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C-SUITE ANALYTICS WHITE PAPER

Speak the CEO Language on Engagement & Retention: DOLLAR$!

Not everything that counts can be counted and not everything that can be counted counts.

Speak the CEO Language on Engagement & Retention: DOLLAR$!

By Dick Finnegan, THE Turnover Expert

Employee turnover and engagement across the United States is in great need of repair. Employee quits are at their all-time high, and according to Gallup employee engagement has not substantially improved this century. Deloitte throws salt on the would saying we spend an astonishing $1.53 billion each year to improve our stuck-in-the-mud engagement…or we might say we flush that amount. And should we want one more statistic to make this worse, this one is it:

Fewer new workers will enter our workforce this decade than anytime since the end of the civil war.

This paper answers three critical questions regarding the quest to improve employee retention and engagement in global companies of all sizes and industries:

- ✓ *Why* placing dollar values on turnover and engagement is your next important step
- ✓ *How* to place dollar values on turnover and engagement
- ✓ *What* to do with the data once you have it

The Financial Impact of Turnover and Dis-Engagement

Research tells us that employee turnover in the U.S. costs companies from 12% to 40% of pre-tax income, that the annual cost is $25 billion, and that turnover costs shareholders a full 38% of additional value in just 4 high-turnover industries. Dis-engagement costs are similarly striking as a one standard deviation improvement in engagement has been associated with $4,675 increase in revenue for each employee. For a typical S&P 500 organization, this amounts to $93.5 million. These aggregated dollar values are staggering.The purpose of this paper, though, is for you to apply mathematical calculators in order to determine the specific financial impact for your organization.

The Role of Dollar Values in Retention

If you are serious about cutting turnover, start by putting a cost to it to motivate every leader in your organization to focus on keeping good employees. Let me introduce Finnegan's Arrow℠, a similar process your company has in place to manage sales or service. We help companies reduce turnover by 30% or more in a year by implementing the following:

Whereas Stay Interviews have proven to make retention and engagement better because they enable leaders to build trust, Stay Interviews must be surrounded by traditional work processes to succeed. So Finnegan's Arrow directs organizations to place dollar values on turnover or engagement, establish goals for either or both, then train leaders to conduct Stay Interviews, and forecast future retention. Executives then hold leaders at every level accountable for two new metrics, performance against goals and forecasts.

Converting turnover…or engagement…to dollars is positioned first because it drives all of the resulting behaviors. Turnover is not just a percentage, nor is it a metric we can feel good about by way of external benchmarks. Turnover is instead likely to be the second- or third-greatest expense for many organizations.

Implementing each component of Finnegan's Arrow is essential for success. For comparison, imagine if your salespeople had similar cost studies, goals, training, and forecasts but no accountability. Few sales would happen.

What Specific Action Must CEOs Take?

The specific action CEOs must take is to hold managers on all levels accountable for improving the engagement and retention of their teams in meaningful ways. Let me explain why.

Think about the fundamental difference between the roles of the line or operating side of organizations and the staff side. In simple terms, the line side is charged with getting the primary business objectives done and the staff side helps. Let's use sales as an example. If your CEO wakes up and sees sales numbers are down, she then rings up the head of sales and tells him to improve them. He then tells his team the same message, and might contact a staff function for help with training or tracking. If the sales team subsequently improves sales, they go to Hawaii and the staff teams stay home. This is the way it works and the way it is *supposed to work.*

We know from research that that employee turnover is managed differently, though, and anecdotally the same is true for employee engagement. In various studies the highest percent of managers who are held accountable for turnover in meaningful ways is just 14%. Instead, executives take one of two paths: they either place HR in charge of retention or no one. HR's response is a full-throttle unleashing of employee programs including surveys, benefit reviews, brown-bag lunches, town hall meetings, improved newsletters, and employee appreciation week. These efforts are well-intended and provide small amounts of help, and are formed on a solid, basic premise: HR can lead managers to water but they can't make them drink.

Why Managers Matter

The crossroads decision executive teams must make regarding engagement and retention is this: Will we manage them as we do our other key metrics, in *process-driven ways?* Or will we manage engagement and retention with *programs?* Here's a short-cut to the right answer: *If you manage engagement and retention as you do your most important metric, you will manage them successfully.* You manage sales via skill-based hiring and defined sales goals, and then provide daily coaching, training, tracking, and ultimately positive and negative consequences. Do the same with engagement and retention and you will win.

Many studies tell us that direct managers are the single critical piece in improving turnover. Here are a few:

"If you have a turnover problem, look first to your managers"…Gallup

Primary reason for seeking a new job is disliking boss's performance…Yahoo

Employees stay for managers first and co-workers second…salary.com

Poor leadership causes over 60% of all employee turnover…Saratoga Institute

"When employees stay, it is because of their immediate managers"… National Education Association

Employees who stay primarily for their supervisors stay longer, perform better, and are more satisfied with their pay…TalentKeepers

Additionally, Kenexa gathered data from a large number of employees who had recently left their organizations and asked their opinions regarding pay, benefits, development, advancement opportunities, and their managers. The results were predictable; those who felt good about their managers felt better about the other topics and those who felt worse about their managers felt worse about them.

Kenexa concluded that "offering a higher salary or developmental/advancement opportunities may not be enough to retain employees".

Viewing all of this data from 10,000 feet brings a clear conclusion: *Employees' decisions to stay in their jobs and perform at their very best is greatly influenced by their relationships with their managers.* How much? More than half for certain and maybe way more. So solving engagement and retention with programs from HR alone is like treating disease with leeches…and failing to hold managers accountable for engagement and retention is a supreme lost opportunity.

Besides, when is the last time you heard a really good worker say, “My boss treats me like dirt…but I’m holding on for employee appreciation week”?

Lessons Learned From Finnegan’s Arrow®

Consider each of these concepts in sequence:

1. The most critical, controllable step to improving employee retention and engagement is giving employees a direct supervisor they trust
2. The absolute best trust-building invention is Stay Interviews
3. Executives are the key to driving accountability for retention with every leader in their organization.
4. Executives are far more likely to address retention and engagement as *business issues* when they first learn their costs.

How to Place a Dollar Value on Turnover

The first step is to establish a turnover cost team with representatives from HR, Finance, and at least one subject matter expert for the job you are costing. The most important member of your team, though, is your Chief Financial Officer. The Finance representative on your turnover cost team must carry the full confidence of the CFO.

Begin your meeting by discussing this quote from Albert Einstein:

> *“Not everything that counts can be counted,*
> *and not everything that can be counted counts.”*

The key points for agreement are (1) that the team and model will be used to develop the closest possible cost for turnover but there will be limitations, and (2) it is more important that executives agree to the cost than the cost is 100% accurate. Said another way, we will develop the best cost and ultimately all must stack hands on the outcome.

Eleven data points are required for the turnover cost model in order to develop the direct costs for exiting and hiring one employee as well as the lost productivity for both while that job is open and the new hire is learning the job. In this example we will calculate the cost of losing one nurse. You will see that the cost estimates are extremely conservative.

These first set of these data points provide fundamental job information and the direct costs of turnover:

1. Nurse annual average compensation & benefits for all positions **$85,000…$354.17 per day based on 240 workdays per year**

2. Annual average compensation & benefits for all positions: **$68,000**

3. Projected nurse exits this year **200**

4. Separation…exit interviews, administrative costs, separation pay **$100**

5. Vacancy…temporary help and overtime **$5,000**

6. Acquisition…advertising, agencies, employee referrals, travel, interviews, assessments, background checks, reference checks, physicals, bonuses, relocation **$12,900**

7. Placement…new supplies, onboarding days, training days **$4,250 based on 2 onboarding days and 10 training days**

Total direct costs: $22,250

Then to calculate lost productivity:

8. Annual revenue divided by the number of full-time equivalent employees **$240,000 based on Saratoga Institute data but insert your own data here**

9. Workdays per year **240 also based on Saratoga Institute data**

10. Average workdays position open **30 for our example but insert your own data here**

11. 50% workdays to total effectiveness **10 also for our example but insert your own data here;** this is the number of workdays typical employees need after full-time training days to become proficient in their jobs, divided by two since they are partially productive each day on an increasing scale

We apply this data to calculate lost productivity this way:

- ✓ We know the daily revenue per each full-time equivalent employee is $1,000 as $240,000 ÷ 240 = **$1,000**
- ✓ We also know the daily revenue for nurses is **$1,250** as nurses earn 25% more than average employees, **$85,000** per year in salary and benefits versus **$68,000** per year for all employees
- ✓ From this data we can multiply each nurse's daily revenue value of $1,250 X the number of days the position is open which is 30 and we then know the lost productivity while the position is open which is **$37,500**
- ✓ And using the same calculation for the lost productivity for the 10 days of ramp-up time while the new nurse is learning the job, there is additional lost productivity of **$12,500**

So the total *gross* lost productivity is $50,000

Two values must be subtracted from the gross lost productivity to ensure accuracy:

- ✓ The salary and benefits saved during the 20 days the job is open results in a credit of **$10,625**
- ✓ And the vacancy costs of **$5,000** for temporary help and overtime must also be credited as these dollars were invested to reduce the amount of lost productivity

So the resulting *net* lost productivity is $34,375

By adding the direct costs and lost productivity, we learn the cost of losing one nurse which is…

Direct Costs	$22,250
Lost productivity	34,375
Total cost for losing one nurse	**$56,625**

Recalling that this organization will lose 200 nurses this year, the annual cost of nurse turnover is

$56,625.00 X 200 = $11,325,000

Savings for reducing nurse turnover 20% = $2,265,000

Savings for reducing nurse turnover 50% = $5,662,500

Our C-Suite Analytics' team has helped scores of clients use this model to determine their turnover costs. The great majority of clients and their CFOs have accepted the model as a fair representation of turnover's costs. The few who did not suggested that their organizations do not lose productivity while jobs are open because others fill in. The obvious remedy, then, is to calculate the cost of the extra people whose positions have been established to fulfill the work when positions are open and new hires are ramping up due to turnover. This total annual cost can then be divided by the number of employees who exit in one year, and the resulting value can replace the costs for lost productivity in the model.

Finance employees might have data that supersedes the model. For example, most organizations know the daily value of salespeople so they can easily calculate the lost dollars while sales jobs are open and new hires are ramping up, and these dollars should replace the lost productivity dollars that the model will produce. Here are three other examples of job-specific studies that provide helpful data:

- ➢ Brokerage: A study indicated that more than half of brokerage clients changed companies to follow a broker who left so what is the real turnover cost?
- ➢ Fast Food: Taco Bell found top 20% stores for retention had double sales and were 55% more profitable; without this data we would assume the cost of losing one fast food employee would have been less than $1,000 but it appears turnover's cost is exponentially higher when aggregated across just one store
- ➢ Call Centers: In a study of an outbound center, the costs of lost productivity due to turnover are 4.4 times the direct costs

Putting Turnover Cost Data to Work

The primary goal of putting dollar costs on turnover is to enable the senior leaders to drive accountability for retention. So making right decisions on how to *apply* this data is as important as generating this data.

One way to put turnover cost data to work is to incorporate it into monthly reports that include actual turnover, performance against turnover goals, and turnover's cost...both by organization and by manager. This data will lead to better decision-making regarding which managers to reward, to promote, and ultimately which managers to retain. And whereas the performance-against-goals data provides a quick look at each manager's performance, the cost data spurs urgency for addressing areas where turnover is high and improvement is required.

We've helped some organizations design reports that contained the total cost of turnover each month for *all* positions. The method for doing so is to group jobs together that have similar turnover costs based on key factors such as pay, length of time jobs stay open/training days/ramp-up time, and other factors that significantly impact turnover's cost such as whether your organization pays relocation costs or hiring bonuses to new hires. Typically all jobs can then be banded into five to eight groups and each job is then assigned one of those five to eight pre-determined costs. Then HRIS systems or excel spreadsheets are prepared to report turnover by aggregated cost.

Another way to put turnover cost data to work is to incorporate the actual dollars into company planning. For example, a major hotel chain determined they were spending $350 million on turnover each year and that cutting turnover in half would increase stock price by nearly 25%. Imagine the high energy and constant reporting that resulted among the CEO and this company's board of directors once this correlation was announced.

Cost data can also be used when considering a new benefit or pay strategy. Estimates of employees saved or lost can now be quantified and the resulting discussion becomes richer when deciding on major policy initiatives.

Placing A Dollar Value on Engagement

There is little data regarding how much engaged versus disengaged employees impact your bottom line, but one study opens the door to developing organizational and department calculations. This study was conducted in 2007 by Watson Wyatt which has since changed its name to Towers Watson. The study compared engagement scores and company revenue over a period several years and declared the following:

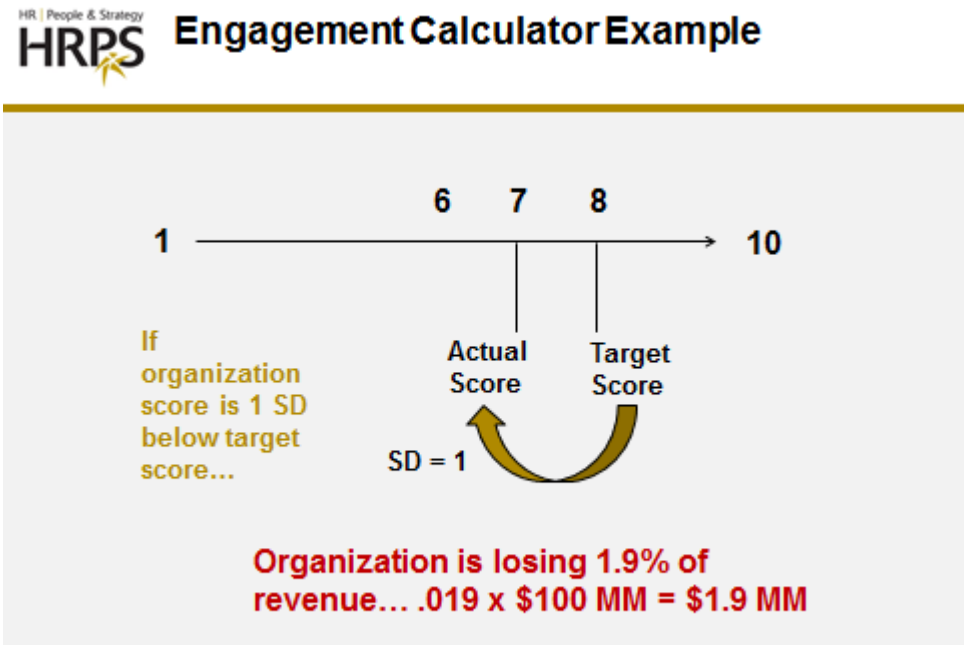
"Watson Wyatt analyses show that a significant improvement (one standard deviation) in employee engagement is associated with a 1.9 percent increase in revenue per employee."

"Debunking the Myths of Employee Engagement", Watson Wyatt…now Towers Watson, 2007

The breadth of this study provides a statistical basis we can apply so let's consider this example. If an organization…

- Earns $100 MM in annual revenue
- Conducted an engagement survey that reported scores on scale of 1 to10
- Their targeted score was 8
- Their actual organization score was 7
- And the distribution of scores indicated a standard deviation of 1

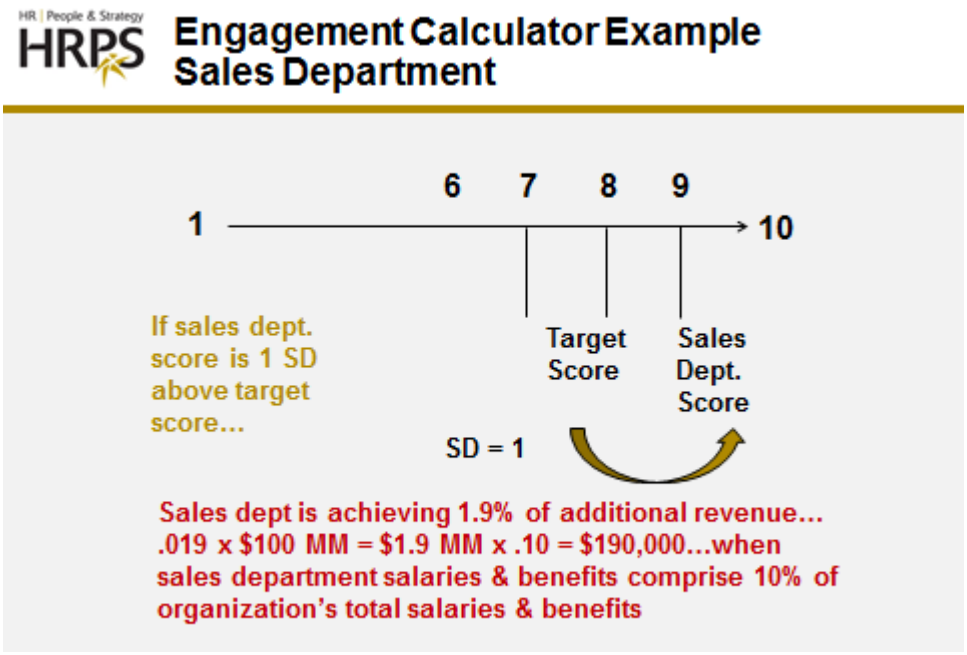
Then we can chart their outcome in the following way and apply the formula to determine their engagement survey impact in dollars:



As the graphic indicates, this organization lost 1.9% of its annual revenue because its overall survey score was one standard deviation *below* its targeted score, losing a total of $1.9 million. These are dollars completely left on the table, dollars that CEOs and most CFOs would not consider when reviewing employee survey results.

Let's now use this same formula but adapt it to one department within this organization and our example will be the sales department. Here's the scenario:

- This is the same organization and it earns $100 MM in annual revenue
- It conducted engagement survey that reported scores on scale of 1 to 10
- Their targeted score was 8
- Actual sales department score was 9
- Distribution of scores indicated a standard deviation of 1
- The sales department's salaries & benefits are equal to 10% of the organization's total salaries and benefits



This graphic tells quite a different story. Because the sales department's score was one standard deviation *above* the targeted score, their dollar value is positive rather than negative. The formula to determine this value begins the same way as we calculated for the entire organization by determining the dollar value for the total company if it had achieved this score of 9, and in this example that value is a positive $1.9 million. Next we multiply the *company's* engagement value that would result from the company scoring 9 which is one standard deviation *above* the target, by the percentage of company compensation and benefits that is paid to the sales department which is 10. The mathematical equation is:

> Company Value (+$1.9mm) X (sales department compensation & benefits ÷ company compensation & benefits which is 10%) = $190,000

The result is that the sales department is bringing in $190,000 of revenue entirely because the employees there are more engaged in their work than the level for which the company set its target. This $190,000 is in addition to the expected performance of the sales department.

Why did we use each department's total compensation and benefits to determine their engagement values rather than their number of employees? Because some departments have a greater impact on revenues than others, and the model assumes that top management designs compensation to reward those who impact revenues the most. Referring back to our example, an administrative department could achieve the same survey score as the sales department and might also have the same number of employees, but a logical assumption would be that that sales team would have a greater impact on revenues than the administrative team. The model accommodates this assumption.

Our examples are designed to use simple computations to make understanding clear. Most standard deviations will not be whole numbers but they will work just as effectively in this model.

Does the Engagement Cost Model Really Work?

Well-respected professionals attest to the validity and value of our engagement model. Here's one testimony:

> *"The C-Suite Analytics Engagement Calculator is a welcomed, one-of-a kind tool to help organizations fully grasp the value of engaged employees…as well as the huge number of dollars left on the table when employees don't give their best. Perhaps its greatest value is that it distinguishes managers who influence engagement from those who do not, in specific dollar values.*
>
> *This calculator is based on broad-based research and its algorithms have a solid statistical foundation. It can work with any engagement survey and assumes that survey measures engagement in a valid way."*
>
> Dr. Gary Borich, Ph.D
> Endowed Fellow, Quantitative Methods Program
> The University of Texas at Austin

How Should You Apply the Engagement Calculator's Resulting Dollar Values?

Recall that our objective is to influence your executives to hold all managers accountable for achieving engagement & retention goals. Step number one, then, is to include engagement values in engagement survey reports. Once executives see in these reports that their organization and each individual manager has now achieved a positive or negative dollar value based on their team's levels of engagement, ask your executives to take the following next steps:

1. Establish engagement goals for each manager for the next engagement survey

2. Survey employees quarterly or at least more frequently than once per year in order to track whether managers are improving their scores; quarterly surveys can be conducted with samples of employees as long as each employee is included each year

3. Challenge each manager's survey improvement plan to ensure it contains skill improvements for that manager and all subordinate managers rather than relies on program fixes alone to increase scores

4. Coach managers who consistently fail to meet their engagement survey targets and if necessary remove them from jobs that require managing people

Earlier I said you will improve retention if you develop processes that mirror sales and other top metrics in your company. You will improve engagement *if you treat employees as you treat your customers* so consider these questions: Would you continue to employ a manager who consistently fails to meet customers' expectations? And would you wait a full year after a disappointing survey to survey again?

Note: The employee turnover calculation suggested here is now available for use at https://c-suiteanalytics.com/cost-calculator/.

Want to retain more of your employees? Get started today.

Call THE Turnover Experts at 844-RETAIN-U or 844-738-2468;
or email solutions@c-suiteanalytics.com to learn more.

CEO Dick Finnegan has been cited by Forbes, BusinessWeek, Chief Executive Magazine, Fast Company and Consulting Magazine as the leading thinker on employee retention. He welcomes your comments at DFinnegan@C-SuiteAnalytics.com.

Data sources are available upon request. More resources available at https://c-suiteanalytics.com/resources/.

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