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**A large quantity of research shows that in many instances layoffs can actually hurt companies more than they help them.**

# The Downside of Downsizing

By ANN CARLSEN

**IT'S ALMOST A KNEE-JERK REACTION. A COMPANY** watches as an economic crisis descends, or it experiences disappointing financial results. And as a result, it jettisons hundreds, if not thousands, of highly trained, experienced and dedicated workers.

It's sometimes hard to fathom that downsizing is a relatively new strategy that never even had a name until the inflationary, post-Watergate days of the Jimmy Carter Administration. Yet much is being written these days about the high costs and negative impact of downsizing. Sifting through these reports, we at Carlsen Resources have come up with seven harsh truths about corporate layoffs.

#### Layoffs may hurt stock prices.

Layoffs were once the darlings of Wall Street, but no more. Newspaper reports in 2008 offer the following insights:

- JP Morgan Chase announced a 10% cut in its workforce, and then watched its stock tumble 15% within days of the announcement.
- The very week that Mattel began instituting a 2.9% rollback in jobs, its stock dipped 17%.

- The same month that Dell finished laying off 9,000 employees, its stock tumbled 25%.

In addition, a 2001 study by the Harvard Business School analyzed stock performance in the 12 months immediately following layoffs and determined that the most drastic cuts resulted in sinking stock prices. The study concluded that businesses that laid off 3% or less of their workforces did just as well on the stock market as those with no layoffs at all. In fact, both groups analyzed in the study posted 9% share price increases, on average. Share prices remained flat at companies that let go 3% to 10% of their employees. And prices plunged an average 38% at companies that laid off more than 10% of their workforce.

#### Layoffs do not increase productivity.

A recent *Newsweek* story cited data from the Census of Manufacturers following layoffs that began in the late 1970s. From '77 through '87, companies that enjoyed the greatest increases in productivity were just as likely to have added workers as those that downsized.

What's more, when any organization engages in layoffs, especially in hard times, many employees cease to be involved in their work.



*Many of the recent layoffs appear to be a result of bad management, Ann Carlsen asserts.*

They're not as vested or committed to the company's success.

A recent Gallup Poll, which surveyed workers whose organizations had laid off employees, showed that 17% of the respondents were trying to subvert the corporate mission and/or were completely disengaged. And nearly 50% said they were actively looking for a job change.

**Layoffs usually do not increase profits.** One study of firms in the S&P 500

determined that companies that downsized remained markedly less profitable than those that did not. And in a recent American Management Association survey, slightly less than half the companies reported that downsizing increased profitability, while only a third said it had a positive impact on productivity.

And if one believes in the link between employee attitude and performance, consider the following: Sears, Roebuck and Co. once quantified the correlation between employee attitudes, customer satisfaction and profit-

ability. Though the findings are now 20 years old, they should be heeded: for every 5% increase in employee commitment there is a 1.3 increase in customer satisfaction, which results in a .5% increase in revenue.

**Layoffs are often a byproduct of bad management.**

Matching the size and abilities of a company's workforce to the short and long-term demands of its target market has always been a benchmark of good management. But there seems to be an awful lot of layoffs these days that, in all candor, must be chalked up to bad management. Of all the factors that go into making up a bad executive, four stand out. The first is ego. It is certainly not hard to imagine the CEO who says to himself, "If Jack Welch could do it at General Electric, why can't I?"

Secondly, there's the issue of laziness. When Aetna purchased U.S. Healthcare it immediately laid off 4,400 workers. Aetna then fell so far behind in processing claims that it not only lost its ability to track costs for a full quarter, it did irreparable harm to many of its provider and customer relationships.

Why? As *Slate* magazine wrote, "It's easier to look at the reduced labor costs from cutting 4,400 jobs than it is to anticipate the potential chaos those cuts will bring."

Thirdly, there's lack of courage. There are many stories of CEOs who responded to critics and short-term investors, not by articulating a vision for the company and then executing it, but by announcing layoffs and then holding aloft the scalps of the departed as a sign that the company was now in good hands.

And lastly, there is greed. In a recent blog posting, noted business writer and managing director of the Solleva Group, Erik Van Slyke, offered a cautionary tale about a friend who attended a monthly meeting of top officials at the multinational firm where he worked.

"The CFO was first on the agenda. After a review of the numbers, he made this statement: 'As all of you can see, we are only slightly behind our projections. All things considered, we have weathered the storm well. The challenge we have for the remaining six months of the year is that if we want to make sure we get full bonuses, we need to make a 5% headcount reduction. A 2.5% reduction will get us to 80% payout, but a 5% reduction should get us to 100%.' The overwhelming sentiment in the room was to move forward with the 5% reduction."

After Van Slyke's friend protested and was

## LAYOFFS DO NOT CUT COSTS

In his book *Responsible Restructuring*, Wayne Cascio details the direct and indirect costs of employee layoffs. And he does so in a way that, it would seem, few companies have ever thought to consider. Among the items on Cascio's long list of costs that must be measured against projected savings are:

- Severance pay;
- Accrued vacation and sick pay;
- Outplacement costs;
- Higher unemployment-insurance taxes;
- Expenses related to rehiring when business improves;
- Low morale among survivors;
- An exodus of talented, most-likely-to-be-poached survivors;
- Potential lawsuits;
- Sabotage;
- Loss of institutional memory and knowledge;
- Reduced productivity.



## **JP Morgan Chase announced a 10% cut in its workforce, and then watched its stock tumble 15% within days of the announcement, according to press reports.**

rebuffed, he said he began to dream of selling hotdogs on the street.

### **Layoffs can eat away at the core of the strongest brand.**

For companies committed to quality service, their employees are their brand incarnate. And the more disgruntled those staff members become, the more their attitudes will negatively impact the corporate brand.

Any company that treats its people as little more than cost centers must be willing to live with the consequences. These include gaining a reputation as a bad place to work and to do business. And such a reputation, thanks to the blogosphere, YouTube and social media, can go viral overnight and spread unchecked for months.

### **Layoffs are slowly killing the U.S. economy.**

In a sad bit of irony, it's possible that Corporate America's 30-year love affair with layoffs will end up being recognized as the single most important reason we ceded our role as the world's leading manufacturer of durable goods – and why we eventually found ourselves in one of the deepest and most protracted recessions in history.

Granted, we are now operating in a global economy, and because of that some loss of jobs, deceleration of wages and off-shoring of job functions should have been expected. But in their zeal to cut costs and maximize short-term profits, many companies failed to consider a deeper consequence: the collective impact of their cost-cutting has gutted the buying power of the people they rely on for survival – ever-aspiring and always-hopeful American workers.

A recent *New York Times* article detailed how, for years, U.S. recessions were always followed by a 21-month period during which

the economy slowly but surely added back the jobs it lost.

What's more, during the post-war periods of the '50s, '60s and '70s, the private sector added new jobs to the tune of 3.5% a year. By 1990, however, things started changing.

Following the '90 recession, for example, the economy took 31 months to recover its jobs. And following the '01 recession, it took 46 months. The yearly growth recovery of those last two recessions was also lower: an average 2.4% after '90 and .9% after '01.

Will the growth statistic be more distress-

ing this time around? There's a good chance. And what should make this "jobless recovery" concept so frightening to all of us is the fact that the three industries that always led the U.S. out of its recessionary times – home building, automobiles and banking – were the hardest hit this time.

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