Human Resources Management in a Recession: A Portfolio Management Perspective

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Human resources professionals often struggle to obtain the resources they need to effectively manage people in the workplace, and the difficulties that they face are augmented when economic conditions worsen. The current global recession has caused most companies to review their allocations of resources more critically and as a result, organizations of varying sizes have laid off a significant number of workers at all skill levels, putting the American unemployment rate at its highest since 1983 (Bureau of Labor and Statistics, 2010). As human resources departments try to keep their remaining employees engaged, motivated, and appropriately trained, they face many challenges including reduced human resources staffing levels and program funding, psychological hardships for workers dealing with the crisis, and employees with different generational mindsets and priorities. These and numerous other difficulties make it difficult for human resources managers to not only manage their people through the downturn but to ensure that their companies are adequately staffed with talent when economic conditions improve.

In this paper, I review the primary unique challenges that human resources managers face as a result of recessionary conditions and provide recommendations for not only surviving the recession but ensuring that an organization is ready to compete when expansion returns. I propose that employers manage their human resources processes using an “investment portfolio” approach whereby they allocate their scarce funding for human resource programs during a recession and afterwards to those initiatives that provide the greatest financial rewards. By measuring the benefits obtainable from investment in distinct “projects,” employers can ensure that the financial resources they allocate to human resources initiatives provide them with excellent returns as well as strategic advantages over their competitors.
Introduction

The economic recession that began in the United States in 2007 has created significant uncertainty for American businesses and laborers as tightening credit markets, a burst of the housing “bubble,” and a financial markets collapse have not only caused employers to analyze their cost structures but to ask, “when will it be safe to invest again?” Though corporate spending is increasing and the gross domestic product is expanding (Bureau of Economic Analysis, 2010b), many companies are hesitant to hire again until they have experienced several quarters of improving economic conditions and the outlook for their businesses is less volatile. This means that the unemployment rate is unlikely to contract significantly in the near future; in fact, the unemployment rate, which stood at 9.6% as of November 2010, is projected to fall to only 9% by the end of 2011 and 8% in the following year (Irwin, 2010). In addition, many companies have cut spending for their current employees, often one of the first line items slashed in budgets during difficult times, and are less likely to significantly increase wage rates, spending on employee benefits, and investment in recruiting and training and development programs until their financial pictures become clearer.

These difficulties place constraints on a human resources (HR) manager’s ability to effectively manage his people in all aspects of the HR function. Uncertainty in business performance as well as in the labor market provides a HR manager with challenges in predicting both demand and supply for labor. When recruiting budgets are reduced, hiring managers can struggle to effectively find talented employees when they need them. Smaller training and development budgets can impair an employee’s ability to obtain the requisite knowledge and skills to effectively perform his assigned tasks. Employers are faced with questions, both practical and ethical, regarding the appropriate level of compensation for current and new employees. Though many companies face these problems even in prosperous economic times, they are intensified in times of economic decline.

In this paper, I describe the most significant impacts of today’s economic recession on HRM processes in the United States. I discuss this issue in two contexts: (1) how the downturn’s impact on individual employees affects a HR manager’s ability to effectively manage those employees and (2) how the downturn’s impact on a HR manager’s employer constrains his ability to manage people. Within each context, I discuss the impacts of a recession on the processes of strategic HRM, including HR planning and the design of jobs and work systems and the impacts on four fundamental functions of HR: staffing, training and development, performance management, and compensation (Mello, 2006). It should be noted that restrictions placed on HR managers during one stage of the HRM process often impact other stages as well. For ease of discussion, I avoid repetition except in those instances where a problem causes distinct effects on individual HR functions.

After discussion of the impacts of recessionary pressures on HRM, I provide recommended solutions, based on past best practices and innovative strategies discussed in recent texts, to these unique problems within an investment-focused framework. I also address how these practices can provide an employer with a unique competitive advantage over other companies.
The Recession’s Impact on Individual Employees and Related Impacts on HRM

The current U.S. economic recession has many impacts on American workers, most notably a significant rise in unemployment that leaves many people searching for jobs. Additional effects such as a lower individual net worth are reasonably evident, while others such as decreased employee motivation from a generally bleak living environment are not clearly visible to an employer but can have a dramatic impact on worker performance and in turn, a company’s success. These problems influence a company’s people management effectiveness in various stages of the HRM process.

HR Planning

Economic uncertainty influences the process of HR planning as managers attempt to accurately predict the labor supply available to the company for meeting its employment needs. To estimate job transition probabilities, many employers have historically used predictive mathematical techniques that rely on historical data regarding turnover in specific positions. Predictions derived from such modeling may no longer be relevant in situations where new factors impact employee availability. As individuals face the prospects of declining values in their homes and investment portfolios and, in a period of extremely low interest rates, declining returns on even the safest investments, traditional voluntary turnover rates may be impractical indicators of future employee attrition, as workers may be less likely to find an appealing job outside of the organization and older employees are more likely to postpone retirement (“Balancing Cost Reduction,” 2009). Such financial impacts can also have an effect on current employees’ availability to work. For example, a non-exempt employee may desire to increase his income by working more hours which, in addition to impacting labor costs, can provide for added variability in his employer’s available labor hours. Alternatively, an employee may desire to work a second job in order to increase his wages, which can have an impact on his first employer’s labor pool if, for example, he is no longer available to work overtime because of his new commitment.

When forecasting the adequacy of the labor supply, employers should also consider the number of people actually choosing to participate in the labor force. Many Americans will decide to seek further education when times are tougher, though there is varying evidence regarding the magnitude of related impact on national labor resources. While the labor force participation rate, the ratio of both employed and unemployed people to the national population, decreased only 1.0% in 2009, the declines among 16 to 19 year-olds and 20 to 24 year-olds were 3.1% and 2.8%, respectively (Hipple, 2010). This suggests that typical first-time job seekers are delaying entry into the workforce for educational or other reasons. Alternatively, tightening credit and economic necessity could force people to enter the workforce more quickly than they would during an economic expansion, as Harvard University economics professor Claudia Goldin suggests (Tucker, 2009). In addition, an experienced employee may be more motivated to return to school during a time of economic uncertainty and perceived job insecurity in order to become a more marketable employee. A HR manager should consider the potential impact that each of these
trends may have on its workforce availability, specifically as they relate to the company’s unique industry or to its individual job openings.

Diversity planning also has its unique challenges during a recession. During the current recession, unemployment for men has increased at a greater rate than for women, resulting in the largest unemployment gender gap since World War II (Sahin, Song, & Hobijn, 2010). In addition, the magnitude of increases in the unemployment rate varies among ethnic groups as well as for employees considered “disabled” and those who are not (Hipple, 2010). Conversely, a disturbing trend has recently developed in the legal profession, where anecdotal evidence suggests that a disproportionate number of employees laid off during the recession have been women or minorities (Taylor, 2009). In addition, Citigroup was recently accused of discriminatory practices in its management of workforce reductions during the recession (Neumeister, 2010). As a result of these various trends, the diversity of an employer’s available job applicant pool may be significantly different than it was during prosperous times, and therefore, an employer may find it increasingly difficult to maintain a workforce with the diversity it desires.

Work Systems and Job Design

J.R. Hackman’s and G.R. Oldham’s Job Characteristics Model suggests that an employer should design jobs in such a way that the characteristics of the job will enhance the employee’s behaviors and ultimately workplace outcomes (1974). A critical component of this strategy for effective job design is the employer’s understanding of its employees’ critical needs for satisfaction in their jobs. While it is often difficult for HR managers to identify employee needs beyond reasonable practical considerations such as a living wage, this task is made even more complex during difficult economic times. In recessions, individuals face financial hardships from decreased net worth, a spouse’s job loss, or financial difficulties among their friends or family members who may suddenly become dependent on the employee himself, each of which places pressure on the employee to increase his earnings. In such situations, an employee may concern himself more with compensation than with other job factors such as task variety, job relevance, or balancing hours spent at work with those spent with his family.

HR managers should consider that financial needs are not an employee’s only focus during a recession, however. Bates (2009) surmises that employers often have misconceptions about what motivates employees during a recession. She suggests that employers focus too often only on compensation as a motivating factor, while employees are primarily concerned with recognition and learning opportunities even in the face of such hardship (Bates, 2009). While motivating factors are certainly specific to the individual, this insight could prove useful to HR managers in their attempts to design work processes that enhance employees’ workplace motivations.

There may also be unique differences among workforce generations to consider when identifying motivating employment factors. Hauw and Ans Vos (2010) suggest that millennials lower their expectations regarding a work/life balance in a recessionary economy but maintain high expectations for compensation, training and development opportunities, and meaningful work assignments. While employers can expect millennials to have a continued dedication to work
during an economic downturn, the results of this study also suggest that employers must find ways to meet the high reward expectations of such employees. This includes ensuring that job dimensions include high levels of task significance and an autonomous working environment for the millenial employee. Employers may need to consider the complexities that generational differences bring to the task of job design, particularly in situations where members of different generations currently work in the same or similar roles. These differences can also cause conflict between individuals in different jobs that significantly interact with each other, resulting in a different prioritization of tasks for people working toward common goals, such as in team-oriented work situations.

**Staffing**

Persisting recessionary economic conditions can dramatically impact the recruiting and selection processes of an organization. When general unemployment is high, the employer’s potential external labor pool is typically larger, presenting both benefits and difficulties to the hiring manager. The most distinct advantage to a larger pool of applicants is the likelihood that there are more “high-potential” employees, the organization’s most valuable personnel resources, available than when labor markets are tight. Unfortunately, there is a conflicting challenge that employers must face: because the labor pool is larger, they must determine how to filter out the best-performing job applicants from the rest of the applicant group.

Unique questions arise in regard to the education of potential employees and how it affects a company’s ability to match its open positions with the appropriate people. As discussed previously, when poor economic conditions persist, individuals may be more likely to continue their education one level further than they might when jobs are plentiful. Those looking for meaningful work and opportunities for advancement, such as millenials, may opt to pursue further education in lieu of taking positions that do not offer these benefits.

There also tend to be dramatic shifts in which fields of study Americans pursue during a recession. Many people by nature are more likely to pursue opportunities in fields that they perceive to offer more stability or growth in the future. For example, despite the significant rise in general unemployment during this recession, a 2009 survey released by the American Society of Mechanical Engineers notes that the median base salary for engineers increased 9.4% over the preceding twelve-month period, with the greatest percentage increase coming from non-licensed, less experienced workers (Hansen, 2009). Research-savvy students who consider available employment surveys like this will likely gravitate toward fields of study where jobs are plentiful, qualified labor is scarce, and salaries and other compensation benefits are high. HR managers who work for companies in those related industries will find a greater pool of potential applicants available, while those operating in contracting or more volatile industries may find that their qualified labor pool does not meet their needs.

Because recessionary pressures can impact a HR manager’s ability to effectively recruit externally, he might find it more appealing to focus staffing efforts on those who are already employed within the organization. Even promotional efforts can be complicated in a downturn,
however, as the desire for greater compensation drives more workers to seek fast advancement and results in an increase in the number of internal candidates for promotional positions. As a result, the applicant pool may include a greater number of unqualified workers. With an increase in employees interested in but not receiving the promotion, the company may experience a higher level of employee discouragement or even voluntary termination as well.

**Training and Development**

An increase in general unemployment presents an employer with unique questions in regard to orienting and training its employees as well as providing them with useful career development opportunities. Because of the difficulty that a company may have in filtering out the best available employees from its labor pool, a HR manager may be inclined to delay training and development educational opportunities until it is surer that its new hires are an appropriate fit with the organization and their specific roles. In addition, because employees may be less likely to leave since the general job market provides fewer opportunities outside of the organization, a company may need to consider whether it should restructure current development programs to cover a greater number of people or to focus on a more discrete population of potential leaders.

**Compensation**

In a recession, HR managers may find it difficult to design compensation programs that adequately provide employees with an equitable level of compensation and an incentive to perform effectively. From an economic perspective, it may be more difficult to identify appropriate market comparisons for wage rates when the supply of and demand for labor are more volatile. In addition, an employer may be faced with an ethical dilemma in setting compensation levels; though the perception may be that employees should feel lucky just to have a job when unemployment is high, should an employee institute wage freezes or make “low-ball” offers to new employees in order to reduce labor costs? Alternatively, a socially responsible employer may be incented to offer employees more compensation in difficult times to assist them in maintaining their usual standards of living. In addition, as voluntary turnover generally decreases during a recession (deWolf & Klemmer, 2010), a company may not replace as many employees with new, first-time employees who often demand a lower wage than experienced employees, which places added pressure on a company’s ability to manage its labor costs.

In addition to these practical matters, an employer may find it necessary to restructure its direct compensation programs due to changes in motivational factors for employees. This could include shifting the balance between base pay and incentive pay, as some employees will desire a greater percentage of their income to be stable during uncertain economic times. Unfortunately, making such a change could reduce the incentive of other employees to maintain productivity. It should also be noted that frequent changes in compensation processes can become administratively burdensome to employers and might also lead to employee confusion regarding prioritization of their objectives.
A recession can also have an effect on the indirect compensation that an employer considers providing to its workers. In addition to providing greater benefits as a form of altruism, an organization may find it beneficial—or even necessary—to provide increased health benefits to employees. During an economic downturn, employees may develop a general melancholic attitude because of the significant media attention given to the situation or impacts on friends and loved ones. A recent survey of employers found that workers are more likely to have increased stress levels and ultimately more common occurrences of sickness leading to absence from work during a recession than during other times (Paton, 2010). As such, HR managers may need to consider the adequacy of their health and welfare benefit programs, and the costs of employee benefit claims may increase with greater levels of stress and resulting illnesses.

**Performance Management**

A company’s performance management process is impacted during a recession primarily by the same factors that influence a company’s job design, training and development, and compensation processes. When employee needs become more volatile and their motivations change, employers must adjust their methods for assessing employee performance and providing feedback to match the characteristics of their jobs. Like compensation systems, performance management systems should not be revised too frequently due to the negative consequences addressed earlier.

A recession can have an important impact on employee receptiveness to performance feedback as well. While managers often must perform a delicate balancing act when discussing bad performance reviews with employees, the increased uncertainty of job security that many employees will experience during a downturn may increase their sensitivity to negative feedback, as they believe they are more likely to be terminated should the company need to cut costs.

**Retention**

While a recession generally decreases the likelihood that an employer will lose workers to competitors or to the allure of retirement, it can often present an employer with the unique problem of having too many available employees. An organization might actually “over-retain” when general economic upheaval occurs and employees have fewer opportunities to find work elsewhere or maintaining their desired standards of living in retirement proves more difficult. In a 2009 survey, benefits consulting firm Towers Watson (formerly Towers Perrin) found that 59% of employers believed employees would delay retirement due to the downturn in the economy (Financial Executive, 2009). While the impact of this trend will differ among companies, many employers may find themselves with an overabundance of experienced employees. While retention of workers with high levels of knowledge and skills can benefit an employer significantly, it may inhibit a company’s ability to bring in new employees with fresh knowledge and innovative perspectives. It may also cause a company to miss high-potential employees who suddenly become available because HR managers typically are not actively looking for them when there are no open positions to fill.
Employers must also confront the difficult reality that the best employees still seem to have
career mobility in a recession and thus, those employees who are most critical to retain are the
most likely to leave. A recent study in the marketing industry indicates this to be the case and
suggests that high-potential employees are not motivated by the mere fact that they have a job
(Ferguson & Brohaugh, 2009). As such, companies may lose their best performers to competitors
who are more willing to invest in workers’ career development.

**The Recession’s Impact on Companies and Related Impacts on HRM**

In addition to the challenges they face when general economic conditions are poor, HR managers
are confronted with many problems when souring market trends directly impact their companies.
The most evident issue is when companies are pressured to cut costs in an effort to maintain or
return to profitability, improve cash flow, or react to limitations on their access to capital. In the
discussion that follows, I review the primary impacts that such cost-cutting measures can have
on a manager’s ability to effectively execute HRM strategies.

**HR Planning**

A recession brings added complexities to a company’s processes for predicting both supply of
and demand for labor. On the supply side, predictive probability analyses are likely unreliable as
historical needs are much less indicative of future expectations. Note that this applies both during
the downward trajectory of a recession, when past supply requirements are higher than current
needs, and as the economy begins to exit the downturn, when the recession-era supply may be
lower than the company will need under improved conditions. In assessing their demands for
labor, employers must balance their focus on short-term needs for filling organizational gaps
with their projected long-term needs for staffing to execute on the company’s strategic objectives.
This struggle is exacerbated during times of economic volatility when an employer has an
incentive to reduce its labor costs in the short-term which could impair its ability to not only
meet its objectives when economic conditions improve but to survive the downturn altogether.
When a company’s operational environment becomes more volatile, it can also be more difficult
to forecast labor demand, as projections that operations personnel provide may be less reliable in
periods of greater uncertainty.

Succession planning, likely overlooked when a company must control spending, is critical to a
company’s ability to succeed during and after a recession for two primary reasons. First,
succession planning helps the company to identify the development needs of its high-potential
employees (Mello, 2006). Because these individuals maintain their career mobility through a
downturn, they may terminate their employment voluntarily if not provided with appropriate
development opportunities. The company will lose the talent most critical to effectively
achieving its strategic objectives, which will make surviving the recession much more difficult.
Second, when a company manages a labor surplus, it may bring upheaval to the organizational
structure of the company. For example, if a company executes a reorganization plan in order to
effectuate a more efficient operating structure (with, undoubtedly, some reduction in
management personnel), it will need to revise its plans for the succession of leadership due to the
change in the management hierarchy. Employers must give attention to this need during a recession through effective succession planning to ensure that they retain leaders capable of guiding them through the downturn and of achieving company strategic objectives afterward.

**Work Systems and Job Design**

A reduction in available resources can significantly affect a company’s strategy for the design of jobs and work systems. When a company cuts labor costs through either a workforce reduction or a reorganization of its operating structure, there is typically a change in the tasks and responsibilities associated with a number of positions as well as a shift in the interrelatedness of jobs within the new structure. This has various effects on a company, including increased risk that employees may not possess the skills and knowledge requisite for completing their assigned tasks, uncertainty among employees regarding their roles in the organization, and the potential for overwork of employees as they take on more assignments. This last effect brings with it a greater likelihood for increased costs of employee benefits and potential for long-term employee absences as stress levels among employees rise.

During a recession, employers will likely find it difficult to continue some of the programs it uses to provide employees with job enrichment. Employers may not see job rotation, through which employees develop skills by rotating through different positions in the organization, as a viable program to continue when there are fewer resources for training employees in the performance of new tasks. The view may be that the company must just “keep the ship afloat” during a downturn, which may result in a reduction in growth opportunities for employees as the variety of tasks they perform diminishes.

A common strategy for making permanent labor cost reductions is outsourcing of non-core operations. While such a move can certainly help a company to control labor costs through a period of economic contraction, the perceived disadvantages of outsourcing, including a decline in employee morale and loyalty as others lose their jobs (Mello, 2006), can be intensified during a recession as employees are generally more concerned about being terminated. In addition, the loss of control and internal talent can bring greater complexity to the company’s management of its operational processes. When a company offshores, or outsources jobs to individuals overseas, there are additional macroeconomic detriments, as the loss of domestic jobs by definition increases national unemployment as well as domestic output. Ironically, in this way an organization’s move to offshore jobs can delay the nation’s return to expansion.

**Staffing**

Despite the fact that there may be fewer total employees and job openings to manage, a HR manager’s job can be more difficult during a recession. Companies that have historically viewed HR positions as administrative may not be willing to invest resources in HR programs, including the retention and development of HR personnel. Management may take the view that with fewer people to hire during a downturn, the need for HR resources also declines. A reduction in HR staff provides an employer with challenges in effectively staffing open positions within the
desired timeframe. When a HR budget is cut, resources to pay external recruiters may become unavailable. Budget reductions may also restrict a hiring manager’s ability to offer competitive compensation to high-potential recruits when key positions are being filled. In addition, a company’s image can be tarnished if it undergoes a major restructuring that garners media attention. As a result of these constraints, the HR manager may find it more difficult to identify and hire top talent during a recession.

**Training and Development**

Resources allocated to training and development programs may logically be the first labor-related cost cut in a recession. An organization may perceive such a move to be less impactful and less demoralizing than workforce reductions or other significant cost-reduction initiatives. Even an organization that views training and development spending as a long-term investment in its people may have a hard time justifying the allocation of resources to these programs when capital availability wanes and company strategists give higher priority to spending on capital assets. In addition, when an employer reduces its workforce and its remaining employees are given increased responsibility, employers and even employees may question whether training and development is an appropriate use of their time. Finally, changes in job roles and organizational structure will likely result in a greater need for employee training as well as more frequent revisions of training program objectives.

**Compensation**

A company that is faced with a need to control costs faces major challenges when determining the appropriate compensation for its employees. A company’s ability to balance employee needs with company expectations for payroll and benefit costs can be of particular concern. HR managers should consider the phenomenon that wages generally tend to be “rigid” (i.e. do not decrease in real terms) during a recession despite the decrease in labor demand and a general expectation that wage rates would decrease (Giancola, 2009). In fact, U.S. median weekly earnings rose by 2.4% from 2008 to 2009, while overall prices as measured by the Consumer Price Index decreased 0.4% during the same period (Hipple, 2009).

Changes in job design will also necessitate a revision of compensation practices as they pertain to specific job roles. In particular, asking an employee to perform more tasks while receiving the same compensation may bring added conflict to relations between the employee and the company. An additional concern for employers trying to motivate employees through direct compensation is the effective pay cut that employees may take if a large portion of their pay is based on incentives related to company performance. Finding a way to motivate employees beyond base pay can be essential to ensuring that desired performance levels are reached.

**Performance Management**

A company’s changes to its organizational structure and prioritization of training and development will ultimately lead to required adjustments of its performance management system.
Effort must be given to ensure that employees’ individual objectives are aligned with the organization’s strategy, both for the short-term and the long-term, and that performance measures still fit with jobs as they are now defined. In addition to those changes to performance management that other HRM processes drive, a company may need to consider the appropriateness of its appraisal methods when considering a workforce reduction. As is also the case when the general economy is suffering, employers may find it tough to provide negative feedback to employees who have concerns that a poor performance review will lead to termination.

Retention

A recession affects an employer’s retention practices in ways beyond merely leaving companies with fewer people when staff reductions are made. As noted, succession planning is critical to ensuring that a company can retain its top organizational talent. As a result, a company may need to revise its retention processes to ensure that resources are properly allocated toward initiatives that will best serve its need to keep high-potential employees from voluntarily leaving. When a company initiates a significant workforce reduction or implements an early retirement plan, it likely will pay upfront as well as ongoing severance benefits which may require a significant cash outlay. HR personnel, financial management, and other key decision makers must be involved in the development of severance plans that will allow the company to realize a net cost savings.

Recommendations

As I have discussed, an economic recession can have many significant effects on an employer’s HRM processes and on its HR managers’ ability to effectively govern them. However, by utilizing an approach based on maximizing the benefits received from HRM spending, companies can implement practices that will enable them to not only survive an economic downturn but to develop unique, strategic positions and gain a competitive advantage over other companies.

Maintaining a Long-Term Focus — HRM as an Investment Portfolio

The most critical and most difficult consideration that a company must make when managing people through a recession is how to balance its current need to cut costs with its long-term desire to achieve strategic results. To ensure that strategy revisions made during a recession will not impair the company’s ability to attain its long-term goals, I propose that HR managers take an “investment” approach to executing their HRM strategies in a downturn. This means that all labor-related spending should be managed as a series of “projects” in a manner similar to capital asset investment projects. A company should include each functional area of HRM in its analysis of a project’s expected costs and returns. I recommend that a company manage its HRM investments as a “portfolio” of projects that individually must meet a company’s desired return and in aggregate should provide an organization with additional value through synergistic effects.
A company has two potential options for determining its method of HRM investment portfolio management. An organization could manage each functional area of the HRM process pipeline (planning, job/work systems design, staffing, training and development, performance management, compensation, and retention) as a separate investment, giving responsibility of each function to a different HR manager. Alternatively, a company may manage by operational group, for example a business unit, whereby one HR manager would have oversight over all HR functions associated with a particular unit.

I recommend that organizations take the latter approach for two primary reasons. First, while a HR manager must have responsibility for ensuring that the HRM investment meets its objectives, it is absolutely critical for business leaders to be involved in the management of their workers as valuable resources. If companies managed their HRM investments by function, each business leader would have to partner with multiple HR managers, adding an unnecessary layer of complexity and management cost to the process. Second, HR managers in turn would have to manage functional areas across a wide variety of diverse businesses, each with its own unique requirements for appropriate strategies. HR managers would spend too much time trying to understand these unique complexities and would find it difficult to efficiently manage the investment portfolio.

Although I recommend that organizations treat HRM associated with each line of business as a separate investment, in making initial assessments of costs and returns on these projects a company should analyze each functional area within the business unit separately at first. This not only makes the process of assessing a return simpler but more importantly provides leaders with a means of identifying individual mismatches between resources allocated and returns realized within particular functions. This can be equated to the analysis of a capital project’s different “scopes” or milestones separately to ensure that every part of the proposed project will add value.

I recommend that the company’s most senior HR personnel each be tasked with providing top-level oversight of a HRM project. These HR leaders should work with various departments, including operations and finance, to develop appropriate forecasts and to aggregate all data relevant to making the investment decision. Both HR and business unit managers, however, must ultimately be held accountable for the success of HRM investments.

While capital investment projects usually include a mix of material and personnel expenditures, the majority of costs associated with HRM investments will be direct and indirect labor costs. This includes many types of costs, including not only compensation for workers but also expenditures for HR professionals’ and operations managers’ time, and various costs of managing each HRM function. While some costs may not be as easily measurable as others, they must be included in project forecasts and analyses of project returns.

In addition to forecasting costs of HR programs, leaders must estimate the expected returns on HRM investments and ensure that they meet company expectations. While many benefits will be quantifiable (for example, specific and measurable increases in productivity), some will likely be more qualitative in nature. For example, a company may seek to foster a culture with greater
employee commitment to firm-wide objectives. Though it will likely be challenging, managers must develop methods for measuring the benefits that such initiatives provide. Managers should consider an approach similar to those often used for measuring the success of training and development initiatives or retention policies, where companies should already be using measures to determine how much value these programs add to the organization.

The first step that employers should take in managing a HRM investment portfolio is to recognize that not all investments are created equal. Companies will inevitably find difficulty prioritizing their spending on HRM programs, especially when budget reductions occur. Once a manager has estimated the returns for each functional HRM area of the business unit, he should review both how the company is allocating its aggregate resources and how each function is contributing to overall investment returns. If a certain function has a poor return but is receiving a proportionately high level of investment, the company should consider either reallocating a portion of its funds to a higher-performing initiative or developing more effective processes to increase the returns realized by its efforts in this function. Alternatively, the company may identify an area where returns are poor but a greater level of investment will foster an increase in scale and ultimately efficiencies. While making these resource allocation decisions will require management to vet many critical assumptions, the alternative—maintaining the status quo—will result in continued investment in poor-performing programs.

Though the HRM functions providing the greatest investments return will vary by company, an organization can prioritize its investments by considering recent trends in organizational management and employee needs. In presenting the results of its 2009 Employee Engagement and Retention Survey, Talentdrain (2009), an employee engagement and retention specialist in the United Kingdom, noted that during this recession, a majority of employers have been revising their HR strategies to focus more on performance management, employee engagement, and retention and less on recruiting. The report hypothesizes that this is occurring as employers recognize that retaining top talent in the current economic situation is more critical to sustaining success but also more difficult to achieve.

On a periodic basis (at least annually), the HR manager should report the results of his investment’s “performance” to the CEO and the company’s Board of Directors. These parties should discuss those investments that are underperforming and those worthy of increased investment, much like a financial advisor who meets with his clients to discuss the performance of their investment vehicles and potential strategies for improving overall returns through a reallocation of funds. The ultimate output from these discussions should be a strategic plan for increasing the return on the HRM portfolio.

**Focusing on High-Potential Employees**

It is no secret that the most talented members of an organization, or “high-potential employees,” are those most critical to a company’s success. The advanced knowledge, experience, and skills that such employees have represent the most viable strategic competitive advantage that a successful organization has. Many studies have provided documented evidence of the correlation
between high-performing leaders and high-performing companies, including the best-selling book *Good to Great* (Collins, 2001).

Because high-potential employees represent a company’s “best-performing asset,” an employer utilizing an investment approach to HRM should allocate the majority of its available investable “funds” to initiatives that impact top talent. In this way, an organization can realize sustained returns that outperform the “market,” or viewed from an HRM perspective, its competitors. As such, the recommendations that follow for maximizing HRM returns through function-specific initiatives focus primarily on ways to get the most out of high-potential employees. However, many of these suggestions can be—and often should be—applied to employees who achieve adequate results but are not the top achievers of the organization.

**Functional Specifics and Supporting Literature**

While I have provided a general framework for developing an investment approach to HRM that focuses on high-potential employees, utilizing such an approach to sustain performance during a recession involves several considerations unique to each functional area of HRM. Fortunately, the severity of the most recent recession has resulted in a plethora of documented support for individual techniques that managers can use to effectively foster change within their organizations.

I discuss several innovative solutions—each of which can create value and provide a company with a competitive performance advantage—that professionals should consider in managing their HRM investment portfolios. Because every company’s operating and HRM environments are different, it is impossible to provide a “one-size-fits-all” solution to maximizing returns on HRM investments. While managers should consider each of these initiatives, they can give greater priority to those activities that will impact the functions in which they should realize the greatest investment returns, primarily those that increase the value of high-potential employees the most.

**HR planning — succession, identifying talent gaps, and maintaining diversity**

Employers should give greater priority to succession planning than to their broader aggregate planning initiatives because such an investment allocation will provide greater returns. The mobility that high-potential employees retain even through a recession suggests that employers must increase their efforts to ensure that when top talent leaves the organization, new high-potential workers are available to step in quickly and keep the company headed in the right direction. In addition, a company that plans for succession effectively will more quickly identify the developmental needs of top performers which will lead to better job design and more effective training and development programs.

In order to effectively improve its succession planning processes, a company’s most senior managers should dedicate more time to updating succession plans. A recent survey by the American Institute of Certified Public Accountants (AICPA) indicated that only 35% of multi-owner CPA firms had developed formal written succession plans (Cingoranelli, Dennis, &
Schamberger, 2009). Given the time constraints that managers in other industries typically have, it is likely that this finding is not unique to accounting firms. A recession presents a good opportunity for managers to update or create original succession plans, which should incorporate changes in those skills and competencies required of key employees brought on by an organizational restructuring, a redistribution of work responsibilities, or most common, a change in company strategic objectives. The AICPA suggests that this process might include an offsite executive brainstorming session for pondering the key questions regarding the organization’s long-term objectives and how a succession plan will appropriately support them (Cíngoranelli et. al, 2009).

Though aggregate planning is less crucial than succession planning during a recession, strategic HR managers with sufficient resources can take an innovative approach to identifying potential gaps in talent based on the organization’s predicted needs. Chemical firm BASF began using revamped workforce analytics when its hiring needs stalled and HR employees could dedicate available time to updating employment models (Flander, 2010a). Such analysis might also include a robust review of job applicant data, whereby a company can develop a clearer understanding of the behavioral traits and motivations of its prospective labor pool, or even review of third party market data, which might give an employer more insight into the educational backgrounds of its region’s newest talent. While not all companies will have such freedom of resources, those that do can obtain an advantage over competitors who do not undertake such planning actions.

Evidence (Herring, 2009; Richard, 2000) suggests that investment in workplace diversity can improve company financial performance, justifying investment in programs that improve a company’s diversity. Despite the fact that unemployment has hit men the hardest during this recession, the economic downturn provides employers with an unexpected opportunity to revamp their diversity planning processes. A company can employ unique strategies for recruiting that enable it to gain advantages over other firms when hiring both during and after a recession. British company First ScotRail, for example, developed a recruiting campaign aimed at hiring women and consequently increased its proportion of female train drivers from 19% to 29% in two years (Simms, 2009). Companies in the United States seeking to maximize their investments in HR planning can identify their own diversity needs and implement strategies to fill identified gaps.

**Work systems and job design — downsizing, outsourcing, and alignment of skills**

While effective execution of downsizing is beyond the scope of this paper, a HR manager who is faced with a proposed reduction plan can think innovatively about alternative cost-saving solutions that will minimize the layoff of staff. For example, an employer might take advantage of today’s wireless and teleconferencing technology and allow employees to work remotely from any location they desire, reducing the company’s need for investment in real estate, usually one of a corporation’s greatest costs. Telecommunications company Sprint recently implemented such a program that generates $80 million in annual savings (Pratzel and Morton, 2009). Parrish Medical Center, a non-profit healthcare organization in Florida, also took a unique approach to
significant cost reductions. Instead of executing a mass layoff, the organization held town hall meetings with its employees to brainstorm ideas for cost-cutting measures (Ruhlman & Siegman, 2009). This innovative move not only cut significant costs from the company budget but served to increase employee engagement with the company.

Noble and Harper (2010) note that phased retirement, allowing older workers to gradually reduce work hours with or without the ability to draw on retirement income, may enable a company to reduce workforce costs. This also could be a strategic method for dealing with a perceived oversupply of older workers and for increasing a company’s capacity to hire high-potential talent into its organization.

If a HR manager ultimately must face the prospect of implementing a layoff, he should consider that staff reductions may have unintended impacts on the employees that remain. In a University of Wisconsin study, Trevor and Nyberg (2008) found that increases in voluntary turnover rates are positively correlated to both the existence of a downsizing event and its severity. As a result, employers will likely be understaffed not long after affecting a significant layoff. Employers should note this phenomenon when determining the number of employees to terminate.

Employers should also consider how its HRM practices associated with other functions impact those employees who are not laid off in a downsizing. Trevor and Nyberg (2008) found that the increase in voluntary turnover that results from downsizing is often minimized when an organization is perceived to have high levels of either job embeddedness, “the level to which employees are bound in a social web (both on and off the job) that keeps them attached to their organization,” or procedural justice, the fairness of decision-making processes that impact employees. Conversely, this study found that companies with strong career development programs, primarily those focused on providing employees with greater job search capabilities and on “signaling” these employees’ strengths to the job market, experience higher voluntary turnover rates following a downsizing (Trevor & Nyberg, 2008). While providing high-potential employees with development opportunities is an essential part of effective succession planning, companies may need to re-think the components of such programs to ensure that they serve the purpose of keeping employees engaged with their current employer. A company intending to enact a major workforce reduction should consider these findings and should also reflect upon these issues when designing its processes for training and development as well as reviewing its embedded cultural norms.

A company’s decision regarding the appropriateness of outsourcing should follow an investment perspective as well. In addition to simply calculating the direct cost savings that outsourcing of certain functions can bring, decision makers should assign values to indirect costs such as reductions in morale and public image that may come with outsourcing initiatives. It is likely that most managers do not fully consider such costs, but they must in order to ensure that the company is truly earning the return for outsourcing that it seeks. GE has taken a unique approach to reducing the costs of its global tax function by using a team in India comprised not of third party workers but of GE employees (Faith, 2009). Such a plan might mitigate the impact of outsourcing’s indirect costs while providing for a reduction in staffing expenses.
The re-assessment of job roles and responsibilities will play a critical part in ensuring that the needs of high-performance employees are being met in a downturn. In a recent survey asking readers of Human Resources Executive (Flander, 2010b) the question, “what do you consider to be the three biggest HR challenges being faced by your organization today?” the top three responses were related to maintaining employee engagement and productivity, retaining key talent, and developing leaders. While a company must address such challenges throughout the HRM process pipeline, it must first ensure that jobs and work arrangements are designed such that they effectively address workers’ motivating factors. Because organizational structures change and the motivations for many workers shift when times are more difficult, jobs and employees who perform them may no longer have an appropriate fit.

HR managers can obtain information about employee motivations either through direct discussion or through distribution of an employee survey, such as Gallup’s Q12 Employee Engagement Survey, which links employee engagement to specific business outcomes (Harter, Schmidt, Killham, & Agrawal, 2009). Once an employer understands his employees’ level of engagement, he should review the core dimensions of each employee’s job and take action for those who no longer have fit by redesigning certain aspects of the job or re-assigning employees’ roles and responsibilities. Other initiatives for increasing engagement, including training and development, should also be implemented.

**Staffing — strategic hiring and new recruiting styles**

HR managers should take innovative approaches to recruiting and selecting employees during an economic downturn. Because the few open positions a company will be filling are likely only those most critical to the organization, hiring professionals have an opportunity to develop methods that will focus staffing resources on finding top talent. John Challenger, CEO of employment consulting firm Challenger, Gray, & Christmas, Inc., suggests that companies should make the seemingly paradoxical move of increasing hiring during a recession (Ladd, 2009). Because higher unemployment levels result in a greater number of talented employees being out of work, companies that are willing to make investments in seeking high-potential employees can find talent that may not be available when job conditions improve. In addition, because such employees are likely very motivated to find work quickly, it may cost employers less to attract them during a recession than it would when labor supply is tight. Employers should be careful to remember, however, that talented people will generally retain their job mobility and may be able to attract very competitive salaries.

While many organizations slash recruiting budgets during a recession due to the decline in hiring activity, strategic companies can use their available recruiting personnel to revise their recruiting processes. Flander (2010a) suggests that recruiting must be more strategic now and should be more “relationship-based” than it was in the past. This may require a different skill set for today’s recruiting professionals, who fortunately may have the time to develop unique skill sets during a slowdown in hiring.
Employers may also benefit by reducing their recruiting fees during an economic downturn. While many companies have been forced to pay significant fees in order to find and attract high-performing talent in the past, the surplus of labor during a downturn should provide an employer with a greater number of talented applicants, especially those who had strong career development opportunities at previous employers. Despite the increased difficulty of filtering out the best employees in a surplus labor market, this increased access to high-potential employees should allow hiring managers to reduce the amounts paid to outside search firms.

**Training and development – employee engagement and management flexibility**

HRM professionals should give strong consideration to increasing resources allocated to training and development during a downturn. The results of the recent *Human Resources Executive* survey (Flander, 2010b) suggest that improving employee engagement is at the forefront of most managers’ minds, and there are several ways that managers can seek to keep employees engaged. The same survey respondents noted that increasing employee communication and providing employees with additional training and development were the top two areas of focus for increasing employee retention during the next year (Flander, 2010b). In addition, Towers Watson has conducted recent bi-annual surveys that shed some light on the desires and behaviors of employees. In its 2007-2008 Global Workforce Study (Towers Perrin, 2008), the professional services company noted that only 21% of workers surveyed considered themselves “engaged” at work, while 38% reported that they were either “disengaged” or “disenchanted.” The survey results also indicated that employees who are engaged are more likely to believe that they can have an impact in their organizations and are less likely to leave their current job (Towers Perrin, 2008). Additionally, 83% of the survey’s respondents indicated that they seek opportunities to develop new knowledge and skills (Towers Perrin, 2008). Though in its 2009-2010 Global Workforce Study Towers Watson (2010) reported that the relative impact of career development on engagement has decreased as the importance of a company’s image has increased, the results of these surveys indicate that both employers and employees recognize the need for continued workplace development.

Employers should design training and development programs that are in line with employees’ needs and the skills required to perform job tasks. This can be more easily accomplished if managers first ensure that workers and their associated job roles have the appropriate fit as previously recommended. Effective training and development programs will also consider how each generation of employees uniquely prioritizes its needs. For example, a strategic training initiative might provide a variety of voluntary programs to train employees in maintaining a work/life balance, understanding compensation, or furthering their opportunities for advancement to senior management levels of an organization. In order to maximize its returns on investment in training and development, a company should also review existing programs to identify and eliminate programs that are no longer relevant to employee needs.

An employer should utilize training and development programs that improve the workplace flexibility of its managers as well. Kaiser (2010) recommends that consulting psychologists can
assist a company in improving management’s adaptability. This represents another unique approach that could have long-term benefits if resources are appropriately utilized.

**Compensation — unique reward strategies**

Compensation practices should be revised during a downturn so that they are aligned with the needs of employees. When typical incentive-based bonuses may be too costly for a company to pay, an employer can use other strategies to motivate employees that may also increase perceived equity of compensation. Many companies are implementing flexible work schedules which not only provide a desired benefit to employees but may also reduce company costs for overhead such as utilities. Brenner (2009) suggests that investing more in healthcare benefits can allow a company to achieve a competitive advantage that it can sustain after the recession, enabling the organization to more easily attract talented employees when labor demand improves. Investment in preventive care including stress management may also help an employer to reduce its long-term employee medical costs. Gilbert, Buxton, Golden and Ryan (2009) argue that providing employees with more company stock in ESOPs and retirement plans will not only increase employees’ vested interest in company performance but will also allow the company to reduce its cash needs during a downturn. Such strategies that can both maximize employee return and decrease employee cost will provide significantly improved returns on HRM investments.

**Performance management — focusing on outcomes and utilizing self-appraisals**

In order to maximize its returns from investment in employees, a company must ensure that employee goals are in line with its strategic objectives, which often have changed dramatically when an economy has entered a recession. Once a company has implemented the job re-design and engagement improvement initiatives that I have recommended, its managers must ensure that employee performance objectives, which should focus on specific performance outcomes, are appropriately revised as well. The results of the Gallup Q12 survey (Harter et. al, 2009) will assist an employer in accomplishing this.

In a study of performance appraisal interviews, Asmuß (2008) found that the method of communicating negative performance feedback had a significant impact on an employee’s response to criticism, which as I have suggested can be enflamed during uncertain economic times. She suggests that if both employer and employee provide negative feedback on the employee’s performance via performance appraisal forms, the discussions could be oriented more toward improving employee performance than on perceived negative consequences of a bad review (Asmuß, 2008). This can be accomplished by explicitly asking employees to identify their weaknesses in employee self-appraisals and being prepared to discuss them in the interview.

**Retention — support from other HRM functions and exit data**

The greatest priority for employers regarding retention is ensuring that high-potential employees remain in the organization. I suggest that my recommendations for strategic recruiting of available talent and implementing innovative training and development, compensation, and
performance management practices are the primary tools that employers can use to mitigate the risk of losing talent in during a downturn. Should high-performers leave the organization, however, HR managers can leverage data gathered from exit interviews to understand what issues may have led to the employee’s decision to leave. Talentdrain (2009) notes that 68% of employers utilize exit data to understand reasons for turnover of high-performers, suggesting that nearly one-third of employers can benefit from implementation of a process to analyze such information.

Disadvantages of Implementing Proposed Initiatives

HR managers and business leaders dealing with company financial distress during a recession may feel that the pressures they face to reduce costs and increase efficiency do not afford them the luxury of making the significant number of changes I have proposed. While I believe that taking an investment portfolio approach to strategically transforming HRM processes will enable a company to focus its efforts on those functions providing the greatest return, effectively freeing up HR hours from less valuable tasks, my proposal does call for many companies to make rather radical changes in their approaches to HRM. I suspect that organizations will find that a significant investment of both financial and personal resources is required to review the HRM functions of each business line and determine how the company should reallocate resources. At a time when many leaders must make substantial cost reductions just in order to keep their companies economically viable, such investment is likely to be met with skepticism.

A portfolio management perspective has some practical difficulties in regard to the management of HRM functions. Because senior HR personnel must become “portfolio managers,” a significant shift in resources must occur to give them adequate time to accomplish these tasks. Existing HR structures, particularly at smaller firms, may not be supportive of increased responsibility in HR functions. My proposals require HR practitioners to manage practices throughout the HRM process pipeline, and as such, HR personnel must have knowledge of each HRM function. An HR professional who has historically specialized in a certain function will require additional training and development opportunities to gain a firm grasp of other areas. Additionally, the skill sets of most HR professionals currently do not include expertise in financial project management or portfolio analysis; therefore, HR managers will need additional training (at a cost) in order to understand how to view HRM functions in financial terms and how to evaluate benefits, costs, and net returns. Finally, the portfolio approach inevitably means that some HR managers will oversee projects or business units that have more room for improvement than others. While CEOs should be careful to assess each manager’s investment performance not strictly on total returns but on how returns have improved from previous periods as well, political tensions will likely result.

Perhaps the most difficult task an organization taking my approach will face is the difficulty of accurately measuring both benefits and costs for programs such as developing succession plans, revitalizing training and development programs, or increasing the use of exit data. Though I argue that companies should make their best efforts in estimating such amounts, a function
inherent in any project forecasting process, I recognize that employers could benefit from additional research on methods for valuing initiatives that have less concrete returns and costs.

**Concluding Remarks**

While the bottom-line impacts of a recession on American individual and businesses is discussed throughout the twenty-four hour media cycle, little attention is given to the impact that such trying times can have on a company’s ability to effectively manage its people. U.S. businesses must contend not only with reductions in financial flexibility for their firms but with the impact that an economic downturn has on employee needs, motivations, and attitudes.

Because they usually think of people costs as payroll and benefit “expenses,” many business leaders’ first reaction to a need for increased profitability and improved cash flow is to reduce employee headcount and spending on employee performance initiatives not seen as critical to company revenue generation. This might be a consequence of a historically manufacturing-based economy in which business owners were more reliant on maintaining physical assets and had little choice but to terminate people in order to shave costs. As the United States economy is now a service-based economy—over 68% of economic “value added” in 2009 was from service-based industries (U.S. Bureau of Economic Analysis, 2010a)—leaders must shed this mindset and realize that employees are no longer a commodity and are also more difficult to replace. By releasing employees, especially those high-potential employees with the greatest skill sets, organizations effectively pay (due to the pervasiveness of severance benefit and other exit costs) to let someone else take the resources most likely to provide value in the future, a move that asset managers will agree is the last thing an intelligent investor will do to improve his portfolio.

An employer that invests in people during a downward economic cycle can develop a true competitive advantage over its competitors who do not realize the value to such an approach. By analyzing the discrete benefits that each function of HRM provides to its various lines of business, a company can identify assets, in the form of employee support systems, that most efficiently increase the value that high-potential employees provide to the firm. Companies who increase employee productivity and contributions to their organizations will not only survive the worst U.S. economic crisis since World War II (National Bureau of Economic Research, 2010) but will thrive when an expansion returns.
References


