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Energizing Employees in
Recessionary Times
*Try Motivating,
Not Mandating*



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Energizing Employees in Recessionary Times

Try Motivating, Not Mandating

Cost-cutting efforts could be a reality for some time to come. One dimension of cost-cutting is often disregarded—the critical need to ensure cost cuts occur in ways that obtain positive emotional commitment within the context of the culture. Employees need to somehow feel positively motivated to support decisions and to commit to behavioral change that reduces costs. This is a “tall order,” especially when layoffs are at the center of the cuts. However, in our experience, cost-cutting and layoffs fail when executives simply try to mandate attitudes and behaviors. These efforts will more likely succeed when companies make positive employee motivation an integral part of the process. The first step is for executives to take on the responsibility of ensuring that front-line leaders’ actions appeal to employees’ hearts and minds. Positive motivation cannot be delegated or mandated.

In this commentary piece we explore how effective cost reduction capitalizes on and reinforces company culture—and integrates emotional commitment of the workforce with the strategic imperatives for the business. While easily said, some companies have done this.

Why Most Cost Reductions Fail

Under tremendous recessionary pressures, executives in a range of industries are currently considering, launching, or already grappling with cost reduction programs. Unfortunately, many of these efforts will be disappointing, to say the least. In 2005, a McKinsey¹ study reported that only ten percent of companies sustain cost reduction benefits after three years. A 2008 Archstone Consulting survey of 350 companies² highlights several reasons why cost reduction efforts fail. In the most frequent reason given—by 44% of respondents—executives indicated that “implementation was not well managed.” In other words, people did not do what they were supposed to do. Why does this happen?

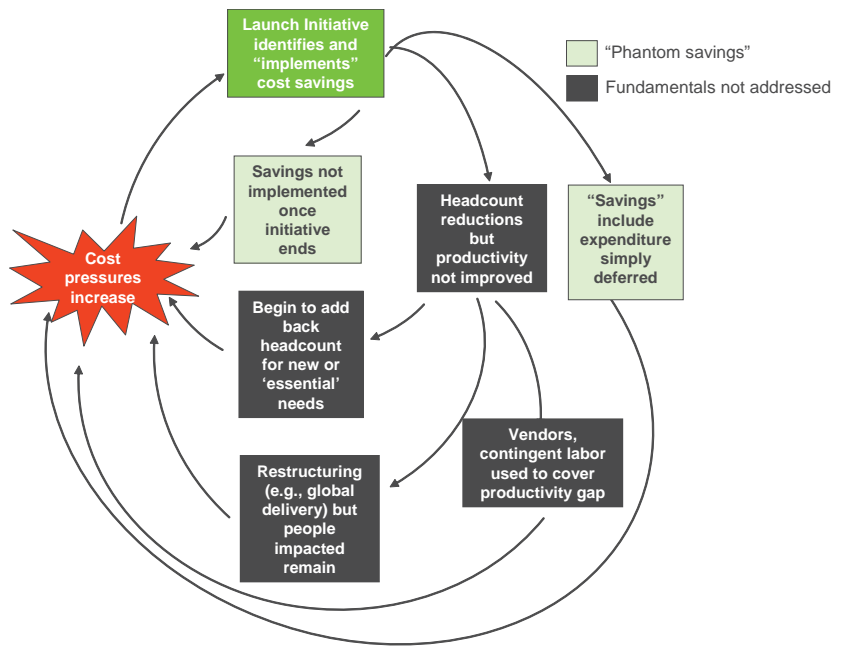
“Phantom Savings” Prevail

A common problem is that companies unwittingly put themselves into a suboptimal cycle of cost reduction that is both short-term and short-sighted. The cycle begins when managers launch an initiative to identify and implement cost reductions in different functions. The first problem is that many of these cost savings are “phantom”—the organization does not sustain the savings once the initiative goes away and many of the savings are nothing more than deferred expenditures.

Fundamentals Are Not Addressed

The second problem is that the initiative does not address fundamentals. Productivity does not improve, leadership systems are unchanged, and “cost-accommodating” behaviors persist. As a result, headcount savings in functions creep back in the form of higher expenditures with vendors, potentially impacting SG&A or cost of goods sold. Moreover, additional hiring occurs (often at higher cost) as “new” needs emerge. The diagram below illustrates the problem:

The Sub-Optimal Cycle of Cost Reduction



It is highly unlikely that companies in the 2008 recession will avoid these two parallel pitfalls. Simply put, the hasty introduction of cost savings programs that recessions prompt makes the likelihood of short-sighted efforts even greater.

“Mandating” vs. “Motivating” Cost Reduction

So what should companies embarking on cost reduction do? They should probably start by asking themselves if “quick and dirty” cost reductions are all they want or need. If not, they should look honestly at the ultimate impact of any earlier cost reduction efforts. Important savings commitments may not have been implemented. Examples include purchasing commitments not followed, or new departments put in place to replace others that were downsized. Pull out the PowerPoint presentations from several years before and ask what happened, separating justified and unacceptable reasons for deviations. Avoid the natural human tendency to justify past decisions. In short, learn from the last effort before launching a new cost reduction initiative.

The “Mandating” Approach – Firmness, Discipline, And Often Fear

If companies are going to approach cost reduction better than they did in the last recession, they have two very different approaches to consider: they can simply rely on mandating or they can emphasize motivating. While there is an unavoidable overlap, the primary emphasis is what matters most.

Top-down mandating is the classic way to launch a cost-cutting effort. “Mandaters” believe that the cycle of suboptimal cost reduction can be broken through more firm resolve, discipline, and fear. It will not be surprising to see the 2008 rendition of Al Dunlap and his provocative style (In 1995 he said it was important to approach restructurings under the principle of “do it once, do it severe, get it over with”³). Targets are set, the axe falls, and everyone from the CEO downwards does their best to follow through on the cost cuts. In many cases, executives call upon experts from headquarters or outside consultants to quantify opportunities for cost reductions and to complete the effort quickly. These initiatives frequently use methods and analytics that are unfamiliar to the organization and are hard for many people to understand and learn. Consequently, many of these efforts remain focused on the project and its science, rather than on the real needs of the company and its people.

Despite well intended top-down communications, employees suspect they are not getting the whole story. Firmness and discipline start to feel more like shouting selective messages and bullying as leaders push managers to “try harder” to enforce the cost reduction effort. Negative rumors circulate, insecurities build, and water cooler skepticism persists. Senior leaders and line managers tend to rely too heavily on human resource departments to find ways to reduce anxieties, clarify top-down directives, and help displaced employees find new jobs. Despite these efforts, the cumulative impact is a set of employee anxieties that often generate “deer in the headlights” reactions. Some of the deer hope the lights will just go away and do not move; others try to hide in the bushes and convince themselves that they are exceptions who will be spared.

Of course, the human resource department works hard to ameliorate the anxiety that people feel. They put proven programs and processes in place to manage the cost reduction effort, and they launch broad-based engagement efforts. Unfortunately, these efforts seldom address the disruption to a company’s culture that the mandated approach brings. Nor do they obtain the help of front-line supervisors, who are the critical link to motivating employee behaviors. A major part of the problem lies in lack

of integration between senior leadership actions, frontline supervisory efforts, and formal HR programs. As a result, the informal elements of the organization become confused, resentful, and counter-productive.

When Agent Orange Turned Sour

The Home Depot co-founder Bernie Marcus believed that if you motivate employees to empathize with their customers, you ensure both low cost operations and high-quality service—a belief that became known as “Agent Orange” and which defined The Home Depot’s unique culture. When we researched The Home Depot in the nineties, one employee confided that she would rather spend her Saturday working than relaxing at home. A store manager proudly revealed he measured each day’s performance simply by counting the smiles on the faces of customers leaving his store. When Robert Nardelli imposed more rigorous management disciplines, important elements of Agent Orange rebelled. Many executives and managers left, and others resisted or simply hunkered down behind the counters waiting for the storm to pass. And pass it did, as the Board replaced the CEO yet again at the beginning of 2007. According to the company’s financial reports, operating expenses as a percentage of sales rose from 20.7% of sales in 2000, just before Nardelli’s tenure, to 22.4% of sales for 2006, just before he departed. Operating costs per square foot, using year-end square foot data, rose from around \$77 to \$79 in the same period. The culture rebelled, even though this operating cost story is hardly harsh. Emotional commitment did not accompany rational compliance. In its latest year-end financial filing, The Home Depot notes that payroll costs increased by 76 basis points due to a number of factors, some of which reflect investments in store labor and bonus plans. After the trauma of prior years, The Home Depot ended up having to re-invest in employees and their motivation. In fact, associate engagement is now listed as The Home Depot’s first key strategic priority. Unfortunately, employee “engagement” on its own will be of limited motivational value unless it connects directly and emotionally to the work itself (and you really need the help of frontline motivators to make that connection). Nardelli’s approach had only limited success in cost containment—not because he was a poor choice as CEO, but because there are no short-cuts around employee commitment. The Home Depot learned the importance of working with the Agent Orange culture.

The Positive Motivational Approach – A “Proud To Be Thrifty” Mindset

Fortunately, companies have a more effective alternative to top-down, negative mandating, as well as to trying to engage employees superficially while the cost-cutting effort runs rough-shod over the positive elements of the culture. They can adopt the “positive motivational” approach. At first glance, executives might dispute that they can motivate employees and managers in positive ways around cost-cutting. Indeed, no one should pretend that headcount reduction can be as intrinsically motivating as other business experiences, and managers at all levels will still have difficult decisions to make. But the motivational approach to cost reduction involves employees committing emotionally to the cost challenge. “Motivators” look for ways to secure positive employee commitment—emotional as well as rational—to company decisions and behavior change. A few companies are able to do this systematically because they have built a culture that is

"proud to be thrifty." They communicate a noble purpose or positive theme that focuses their people on cost and value, such as the commitment by Southwest Airlines to making safe, comfortable air travel available to the average American. At Southwest, employees have been known to pay for energizing events, such as holiday celebrations, out of their own pockets.

Some companies also use formal processes to support motivation. For example, hourly employees at Nucor have lower per-hour compensation, and yet they earn more than their counterparts since Nucor uses an incentive structure that encourages low-cost behavior. These companies also generate informal momentum to encourage frugality. Thrifty companies draw on stories to celebrate the frugality of leaders, like Ingvar Kamprad, the founder of IKEA, who said "waste of resources is a mortal sin." Marshalling these different approaches can help people across an organization take pride in keeping costs low at all times, thus creating a sustained cost reduction program that continues as an integral part of the culture.

But Can the Motivating Approach Work In The Short Term?

Unfortunately, companies facing an urgent need to cut costs seldom have a "proud to be thrifty" culture and cannot create one overnight. Hence, executives might be tempted to say: "I know positive motivation is important, but we don't have time to worry about that right now. I can't see anyone feeling very positive about what we have to do in any case. So let's go with mandating."

In fact, employee engagement is always critical in peak performing cultures—particularly when it connects directly and emotionally to the work itself. A 2006 study from Towers Perrin-ISR⁴ showed that over a period of one year, companies with highly engaged employees increased net income by thirteen percent, while those with less engaged employees showed a four percent decline. In recessionary times, this employee engagement can be harnessed to speed cost reduction—because lots of people energize one another around specific tasks that move towards the same goal. Executives who are tempted to ignore employee motivation and alignment in their cost reduction efforts should ask themselves the following questions:

- Are we sure we have all the solutions needed for cost reduction (e.g., outsourcing, discarding a business, headcount reduction, bonus cuts), or does the complexity of our problem require individual responsiveness and on-site problem-solving from our employees?
- Will mandated cost reductions be undermined without positive support from employees? Will rational compliance be enough to sustain the behaviors we need, or do we also need emotional commitment?
- Will cost reductions damage our value proposition to employees, relative to our competitors? Are we in danger of forcing short-term actions that we will regret when our company is growing again?
- Are innovation, collaboration, and customer empathy critical in our business, at the level of requiring the energy and enthusiasm of our employees?

In most cost reduction efforts, employee motivation will be a critical business objective that executives, as well as front-line managers, must personally lead in consistent ways.

Motivating – Getting People To Do More Than What You Ask

Positive motivation is not about engaging people broadly at a company-wide level while compelling them at their work stations to do what you prescribe from the top. It is about energizing employees to work with you on reducing costs, encouraging individual employee actions that cannot be prescribed, and recognizing employees with more than money when they take these actions. For example, Amazon.com perpetuates a “door desk” award that is given on a monthly basis to an employee who achieves significant savings. The door is not worth much money and it symbolizes the makeshift desk that Jeff Bezos used as a thrifty measure in the early days. Generating positive motivation is seldom easy to and it rarely depends on money alone. People have to feel good about tasks that are not financially rewarding or intrinsically motivating. This requires developing emotional commitment to support painful decisions, applying self-disciplined behaviors beyond mandatory processes, building peer respect and support for reducing any and all costs employees can control, and making sure the informal organization supports the formal.

Motivating Cost Discipline

Reliant Energy, a Texas-based electricity provider, significantly reduced its cost base by integrating critical leadership objectives with a positive motivating approach to get the best of both the mandating and motivating approaches. In October 2002, Reliant’s stock was trading at less than a dollar, compared to \$30 at the time of its IPO in May 2001. The company grappled with debt from major acquisitions and the uncertainties of a deregulated Texas energy market, was rapidly losing the confidence of Wall Street, and faced bankruptcy. But in two years, Reliant turned itself around by cutting \$340 million in operating costs out of a base of approximately \$1.3 billion. The urgency of Reliant’s situation certainly made these changes mandatory.

At the same time, Reliant saw a twenty percent lift in measures of both employee satisfaction and pride.

What is it that Reliant and other successful cost-cutting “motivators” do that allows positive feelings to counter-balance negative fears?⁵

Leadership Cohesion & Commitment

“Motivators” establish leadership cohesion and commitment at all levels, conducting a fair process for cost reductions. Reliant leaders were aligned and united in the task of significantly reducing the company’s cost base and were highly visible in communicating both formally and informally after committing to a thirty-five percent reduction in costs. Senior executives recognized that motivation was a critical issue from the start. For instance, their “brown bag” lunches with employees became known as venues for candid discussion and underscored what leaders and employees were trying to do: talking and acting together—with integrity—to achieve what needed to be done.

Importance of Fairness

“Motivators” recognize that employees care deeply about fairness—which means making the cost reduction process transparent, timely, and effective. Reliant balanced a central mandate with a significant amount of local autonomy. Different groups were allowed to pursue savings on their own schedules, subject to an overall corporate timeframe. Similarly, BMC, a leading software company, developed a turnaround plan with milestones and a scorecard on its top five priorities, including cost reduction and a monthly report out to the whole company.

The Emotional Case and Role of Frontline Motivators

“Motivators” create a positive emotional case in addition to a rational business case. Both need to be clear and well reasoned. Companies need to develop an emotionally appealing theme as well as deciding on the primary carrier or carriers of that emotion through facts, not guesswork. Reliant conducted a survey of its employees in 2002 and learned that the two most important potential sources of pride were the company’s reputation—and the quality of its people. That became the basis of a well-organized change plan. The most effective cost-cutters also enlist the best frontline motivators, collectively as well as individually, to connect sources of pride to the work itself in ways that mobilize the organization. Reliant established “Motivation Governance,” including a Motivation Champion, a Motivation Squad, and most critically, Local Connectors. These Local Connectors were selected from interviews and peer nominations and were responsible for carrying out motivation activities locally (e.g., celebration events for achieving company objectives), as well as providing frontline perspective and upward feedback to the Motivation Champion.

More Than One Hammer

Executives require objective data to make critical decisions around where and how to cut costs. Multiple approaches are required to get everyone onboard. Too often, companies adopt one method (e.g., benchmarking) and impose it on the organization, ignoring the complexity of what might be driving costs. As one executive said, “You need more than one hammer.” For instance, costs are often driven by organizational inefficiencies, such as too many layers or too many hand-offs. Employees know this, and want these issues examined. Employees also want to be involved in the problem-solving. In 1993, Texas Commerce Bank hosted hundreds of focus groups that involved almost half of its 9,000 employees in a major improvement initiative that replaced its monetary target with an aspiration of “eliminating what annoys our bankers and customers.”⁶ The initiative eventually exceeded the initial target of \$50 million in reduced costs, achieving savings that were around three times the target. It is critical to do the analysis to shed light on a broad set of opportunities and to use the findings to design organizational solutions that create lasting behavior change. At Scholastic, there was a need to create a shared services organization to better manage and leverage spend across several business units. Rather than creating an expensive new organization with the associated hand-offs, the company created a council with clear authority and the right balance of membership.

Getting Through a Recession Requires “The Best of Both”

Mandates have their place in serious cost reduction efforts, but you also need “a little help from your friends” down the line. Cost-cutting has never been easy but companies will increase their chances of success by involving their employees in ways that obtain positive emotional commitment to decisions and behavior change. You may be able to mandate your way to an immediately lower cost structure, but if you also motivate people in positive ways that produce emotional as well as rational commitment, we believe strongly that you will get more costs out sooner, and the benefits will be more lasting.

Endnotes

¹ Managing Overhead Costs, Suzanne P. Nimocks, Robert L. Rosiello, and Oliver Wright, McKinsey Quarterly, May 2005

² Cost Transformation Driving Results, Archstone Consulting, 2008

³ Al Dunlap, corporate downsizer, was known for his aggressive approach to cost-cutting in the 1980's and 1990s but his methods were ultimately viewed as unsuccessful, culminating in his termination as CEO of Sunbeam in June, 1998; Al Dunlap at Sunbeam, Harvard Business Review, 1999

⁴ Engaged Employees Drive The Bottom Line, ISR-Towers Perrin, July 2006

⁵ The Reliant example is excerpted from the book The Informal Advantage by Jon Katzenbach and Zia Khan, which will be published in 2009.

⁶ Real Change Leaders, Jon Katzenbach and the RCL team, 1996

About the Author

Jon Katzenbach is a Booz & Company senior partner in New York. He is one of the co-founders of Katzenbach Partners LLC and has expertise in helping clients mobilize their informal organization to realize performance advantages.

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