Involuntary Downsizing: The Impact of a Labour Shortage

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Abstract
Labour shortages are imminent in a variety of different industries, particularly those that require high levels of skills. Organizations will need to plan for these shortages as many of the solutions will have fairly long lead times before an impact is felt. One area from which short-term gains may be achieved is the reduction of voluntary turnover, particularly the loss of productive employees. An area with potential for longer-term success in combating the labour shortage is in restructuring. Through restructuring, organizations can redesign the work processes so that when employees do leave, the position will have to be reworked and a replacement may not be needed. The organization will be shrinking in headcount, but it will remain as productive as it was before downsizing due to efficiencies gained; it will have successfully navigated “involuntary downsizing”.

The purpose of this paper is to develop the concept of involuntary downsizing” by expanding the definition of downsizing to include situations in which organizations are competing in diminishing labour markets. Similar to the current concept of downsizing, organizations will need to accomplish more, with fewer resources; however, the cause of the downsizing and the solutions that are available will be different.

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Introduction

The discussion regarding downsizing began in the 1980s (Davis et al., 2003) as organizations saw the need to respond to changes in the environment and within the institution with a new strategy to restructure with staff reductions (Davis et al., 2003). Organizations were eliminating employees, positions, departments and product lines (Davis et al., 2003) in an attempt to improve the profitability of the organization through reducing waste (Gertz and Baptista, 1995), improve productivity (McKinley et al., 1995), and improve the competitive stance of the organization (Cameron, 1994). Davis et al. (2003) discuss the external environmental pressures on organizations to downsize; however, these pressures include only those external elements that are related to the demands upon the organization for production and do not include the pressures on the supply of resources to the organization, such as a limited labour force.

Tight labour markets are created when economic growth exceeds the level of productivity (Capelli, 2005), a low unemployment rate exists in an industry, weekly wages fluctuate, and employment is growing and is anticipated to continue growing (Levine, 1996). When the supply of labour is greater than the demand, organizations can use different compensation strategies for recruitment and retention, but when there is a labour shortage, the negotiating power for positions is held by the workers. The transfer of power to the workers is due to the significantly greater opportunities for the worker, and organizations are forced to bid for employees in order to obtain their services (Ang et al., 2002). A debate has sprung up regarding the existence of a current or potential labour shortage, and there is a lack of research on the impact of a labour shortage on organizations. A labour shortage may have a dramatic impact on an organization, particularly one that operates in an industry of stable or increasing demand in that the limited resources for labour may create a conflict between the demands of the customers of an industry and the capacity of the organization to meet those demands.

A significant amount of work has been completed on the subjects of voluntary turnover, downsizing and restructuring. Researchers have looked at these elements from different perspectives (individual, organizational, and extra-organizational), and through a variety of different methods. It appears, however, that there may be a lack of research conducted on these concepts in an environment where there is a shortage of skilled labour. Not all trades and professions are able to boast an unlimited supply of human resources, and this scarcity of labour will have an impact on the organizations that rely on these skills for achieving their objectives.

The environment in which businesses operate is changing rapidly. Where once there were abundances of skilled workers, there are now unemployment rates at levels lower than they have been in more than 32 years (Grant & Sethi, 2006), a population that is aging leading to significant numbers of workers leaving the workforce due to retirement (Oromaner, 2006), and climbing wage rates (Grant & Sethi, 2006) that are following the simple rules of supply and demand. This shortage has been felt by numerous industries for many years (for example, the trucking industry was shown to be suffering from a shortage of skilled labour almost a decade ago in a study by
Shaw, Delery, Jenkins and Gupta (1998)) and the shortages are still a major concern today (Grant & Sethi, 2006). Along with the shortage of skilled labour, there is also a shortage of research on the impacts of this diminishing labour pool to organizations. This impact is exasperated as excess capacity disappears and new strategies are needed for restructuring in order to deal with voluntary turnover and the organizational shrinking ("involuntary downsizing") that is taking place.

This paper will present two areas in which a labour shortage will dramatically affect the way organizations operate: dealing with voluntary turnover (which will include retirement for the purposes of this paper) and restructuring of work processes. A new way of conceptualizing downsizing will be presented. This new perspective of downsizing, termed in this paper as "involuntary downsizing" will incorporate the forced reduction in workforce due to labour shortages into an expanded definition of downsizing. The purpose of this paper will be to examine the literature in downsizing, voluntary turnover and restructuring in an attempt to determine which elements may be applicable during labour shortages. The goal is to provide organizations with some potential tools for managing this type of environment and to provide a basis for further research in extending these concepts to labour-scarce environments. This paper contributes to the literature on voluntary turnover and restructuring by investigating areas that overlap with "involuntary downsizing" and therefore provides insight into potential remedies for the labour shortage problem. The new classification of downsizing will be developed by segmenting the original concept of downsizing into two distinct areas: those downsizing activities that incorporate intentional reductions in the size of organizations which will be termed "voluntary downsizing" and the new area proposed by this paper, "involuntary downsizing" which is a result of activities that reduce the size of the organization unintentionally.

Labour shortages

The statistics are exposing a trend that is impacting strategic human resource management today, with approximately 70% of employers surveyed stating that they had experienced problems in hiring people for core functions within their organization (Herman, 2004). The inability to hire qualified individuals had the result of leaving these positions empty (Herman, 2004). Projections for the future do not appear promising. The Bureau of Labour Statistics in the US estimates that in 2010, there will be over 10 million jobs unfilled (Herman, 2004) with that number increasing to between 21 and 40 million jobs unfilled by 2015 (Jamrog, 2004).

The shortages appear to be wide-spread. Numerous industries are reporting problems due to a diminishing labour pool including the automotive industry (Anonymous, 2006), finance and accounting (Espenshade, 2001; Messmer, 2006), nursing and other health-related areas (Camden, 2005; Espenshade, 2001; Spetz & Adams, 2006), government (Soni, 2004), technology (Ang et al., 2002; Camden, 2005; Carter, 1997; Espenshade, 2001), managerial and professional (Carter, 1997), and in general, positions that require high levels of skills and training (Levine, 1996; Messmer, 2006). With so many industries affected by this labour shortage issue, it seems surprising that researchers have not taken the lead on examining the issue. The reason for a lack of research in this area may be due to the conflicting reports regarding whether or not there is really a problem with the availability of labour.
Some of the arguments in opposition to a shortage in labour include that people are living longer, and this increased life expectancy will likely lead to people staying in the workforce longer (Capelli, 2005). These individuals may choose to remain working in a full-time capacity, or perhaps take on positions of lesser responsibility, potentially in a part-time capacity, to supplement their retirement income. The result of these changes should be an increase in experienced people remaining in the workforce. Additionally, an increase in graduates from post-secondary education should lead to a higher quality workforce with a decline in less-educated and less experienced employees – a group of employees that will experience decreasing demand (Capelli, 2005). Capelli (2005) also argued that equipment and system improvements should lead to increased productivity per employee, thereby reducing the demand for labour. The appearance of shortages may simply be due to employers being unwilling or unable to pay the market price for labour (Capelli, 2005). Many of the companies reporting shortages are the same ones that have been laying off employees in recent years (Espenshade, 2001). Human resource managers may be reacting to the pressures of achieving quick gains from restructuring initiatives – a process that creates high turnover and a reliance on obtaining new skills and knowledge by hiring people from outside of the organization (Capelli, 2005). And finally, it has been proposed that studies on the potential shortage are methodologically flawed and politically motivated (Espenshade, 2001). When examining all of these arguments as a whole, it would appear that there is an ample supply of labour and that shortages are experienced by specific organizations only as a result of the backlash from the layoffs.

There is, however, a counter-argument. Research on the changing labour pool can be divided into factors that affect the entry of individuals into the labour pool, demographic factors that affect the exit of individuals from the labour pool, and organizational factors that affect the usage of the labour pool. One’s education level will influence the segment of the labour pool in which one can enter. The number of graduates from post-secondary education is increasing (Capelli, 2005), which should lead to an increase in the labour pool for skilled and knowledgeable labour; however, enrollment in university programs is not necessarily distributed among the various disciplines according to the needs of organizations. For example, finance and accounting programs have been facing declining enrollments in recent years which is affecting the pool of available employees for positions requiring these skills (Messmer, 2006).

Demographics are also changing the nature of the labour pool and it is anticipated that the working age population will shrink by 7% over the next 20 years in industrialized countries (Camden, 2005). Although the increased life expectancy may keep older workers in the labour pool past the current normal retirement age (Capelli, 2005; Jamrog, 2004), the majority of those who remain in the workforce may do so in a temporary or part-time capacity and in many instances in a function different from the one that they were in prior to retirement (Adams & Rau, 2004). There is also a strong trend for early retirement that has not changed even with recent market fluctuations and stock market losses (Jamrog, 2004). Therefore, in many industries, such as consulting, part-time executives, volunteerism, and post-secondary adult teaching, there will be large surpluses of workers due to the entrance of the retirees into the labour pool. However, in the industries that they left, there will be significant voids of talent (Weiss, 2005). Increasing the problem is the reduction in the birth rate in Canada, down to a low of 10.5 births for every 1000 people in the population (Statistics Canada, 2006), which is reducing the number of people entering the work force to replace those who are retiring.
Organizations are not innocent bystanders in the events that cause fluctuations in the demands on the labour supply, and the implementation of certain efficiency-driven initiatives are now resulting in higher demands for labour. For example, companies are urging salespeople to sell products, but in an atmosphere of low-inventory manufacturing or just-in-time systems, the only way to satisfy the increase in demand brought on by the focus on sales is to increase production levels, which in turn increases the demand for labour (Herman, 2004). Capelli (2005) also questioned the applicability of the claims by organizations that they are forced to leave critical positions empty due to labour shortages: he argued that organizations are only experiencing these difficulties because they may not be able to compete in the market to offer the wages and benefits that are demanded by potential employees. However, rising wages are an indication of a shortage of labour (Spetz & Adams, 2006), and therefore, the inability of organizations to offer market wages may be an indication of the existence of a shortage, as opposed to justifying the opposite as claimed by Capelli (2005).

The two sides of the argument can be brought together. There may be a sufficient number of people available for work; however, there is an issue with the distribution of skills and the number of employees with obsolete skills (Herman, 2004). Therefore, some organizations will not have problems finding enough employees, but there will be some organizations, particularly those that require a high level of skills and knowledge, who will find a limited supply of potential employees from which to choose. These latter organizations may need to change their demands on the labour pool by utilizing their human resources more efficiently and effectively, reducing the number of current employees leaving the organization, or tailoring the labour pool to their own needs.

Some of the potential solutions available to organizations will be to educate and train a new supply of labour (Anonymous, 2006; Camden, 2005; Spetz & Adams, 2006), outsource various functions (Anonymous, 2006), extend work week hours (Camden, 2005), utilize immigration strategically (Camden, 2005; Carter, 1997; Espenshade, 2001), raise the retirement age (Camden, 2005), utilize free-agent or contingent workers (Camden, 2005), improve the quality of leadership (Herman, 2004), develop an appropriate strategy for the resources that exist within the organization (Herman, 2004), increase retention and recruitment to reduce voluntary turnover (Herman, 2004; Spetz & Adams, 2006), and examine the systems or the way organizations operate (Herman, 2004), or in other words, restructure. The difficulty with most of these solutions is the length of time needed before changes will begin to affect the labour pool issue. For example, education and training for high-skilled workers will take many years to prepare and many years more before workers complete the program and are ready to join the workforce. To compound the effect of the labour shortage, it is the jobs that require the highest level of skills and knowledge that will be in highest demand and yet those will take longest to respond to shortages due to the length of time needed in the educational system (Levine, 1996). Changing retirement ages, work-week regulations and immigration policies will require substantial lobbying efforts and governmental action. There are, however, two areas over which organizations have more direct control – voluntary turnover and restructuring – to combat the pressures of a diminishing labour pool.
Labour Shortages and Voluntary Turnover

In order to discuss the effects of voluntary turnover on organizations experiencing labour shortages, it is important to define what voluntary turnover is. Voluntary turnover can be segmented into functional (ineffective employees who leave) and dysfunctional (the loss of productive employees). Dysfunctional voluntary turnover can, in turn, be segmented into unavoidable (for example, employees who leave in order to move with a transferred spouse) and avoidable (employees who choose to leave for reasons that are under the organization’s control) turnover (Griffeth & Hom, 2001). The attention of researchers has been captured by the impact of turnover on organization performance including the direct and indirect costs of turnover (Griffith & Hom, 2001), the connection to sales in a service-oriented industry (Batt, 2002), and productivity (Shaw et al., 2005). The literature also examines the causes of turnover, both at an individual level (Griffith & Hom, 2001), and at an organizational level (Shaw et al., 1998). Shaw et al. (1998) examined the relationship between human resource management practices and quit rates while recognizing the evidence of regular shortages of labour in the industry; however, this evidence did not play a prominent role in the analysis.

How is turnover contributing to the problems associated with labour shortages? Voluntary turnover, and in particular, avoidable dysfunctional voluntary turnover, compounds the effects of labour shortages because when the labour pool is shrinking, each employee lost means an accelerated shrinking of the organization. The management of turnover, therefore, will become even more critical (Griffith & Hom, 2001). Turnover, on its own, affects organizational effectiveness due to the loss of organizational knowledge and customer relationships (Endres & Alexander, 2006; Koys, 2001) and can be very costly to the organization through lost productivity, sales and morale. Turnover, when there are limited resources to replace the exiting employees, will become even more costly as organizations are forced to negotiate to lure new talent into the organization (Ang et al., 2002). For example, retention in the insurance industry has been found to be critical as only one agent in six tends to remain and the costs are significant enough to translate to a 15% savings in training costs when turnover can be improved by 5% (Hersch, 2005).

In order to increase retention and lower quit rates, organizations need to foster high skills, employee participation in decision making and in teams, and human resources incentives, such as high relative pay and employment security (Batt, 2002). Mentoring (connecting those individuals close to retirement and new employees to the organization) has also been used as a tool to enhance retention in the firm (Hersch, 2005). The concern with implementing these activities is that practices that are effective in industries with an abundance of labour may not generalize to industries that suffer from a labour shortage; therefore, research is needed on labour-constrained industries to determine the effectiveness of retention-enhancing programs.

Retirement did not really become prevalent until after WWII because organizations did not offer pension plans, government old age security programs were non-existent, and people could simply not afford to retire (Heinbuch, 1995). Since then, a mandatory retirement age was initiated and now, in many jurisdictions, the mandatory retirement age has been removed. The elimination of a mandatory retirement age has had the effect of making retirement a voluntary choice for employees (Adams & Beehr, 1998) and therefore an element of voluntary turnover. Many individuals are also choosing to retire early, with the median retirement age dropping from
65, in 1976, to close to 60, in 2001 (Kieran, 2001). An interesting note is that those individuals who decide to retire early are more likely to be those with a higher level of education (Kieran, 2001), which coincides with the labour shortages affecting the industries who require the highest levels of skills. With the upcoming retirement of the baby boom generation, organizations will need to prepare for the loss of knowledge and talent that will take place and devise innovative ways to increase retention of these valuable, experienced and skilled employees.

Restructuring, Redesign, and Downsizing

Restructuring is defined as planned changes in an organization’s structure that affect its use of people (Morrow, 2003). It is being used as a tool to combat the effects of macro environmental factors such as competitive markets and demands on cost controls (Lee & Teo, 2005). Although the terms “restructuring” and “downsizing” are used interchangeably by many (Cameron, 1994), they are distinct (yet linked) functions within an organization (Budros, 1999). An organizational strategy that focuses on restructuring may have significantly different results than a strategy that focuses on downsizing. The research on the link between downsizing and organizational restructuring includes an investigation into successful strategies for downsizing and how work redesign contains the potential for eliminating function, hierarchical levels, groups, division, and/or products (Cameron, 1994), as well as the negative impact of downsizing when restructuring is not implemented concurrently (Dougherty & Bowman, 1995).

When restructuring, or redesign, is the goal, the organization’s focus will be on finding new structures and processes for conducting business and a reduction in the workforce (downsizing) is likely to be an outcome (Freeman, 1999). Freeman (1999) detailed the differences between organizations that downsize and as a consequence redesign organizational structures, and those organizations that implement redesign strategies that lead to downsizing. It is the latter set of organizations that could provide insights for organizations in situations of labour shortages because a redesign strategy may be used proactively, prior to the initiation of a severe labour shortage, to improve productivity and therefore, require fewer employees. Freeman (1999) noted, however, that downsizing is an intentional action of an organization, and therefore, the applicability to organizations experiencing an involuntary downsizing effect will need to be investigated.

Downsizing and Decline

The contributions of this paper revolve around the expansion of the term downsizing to include situations of organizational shrinking due to labour shortages; therefore, it is important to understand how the literature defines downsizing currently. There are numerous different definitions, some of which contradict each other including that downsizing is a reduction in workforce (Barrick et al., 1994), an intentional reduction of the number of people within an organization (Freeman, 1999), a reduction in a firm’s use of financial, physical, human or informational assets (Morrow, 2003), the conscious use of reductions in the permanent personnel complement in order to bring about increased efficiencies, productivity or competitiveness (Budros, 1999; Cameron, 1994), the planned elimination of positions or jobs, which will include reducing work (not just employees), eliminating functions, hierarchical levels or units, cost containment strategies to streamline activities but not terminations of employees for cause, normal retirements or quitting (Cascio, 1993), and the elimination of jobs in an organization due
to either decreases in market demand or cost-cutting measures (Chadwick et al., 2004). Depending on the definition, there may be confusion with restructuring or with organizational decline (a decrease in market demand causing an organization to shrink). Cameron (1994) recognized that organizations can shrink from an unintentional lack of human resources; however, only shortages due to organizational decline were examined, and not shortages that may be due to a reduction in the labour pool from other factors. The importance of these definitions lies in the focus on the intention of organizations to reduce the size of the workforce. Absent from these definitions are situations in which an organization finds itself unable to maintain or grow its labour force due to the supply of new labour being unable to compensate for the loss of personnel through turnover.

**Discussion**

Labour shortages are imminent in a variety of different industries, particularly those industries that require high levels of skills. Organizations will need to plan for the imminent labour shortages because many of the solutions will have fairly long lead times before an impact is felt. Although short-term gains may be achieved through reducing voluntary turnover, longer-term success in combating the labour shortage may be in restructuring. Through restructuring, organizations have the opportunity to redesign the work processes so that when employees do leave, the position will have been reworked and a replacement may not be needed. The organization will be shrinking in headcount, but the goal will be to remain as productive as it was prior to the downsizing due to efficiencies gained and to successfully navigate “involuntary downsizing”.

**Development of “Involuntary Downsizing”**

“Involuntary downsizing” occurs when an organization is forced into shrinking the size of the workforce due to reductions in the labour pool. This reduction of the labour pool means that there are insufficient numbers of potential recruits to replace the employees who leave the organization due to turnover, and in particular, the number of baby boom employees who will be retiring in the coming years. A classification of downsizing has been created by assessing the various definitions of downsizing and grouping them into segments that incorporate both the intentional motivations for downsizing and the situations where downsizing is a result of factors that have caused an unintentional shrinking of the workforce (see Figure 1). This paper differs from the rest of the downsizing literature because it distinguishes between the voluntary and involuntary segments of the classification scheme and the addition of the labour pool shortage as a cause of involuntary organizational downsizing.

The first division of downsizing is between the voluntary and involuntary segments. Voluntary downsizing includes any actions of management that are intentional including the three downsizing strategies detailed by Cameron (1994): workforce reduction, work redesign and systematic downsizing (a focus on changing the organizational culture and attitudes to one of continuous improvement). The voluntary downsizing segment is then further divided into the two categories of organizational voluntary downsizing and extra-organizational downsizing, as defined by Budros (1999). His study on the reasons why organizations downsize investigated internal organizational forces such as mergers and acquisitions, implementation of new
technologies, and CEO competencies, and forces external to the organization such as shareholder values, regulatory environments, economic trends, the prevalence of downsizing within the industry and the level of competition in the industry (Budros, 1999). These forces, both internal and external, may result in the decision-makers of organizations choosing to respond in a way that includes the reduction of the workforce within the organization.

Figure 1: A Classification Scheme of Downsizing

A critical difference between voluntary and involuntary downsizing is held within the intent of management. Voluntary downsizing is achieved through intentional actions whereas involuntary downsizing is a result of forces outside of the intent of management and hence, a second branch is added to the downsizing schematic. The involuntary downsizing segment can be influenced by both internal and external factors, similar to the voluntary downsizing segment and therefore, involuntary downsizing is divided into organizational and extra-organizational involuntary downsizing. Organizational involuntary downsizing is the presence of characteristics within the organization that cause employees to leave. The majority of instances when employees leave an organization, they are leaving because of factors within the manager’s control (Carsten, 2006). Organizations will need to look inwards to analyze their internal environment for designing a better work environment and retention strategies.

Extra-organizational involuntary downsizing can be a result of forces external to the organization such as organizational decline and a reduction in the labour pool. Growth has been assumed to be essential for success; however, organizational decline is also recognized as a normal and sometimes essential part of the business cycle (Cameron, 1994). Organizational decline is encountered in a variety of different forms including, for example, the reduction of governmental funding or a loss of market share, which can result in the organization finding new ways of operating or exiting from the industry altogether (Cangemi & Miller, 2004). A shrinking labour market also has the ability to cause an involuntary downsizing of the organization. Immigration laws, the aging of the baby boom generation and the impending retirement of this demographic group, and the impact of post-secondary education enrollments that are mis-aligned
with the needs of industry are just some of the factors that are working together to create a shortage in labour in many industries.

The danger for organizations will be situations where there is both an external force and an internal force on involuntary downsizing. This would occur when there is, for example, a shrinking of the labour force and an internal environment that is causing a high level of turnover. The combination of not being able to retain employees effectively and not having an adequate labour pool from which to draw could leave an organization with a rapidly decreasing employee base.

**Consequences of Downsizing**

Voluntary downsizing can affect morale when the people who are left behind (the survivors of downsizing) have to pick up the slack and complete their own work plus the work of a position that has been left empty (Herman, 2004). Downsizing that is initiated through intentional managerial actions is fraught with negative consequences even though downsizers expect to take advantage of lower overhead, less bureaucracy, faster decision making, smoother communications, greater entrepreneurship, and increases in productivity (Cascio, 1993). Surviving employees become narrow minded, self-absorbed and risk averse (Cascio, 1993) and move from grief, to resistance to change, to fear and distrust all while they are required to complete more with less (Grossnickle, 1996). In addition, strategic human resource initiatives may be affected thereby impacting the long-term competitive advantage of the firm (Chadwick et al., 2004). The question that arises when looking at organizations that experience downsizing due to a shortage of labour is whether or not these effects are exclusive to voluntary downsizing situations and if they do appear in times of involuntary downsizing, will the impact be comparable, less, or worse? The differences in the causes of downsizing may impact the responses of the employees who remain with the firm. Survivors may have different reactions including commitment to the organization, job satisfaction and perceptions of fairness depending on whether the downsizing has been voluntary or involuntary. Research in these areas will be needed in the future as organizations learn to respond to involuntary downsizing forces.

**Conclusion**

The research on voluntary turnover, downsizing, and restructuring has developed a wealth of knowledge from which organizations can draw insights to facilitate increased organizational performance in periods of change. However, with companies across Canada as varied as trucking, retail, manufacturing, and exporting facing a potential long-term drought in terms of skilled labour (Grant & Sethi, 2006), voluntary turnover, downsizing, and restructuring should expect some increased attention by researchers in the future. The researchers will need to take a new perspective, though – one that removes the assumption of renewable human resources.
References


