



Opportunity Amidst Recovery: the Value to Profit Model

2011 IMPACTABILITY REPORT

Covering the years of 2007 to 2010, the Celerant Consulting Annual Impactability Report looks at internal and government data collected during one of the most tumultuous times in American economic history.

Business leaders with track records of growth and sustainability have long understood that the only constant is change. The worst recession to rock the country in generations placed that maxim center stage – indeed, there was in most cases no opportunity to move forward without changing. In the gradually expanding wake of that global economic crisis, managers at every level are adapting to shifting conditions brought on by a new operational climate. The future is as uncertain as ever, but there are distinct managerial lessons that will lead to more stable, productive organizations.

A field study conducted by Celerant Consulting examined the value created within organizations, and determined which areas of the enterprise are most prone to lagging in productivity and which can be impacted to improve output. The resulting Annual Impactability Report breaks down workforce time into value adding (VA), non-value adding (NVA), and non-value adding but required (NVAR) activities.

Perhaps most important, the study drew firm correlations between ideal employment levels and company output. There is a fine line between building a workforce focused on value and one that fights against it, and leaders who strike the right balance can be more effective at turning value into profitability.

During the downturn, layoffs were a common first choice of budget trimmers – and all too often those measures

were mistaken for value creation. Mass reductions in labor can improve the bottom line in the short term, but studies have shown time and again that they can also introduce long-term, damaging effects on company performance.¹

The road less travelled during this period was to better employ existing resources to maximize value. In terms of manpower, this entails striking a balance between the size of the workforce and its value creation by ensuring that employees spend more time adding value to the final product or service. Though it may seem an obvious finding, national and multinational organizations consistently missed this balance; the annual assessments of field data show that employees across the board spend less than one-third of their time so engaged. Even small improvements can result in significant savings, preserve jobs, and strengthen both individual companies and the overall economy.

This period of recovery is an ideal time to re-evaluate the balance, as executives are increasingly focused on preparing for the future and generating more revenue now that the economy is growing again.² Previous studies found that during darker days, the attention of business leaders was concentrated squarely on trying to cut costs. It is clear the economy is turning a corner, and those who truly wish to position their company for more robust growth would be wise to increase the amount of value created by each employee.

¹ Cutting Costs Without Cutting People, Harvard Business Review Blog, Maurice Ewing, April 4, 2011

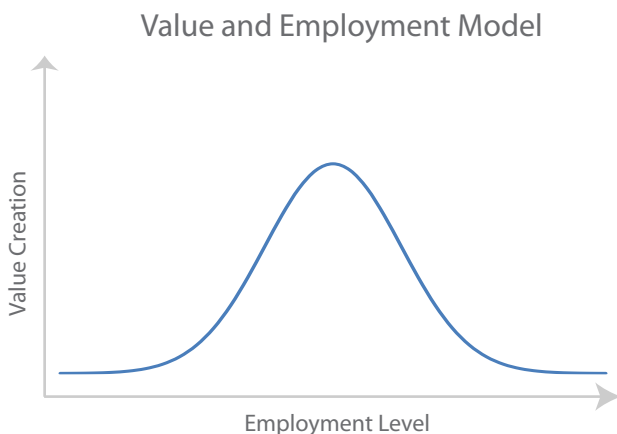
² Leaders of Change: Companies prepare for a stronger future, Celerant Consulting 3rd Annual Change Management Survey

OPPORTUNITY AMIDST RECOVERY: THE VALUE TO PROFIT MODEL

To accomplish the goal of controlled growth, companies should consider a “Value to Profit” model.

The “Value to Profit” model is captured by a cross-reference of Celerant Consulting and Bureau of Labor Statistics’ (BLS) data, which demonstrates an extremely strong correlation (.891) between rising value-added time and increased output in manufacturing across all sectors. Simply put, employers who can drive up the amount of value created by employees will see their output rise almost in equal measure.

That finding may seem self-evident, however less instinctive is another balance that must be struck: over-employment can be as destructive to value as running on a skeleton crew. A strong correlation (.775) exists between manufacturing employment and value creation, with the optimal ratio of employees to output for any given company expressed as a bell curve.



If the staffing level is to the left of the peak, representing too few employees, they will be unable to produce the most profitable level of output. Too many employees, on the other hand, will weigh down an operation with additional costs and unneeded levels of complexity.

Finding the perfect balance is difficult, but evidence points to some indicators that light the path. In the high-growth bubble years preceding the recession, the US economy was on the right hand side of the bell curve. When the economy plummeted, the position on the curve swung well past the peak and landed on the left. This overreaction compounded the downturn and cost more than 10% of American workers their job.

Healthy companies that remain resistant to hiring despite being on the left hand side of the curve are destroying their own potential for value creation. The opportunity costs of low output due to a workforce insufficient to meet demand are potentially tremendous. Many companies particularly those that reduced staff during the downturn could create value in the recovery by hiring additional employees.

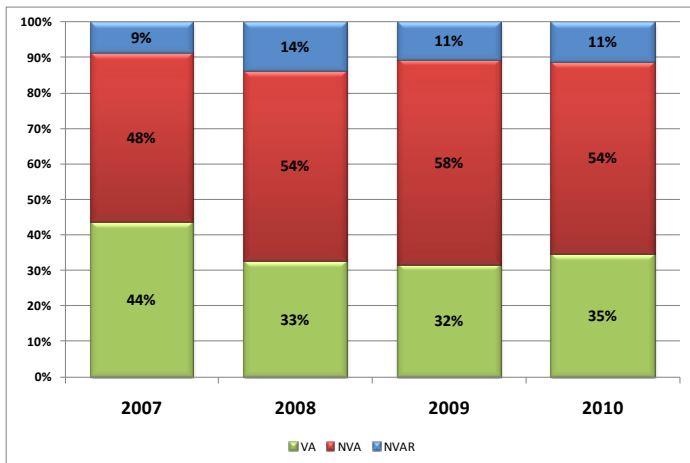
As revenues regain stability, though, employers must be cautious about over-hiring. Taking a lesson from the downturn means following a slow, steady increase in labor that is combined with training and organizational road maps designed to maximize the value of each employee. In this manner, non-value adding (NVA) time can be held at bay and companies can better track their output directly to the ideal balance of people, processes, and value.

The multitude of impacts and The Great Recession.

REVERBERATIONS FROM THE RECESSION

The multitude of impacts – human, corporate, political, and more of what has come to be known as The Great Recession have been well reported, but often left untold are the psychological ramifications it has had on American corporations. At the bottom of the downturn, when uncertainty about the future was widespread and another round of pink slips seemed to lurk around every corner, executives were desperate to prevent their companies from being pulled under by the economic undertow.

2007 - 2010 Value Add Impactability



With well more than half of the time employees spent at work not adding value to the end product, each wasted minute seemed to be an opportunity. Impactability (the ability to positively impact a specific activity) spiked during particularly challenging periods such as year-end 2009, showing that executives were looking for improvements everywhere -- perhaps even where they did not exist.

With an ominous shroud enveloping the economy, no job or company was safe. The unemployment rate, already on the rise, shot up nearly 2.5% in 2009 and peaked with more than one in 10 workers unwaged and countless more underemployed.³

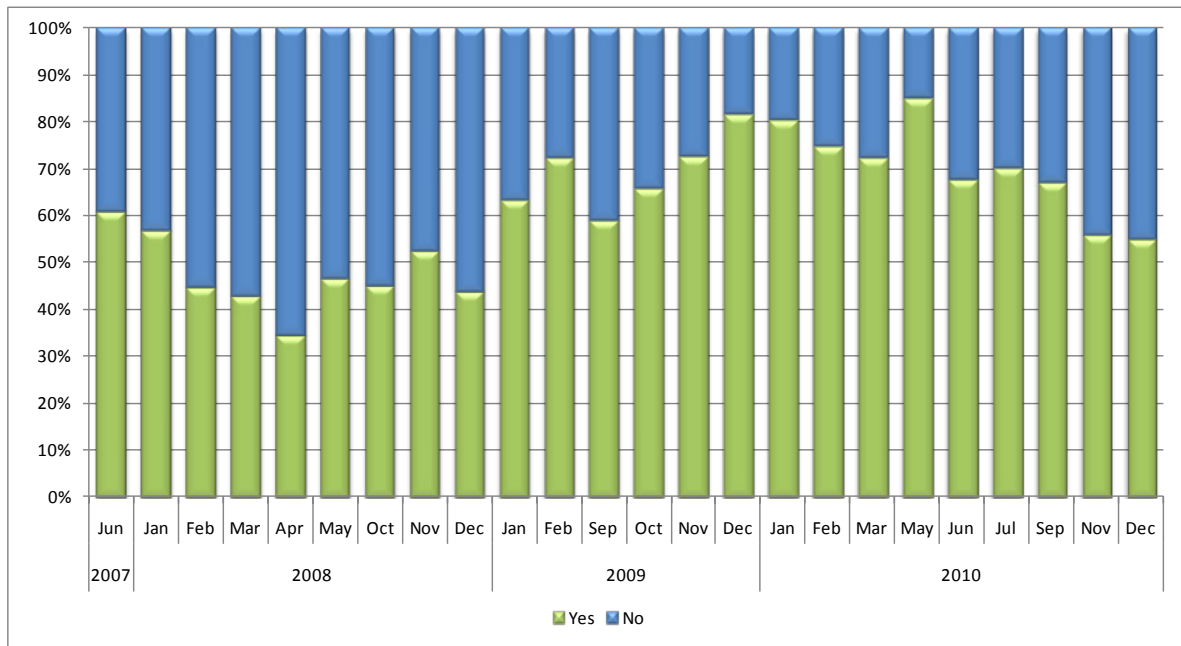
Acutely aware of the dire conditions in which they were operating, the NVA time employees spent came into clear focus for employers. With careers and mortgage payments on the line, every manager, supervisor, and front line employee was looking for opportunities to cut costs and prove their value.

As profits begin to rise, job losses subside, and the economy gains upward momentum, the pressure business leaders felt in the late part of the last decade is beginning to abate. Not surprisingly, field data from the same time period shows a corresponding downward slope in the amount of impactable NVA time they see in their employees.

The recession officially ended in mid-2009, and while growth rates are still suboptimal, the situation has improved. The recession did not begin or end everywhere at the same time, nor did it hit each region with the same severity. It likewise took time for the idea that the bleeding had stopped to seep into the collective consciousness of American businesses.

³ Labor Force Statistics from the Current Population Survey, Bureau of Labor Statistics

Impactability for Production



Impactability spiked at the end of 2009 and the beginning of 2010, and as the stock market climbed impactability took an opposite track. Executives are clearly feeling more confident about the future but, as a previous Economist Intelligence Unit study for Celerant Consulting showed, more than half of them reduced headcounts before attempting to create efficiencies. Indeed, only 22% implemented any changes in processes in response to the downturn. While that may have improved the short-term picture, it created an even larger long-term problem when seen through the lens of historical productivity.

PUTTING A COMPANY'S MOST VALUABLE RESOURCE TO WORK

While productivity as measured by the BLS is an important measure of how a company or economy is doing, it is not the same as value creation, nor does it automatically imply increased profit. It should give employers great pause to consider the loss of value they are seeing from their highly developed workforces. Business leaders often tout that their most valuable resource is their employees, but the fact is that almost half their time could be better spent.

Few would believe that either they or their employees contribute as little as they do. When Key Performance Indicators (KPI) are established for both individuals and teams, however, it not only becomes clear that there is great room for improvement, but occasions for improvement begin to present themselves. Once established and implemented, frequently communicating the KPI results will help employees develop a sense of ownership and will motivate them to produce increasingly superior results.

Employees who are given the structure and tools to increase the amount of value they create, even by just a few percentage points, can save struggling companies and rally those that are well positioned to take advantage of the recovery to even loftier heights of profitability. When forward thinking businesses adapt by focusing more of their workforce on value, they will be less likely to be pulled down by pitches in the economic climate and more likely to stay stable, profitable, and ahead of the curve.

About Celerant Consulting's Annual Impactability Report

Covering the years from 2007 to 2010, the Celerant Consulting Annual Impactability Report looks at internal and government data collected during one of the most tumultuous times in American economic history.

The Celerant data consists of over 21,000 individual log entries totaling more than 2,500 hours of direct observation of employees across 22 firms in the United States and Canada. In 2010 alone, data for the equivalent of more than 80 workdays was collected.

In a minute by minute breakdown, time was divided into three categories: value added (VA), non-value added (NVA), and time spent on activities such as regulatory reporting that do not add value but are required (NVAR). All NVA time was further divided into impactable time – that is, time that can be easily converted into VA time -or non-impactable.

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