,000 employees across 13 countries over the next two years. Chastened by their experience in Germany, Nokia's executives were determined to find a better solution. This time, Nokia implemented a program that sought to ensure that employees felt the process was equitable and those who were laid off had a soft landing.

One of us, Sandra, has spent eight years researching best practices for workforce change in global

multinational companies. She has seen that all too frequently companies do bad layoffs, do layoffs for the wrong reason, or worse, do both. By "bad," we mean layoffs that aren't fair or perceived as fair by employees and that have lasting negative knock-on effects. The job cuts in Bochum ignited outrage because Nokia had generated so much profit the year before. Consequently, they were seen as unjust and took a steep toll on Nokia's reputation and sales. And when we say "wrong reasons," we mean done to achieve short-term cost cuts instead of long-term strategic change. In 2008, Nokia did have the right reasons, but it still suffered because of its process.

Some governments, recognizing the massive damage layoffs create, have written laws protecting employees against them. For example, a number of European countries require companies to provide a social or economic justification before they can conduct layoffs. France, however, recently eliminated the requirement to provide an economic justification, and in the United States companies can conduct layoffs at will. Regardless of how easy it might be to cut personnel, executives should remember that doing so will have consequences.

The research clearly shows that bad layoffs and layoffs for the wrong reasons rarely help senior leaders accomplish their goals. In this article, we'll present a better approach to workforce transitions—one that makes sparing use of staff reductions and ensures that when they do happen, the process feels fair and the company and the affected parties are set up for success.

WHY LAYOFFS ARE INEFFECTIVE

If Nokia's story sounds familiar, albeit a little more colorful than usual, that's because it is. In the United States alone, the Bureau of Labor Statistics reports, 880,000 to 1.5 million people were laid off annually from 2000 to 2008 and from 2010 to 2013 (the last year data was compiled). This happened even when the economy was expanding. During 2009, the height of the Great Recession, 2.1 million Americans were laid off. Globally, unemployment rose by 34 million from 2007 to 2010, data from the International Labour Organization shows.

Layoffs have been increasing steadily since the 1970s. In 1979 fewer than 5% of *Fortune* 100 companies announced layoffs, according to McMaster University sociology professor Art Budros, but in 1994 almost 45% did. A McKinsey survey of 2,000 U.S. companies found that from 2008 to 2011 (during the recession and its aftermath), 65% resorted to layoffs. Today layoffs have become a default response to an uncertain future marked by rapid advances in technology, tumultuous markets, and intense competition.

Yet other data on layoffs should give companies pause. In a 2012 review of 20 studies of companies that had gone through layoffs, Deepak Datta at the

University of Texas at Arlington found that layoffs had a neutral to negative effect on stock prices in the days following their announcement. Datta also discovered that after layoffs a majority of companies suffered declines in profitability, and a related study showed that the drop in profits persisted for three years. And a team of researchers from Auburn University, Baylor University, and the University of Tennessee found that companies that have layoffs are twice as likely to file for bankruptcy as companies that don't have them.

All too frequently, senior managers dismiss such findings. Some argue that since companies do layoffs because they're already in bad shape, it's no surprise that their financial performance may not improve. Layoffs are so embedded in business as a short-term solution for lowering costs that managers ignore the fact that they create more problems than they solve.

AFTER A LAYOFF, SURVIVORS EXPERIENCED A 41% DECLINE IN JOB SATISFACTION, A 36% DECLINE IN ORGANIZATIONAL COMMITMENT, AND A 20% DECLINE IN JOB PERFORMANCE.

Companies that shed workers lose the time invested in training them as well as their networks of relationships and knowledge about how to get work done. Even more significant are the blighting effects on survivors. Charlie Trevor of University of Wisconsin-Madison and Anthony Nyberg of University of South Carolina found that downsizing a workforce by 1% leads to a 31% increase in voluntary turnover the next year. Meanwhile, low morale weakens engagement. Layoffs can cause employees to feel they've lost control: The fate of their peers sends a message that hard work and good performance do not guarantee their jobs. A 2002 study by Magnus Sverke and Johnny Hellgren of Stockholm University and Katharina Näswall of University of Canterbury found that after a layoff, survivors experienced a 41% decline in job satisfaction, a 36% decline in organizational commitment, and a 20% decline in job performance.

While short-term productivity may rise because fewer workers have to cover the same amount of work, that increase comes with costs—and not only to the workers. Quality and safety suffer, according to research by Michael Quinlan at the University of New South Wales, who also found higher rates of employee burnout and turnover. Meanwhile, innovation declines. For instance, a study of one *Fortune* 500 tech firm done by Teresa Amabile at Harvard Business School discovered that after the firm cut its staff by 15%,

the number of new inventions it produced fell 24%. In addition, layoffs can rupture ties between salespeople and customers. Researchers Paul Williams, M. Sajid Khan, and Earl Naumann have found that customers are more likely to defect after a company conducts layoffs. Then there's the effect on a company's reputation: E. Geoffrey Love and Matthew S. Kraatz of University of Illinois at Urbana-Champaign found that companies that did layoffs saw a decline in their ranking on *Fortune's* list of most admired companies.

Employees who are downsized pay a price beyond the immediate loss of their jobs. Wayne Cascio, a professor at the University of Colorado, points to the Labor Department's survey of workers who were laid off during 1997 and 1998, an economic upswing. Most were worse off a year later: Only 41% had found work at equal or higher pay, 26% had found jobs at

lower pay, and another 21% were still unemployed or had left the workforce entirely. The effects follow people throughout their lives. A 2009 Columbia University study that looked at employees who had been laid off during the 1982 recession showed that 20 years later they were still earning 20% less than peers who had kept their jobs. The aftershocks aren't limited just to earnings: According to a study by Kate Strully, an assistant professor at SUNY, laid-off employees

have an 83% higher chance of developing a new health condition in the year after their termination and are six times more likely to commit a violent act.

THE SEARCH FOR ALTERNATIVES

A few companies have been experimenting with better ways to handle their changing workforce needs. Take AT&T. In 2013 the company's leaders concluded that 100,000 of its 240,000 employees were working in jobs that would no longer be relevant in a decade. Instead of letting these employees go and hiring new talent, AT&T decided to retrain all 100,000 workers by 2020. That way, the company wouldn't lose the knowledge the employees had developed and wouldn't undermine the trust in senior management that was necessary to engagement, innovation, and performance. So far, the results seem very positive. In a 2016 HBR article, AT&T's chief strategy officer, John Donovan (now CEO of AT&T Communications), noted that 18 months after the program's inception, the company had decreased its product development cycle time by 40% and accelerated its time to revenue by 32%. Since 2013, its revenue has increased by 27%, and in 2017 AT&T even made *Fortune's* 100 Best Companies to Work For list for the first time.

In her work, Sandra has studied seven companies that, like AT&T, have successfully pursued alternatives

to traditional layoffs. An analysis of their experiences reveals that an effective workforce change strategy has three main components: a philosophy, a method, and options for a variety of economic conditions.

A philosophy. A workforce change philosophy serves as a compass for senior leaders. It builds on a company's values and spells out the commitments and priorities the company will abide by as it implements change. A philosophy helps leaders answer the following questions:

- What value do we believe employees contribute to our business and its success?
- What expectations do we have for employees' engagement, loyalty, flexibility, and ability to adapt and grow?
- What do we owe employees as a fair exchange for what they have given us?
- How can employees help us develop and implement workforce change?

The philosophy of the French tire maker Michelin, for example, includes hiring people for their potential rather than for the job. In its labor relations policy, the company describes its commitment to employees' long-term growth. Each employee is assigned a career manager who oversees his or her development and helps make sure it aligns with Michelin's needs.

The company also has a defined approach to workforce change and restructuring. Michelin's labor relations policy described it like this in 2013:

Restructures are inevitable in certain circumstances in order to maintain the company's global competitiveness. These restructures must, as far as possible, take place at times when the company's health allows mobilization of adequate resources to attenuate the social consequences. Whenever possible, staff at the entities concerned and their representatives are invited to work together to seek and suggest solutions for restoring competitiveness and reducing overcapacity, which may open up an alternative to closing an activity or site. When restructuring is unavoidable, it must be announced as soon as possible and carried out according to the procedures negotiated with the staff representatives. The ensuing changes on a personal level must be supported for as long as is necessary to ensure that the reclassified employees find a satisfactory solution in terms of standard of living, stability, family life and self-esteem.

When Nokia was contemplating that massive workforce reduction in 2011, its senior leaders articulated a philosophy with four core values:

1. *We will accept our responsibility as the driver of the local economies and aim for the highest of aspirations in supporting our previous and current employees.*

2. *We will take an activist role and lead the program with our brand, expertise, and resources in the key areas that matter most.*
3. *We will involve all of the relevant parties in the program design and operations.*
4. *We will communicate openly towards all stakeholders, including employees, unions, government, and local stakeholders, even when we do not know the full answers.*

As Nokia's philosophy highlights, workforce change can affect many people beyond employees. A company must communicate its intent directly without leaving any of them in the dark or piecing together scraps of information to figure out what the future holds.

A WORKFORCE CHANGE STRATEGY SHOULD ANTICIPATE THREE DIFFERENT SCENARIOS: A HEALTHY PRESENT, SHORT-TERM ECONOMIC VOLATILITY, AND AN UNCERTAIN FUTURE.

A method. Having a clear methodology will allow companies to explore alternatives to layoffs, and if they cannot be avoided, minimize the harm they cause. To establish one, firms need to address three questions:

- How will we plan for workforce change on an ongoing basis?
- Who will be accountable for managing and supervising it?
- What metrics should we use to determine whether our actions are effective?

In 2013, Michelin's CEO, Jean-Dominique Senard, asked the members of his team to turn the insights they'd gathered from the previous decade's restructuring efforts into a formal process for workforce change. As a result, Michelin integrated three planning processes—product planning, territory planning, and restructuring planning—into one. The product-planning groups project their anticipated production for the next five years, and then the territories identify which regions will have too much or too little production capacity and what technologies each factory will need. The restructuring plans come out of the dialogue between the product and territory heads. For example, in October 2013, Michelin determined that it would have overcapacity for truck tire production in its Budapest factory and decided to close it in mid-2015. By making that call early, Michelin's team had

time to carefully plan objectives for the shutdown and create a way to reduce the impact on the affected employees (something we'll discuss more later).

Michelin has set up an accountability structure that clearly delineates who is responsible for what. The company's executive committee, led by the CEO, oversees workforce change globally. Because more than 50% of Michelin's factories and most of its workforce reductions are in Europe, a European restructuring committee supports the executive committee. It identifies factories that should be closed or downsized and directly oversees all European restructurings. Finally, Michelin establishes a committee for each factory that will be affected, consisting of regional and country executives who are responsible for implementing the restructuring plan. Two senior executives at headquarters—a director of restructuring and a director of product planning—coordinate the entire process.

Like any other good strategy, an effective workforce change strategy includes goals against which success can be measured. An example of these comes from Honeywell. In the 2001 recession, right before Dave Cote became its CEO, the company laid off 25,000 employees, or nearly 20% of its staff. Sales fell by 11% from 2000 to 2002. When the recession hit in 2008, and it looked as if more workforce changes might be required, Cote set two goals: to improve on Honeywell's poor performance during the 2001 recession, and to be in a stronger position than its competitors when the recovery came.

To measure the first goal, Cote decided to compare the company's sales, net income, and free cash flow figures for the two recessions. As it turns out, the firm was able to improve substantially on all three measures. In 2009 Honeywell's sales were 39% higher than its 2002 sales, its free cash flow was 94% higher, and its net income was more than six times higher. To monitor progress on the second goal, performance against competitors, financial data providers developed two measures: the percent change in operating income from the 2007–2008 peak to 2011, and total stock returns in 2012. At +1.8%, Honeywell had the highest postrecession increase in operating margins (versus -4.5% to +1% among its peers). And at 75.28, Honeywell also had the highest three-year total stock return in 2012, 50% better than its closest competitor's return and four times better than the lowest-performing competitor's.

Options for a variety of economic conditions.

A workforce change strategy should anticipate three different scenarios: a healthy present, short-term economic volatility, and an uncertain future.

A healthy present. In the immediate term, senior leaders should practice disciplined hiring and use stringent performance metrics to build a strong organization that can weather change. A lean approach to staffing will help companies avoid yo-yoing between overexuberant hiring during growth and damaging staff reductions when demand falls.

Before Cote began his turnaround in 2002, Honeywell had a policy of hiring freely during good times and then cutting jobs in downturns. The drastic head count reduction of 2001 was too much for Cote, who responded by introducing hiring controls. Senior leaders had to justify how staff additions would help new-product or market development, and if they couldn't, had to trim costs elsewhere to fund the hires.

Too often managers use layoffs as an excuse to avoid difficult discussions about performance. Many companies practice “rank and yank” layoffs to thin out weaker employees, often on an annual basis, but it's more productive to use meaningful performance reviews and employee development plans to cultivate a base of high performers. Lincoln Electric, an arc-welding products and consumables manufacturer headquartered in Cleveland, Ohio, has had a no-layoff policy in its U.S. operations since 1958. Part of the reason it maintains that policy is that it has a reputation for high-quality and efficient staff, thanks to very strict performance standards and a rigorous evaluation process. Employees are assessed twice a year in five areas. Performance is competitive within departments, and performance ratings are tied to a merit-based compensation system. Employees who fall in the bottom 10% receive an improvement plan and, if they remain there consistently, are eventually let go.

Short-term volatility. Experienced managers develop a range of ways to reduce costs without resorting to destructive layoffs. Three approaches implemented by Honeywell, Lincoln Electric, and Recruit Holdings, a Japanese human resources and advertising media conglomerate, demonstrate how much room there is for creative management during downturns.

During the Great Recession, Cote used furloughs instead of layoffs at Honeywell. Having weathered three recessions when he was at GE, he had developed a sense for when a business cycle might run its course. Two years before any sign that the economy was in trouble, he began to pull back on hiring. Once the recession hit, Honeywell furloughed employees for one to five weeks, providing unpaid or partially compensated leaves, depending on local labor regulations. According to an article by Tom Starnier in *Human Resource Executive*, the company's finance department estimated that furloughs saved Honeywell the equivalent of 20,000 jobs.

In a 2013 article he wrote for HBR, Cote explained, “I've never heard a management team talk about how the choices they make during a downturn will affect performance during a recovery....I kept reiterating that point: There will be a recovery, and we need to be prepared for it.” Furloughs allowed Honeywell to retain the talent it needed when demand resurged and helped it stay profitable throughout the recession and achieve strong growth during the five years after the recovery.

In 2000, Recruit Holdings developed an innovative system, Career View, through which it hires employees

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with nontraditional backgrounds as three-year contractors. The system helps Recruit achieve two goals: expand its reach outside Japan’s major cities and increase workforce flexibility—a real feat given that Japanese companies traditionally don’t do layoffs. The program targets rural employees who lack the education and experience to land a job at a major Japanese corporation, hiring them as sales associates for regional offices near their hometowns. Six months after joining Recruit, these contractors meet with career counselors to discuss their goals. They also receive detailed performance reviews that lay out the skills they’re developing, the skills they need to get their next job—generally at another company—and what they can do to bridge the gap between the two. Approximately 90% of Career View employees are able to get another job at the end of their three-year stints, and Recruit is able to expand its regional presence and adjust its sales staffing up or down according to the economic cycle.

Lincoln can avoid layoffs because it requires employees to accept flexible assignments. Employees are expected to work extra hours when demand ramps up, and they understand that they’ll work shorter hours when it ramps down. In addition, they can be reassigned to any other job, including one with a lower salary, for the duration of a downturn. When orders fell during the Great Recession, for instance, Lincoln moved some factory workers into sales. Those employees developed a deeper understanding of Lincoln, and customers benefited because the factory workers had a thorough knowledge of the firm’s products. In addition, during economic lulls, Lincoln’s leaders automatically shift their priorities to initiatives they aren’t able to fully attend to when business is booming, such as developing quality improvements, scrap-reduction programs, research and development projects, and maintenance tasks—all enabled by the availability of skilled employees who have more time to help out when demand falls.

An uncertain future. Market shifts, new technologies, and new competition can require companies to do major restructuring. Before considering a layoff, they should see if they can take a cue from AT&T’s transformation.

Michelin, for one, has embraced transformations as part of its workforce strategy. When Bertrand Ballarin joined the company, in 2003, one of his first jobs was to manage a factory in Bourges, France, that was going to be shut down. He gathered its managers and union reps, explained the situation, and gave them a year to come up with a plan to save the plant. After analyzing how other Michelin plants were producing airplane tires, one of three product lines handled in the factory, the team concluded that the Bourges facility had a better, more consistent industrial process for making them than the other plants did. The team successfully argued that Bourges should specialize in airplane tires and get a new research center to aid product development.

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In 2013, Michelin began applying the lessons from Bourges to a factory in Roanne, France, that was at risk of being shut down. From October 2014 to March 2015, more than 70 individuals, including leaders from headquarters, union representatives, plant managers, and employees, met to develop a transformation strategy for Roanne. Rather than closing the facility and laying off its employees, Michelin agreed to put €80 million into creating a new line of premium tires there; the head count would fall from 850 to 720 employees through natural attrition. Instead of the traditional four teams working Monday to midday Saturday, the plant would reorganize into five teams that kept operations running seven days a week around the clock, and all employees would work six additional days a year. These changes allowed the plant to flex production up or down by 12% according to market conditions. In addition, Michelin dedicated €2 million to programs for improving the quality of management and work-life balance—issues that had emerged during the transformation strategy planning—for the plants' employees.

However, there are times when a transformation isn't possible or the transformation itself results in layoffs. In these cases, companies have to ensure that employees are treated fairly. This isn't just about being a good Samaritan. Datta found that companies tended to get better financial results after a layoff when employees thought it was handled equitably and done for strategic reasons rather than cost cutting.

Let's look again at what happened at Nokia in 2011, when its senior leaders realized the company needed another restructuring. Then-chairman Jorma Ollila was determined to avoid another Bochum. To help the company do so, a small team of senior leaders developed Nokia's Bridge program, which aimed to see that as many employees as possible had a new opportunity lined up the day their current job ended. Nokia opened Bridge centers in the 13 countries where the layoffs would take place. The program outlined five paths employees could choose from:


- 1. Find another job at Nokia.** In order to avoid favoritism, selection committees were formed to determine which employees to retain, instead of having local managers choose.
- 2. Find another job outside Nokia.** The centers offered outplacement services, including career coaching, résumé workshops, career fairs, and networking events.
- 3. Start a new business.** Individual employees or teams could present business proposals to win grants of up to €25,000. Employees were given two months to develop their plans, as well as support such as coaching and mentoring, networking introductions, and training. Nokia took no stake in any of the funded businesses.

4. Learn something new. Nokia offered training grants for business-management and trade-school courses in many areas, including restaurant management, cosmetology, construction, and firefighting.


5. Build a new path. The company offered financial support to employees who had personal goals they wanted to accomplish, such as volunteering.

Nokia spent €50 million on Bridge, or about €2,800 per employee. That accounted for just 4% of the €1.35 billion it spent on restructuring from 2011 to 2013. As a result of the program, 60% of the 18,000 affected workers knew their next step the day their jobs ended. Overall, 85% of the Finnish Bridge participants said they were satisfied with the program, while 67% of global employees said they were. Furthermore, the layoff candidates and the remaining employees maintained or improved quality levels throughout the restructuring. Employees at the sites that were targeted for downsizing achieved €3.4 billion in new-product revenues, one-third of new-product sales—the same proportion they had brought in before. Employee engagement scores in all areas of the company held steady throughout the restructuring. And, unlike the situation in Bochum, there were no labor actions of any kind in the 13 countries where the layoffs happened. By all accounts Nokia had indeed found a better approach to workforce change.

In 2017, three years after selling its devices and services business to Microsoft, Nokia used an enhanced version of the Bridge program to handle its latest restructuring. Microsoft Finland has rolled out a similar program. And Finland's government has even taken cues from Bridge and incorporated ideas from it into legislation outlining what companies that conduct layoffs are required to provide for affected employees.

ONE OF THE biggest questions organizations face as they grapple with a constantly shifting economic landscape is whether their current workforce can help them make the transitions necessary to their success. While companies tend to prioritize short-term financial results over the long-term well-being of their employees, employees are the lifeblood that enables a company to keep delivering the products and services that ultimately generate shareholder benefits. Michelin's and Nokia's experiences show that employees can and should be trusted to perform well, even when they know they might lose their jobs. For all companies, planning thoughtful workforce change instead of automatically resorting to layoffs is a better way to address the vicissitudes of technological transformation and intensifying competition. 

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