WORKFORCE INSTITUTE

Retaining Your Best Hourly Workers

Introduction

Why is it important to manage the turnover of hourly employees?

According to the U. S. Department of Labor, hourly workers have an average turnover rate four times higher than that of their exempt counterparts. Do you know what the turnover is among your hourly workers? If you're looking at blended turnover rates, you may be understating the problems you have with hourly and overstating the problems you have with salaried.

It's important to manage the turnover of hourly employees because of the costs and risks associated with excessive turnover. Let's take a closer look at both the costs and the risks.

Costs
The population of hourly workers in the US tops 75 million employees. It's expensive to keep hiring and replacing even low-wage earners. Replacement costs will vary depending on the industry, the person's wage, and the scarcity of the skill set that you are trying to backfill, but some studies show it costs as much as $8,000 to replace an hourly low-wage employee[1]. Here are some recent estimates:

- The Hay Group study pegged the cost of replacing hourly workers at six months' salary; the replacement cost for a full time employee earning $8/hour would be $8,000.
- For a call center, the most conservative direct-cost estimate of replacing an employee was 50% of the annual salary[2]. This includes costs associated with recruitment, orientation, training, and ramp-up.
- According to the U.S. Department of Labor, it costs one-third of a new hire's annual salary to replace him or her. For an $8/hour employee, the costs would total over $5,000.

[1] The cost associated with turnover can be attributed to
- Cost of advertising the vacant position
- Cost of screening and pre-employment tests
- Lost productivity
- Cost of orienting and training the new employee
- Lost sales for employees who take customers with them
- Manager's time to interview, screen and test candidates
- Management time to train new employees

[2] http://www.sashacorp.com/turnframe.html

- A study by Coca-Cola Retailing Research estimated total direct and indirect costs of replacing a supermarket cashier earning $6.50/hour was at least $3,630. This is about 28% of a yearly full time salary.
- The American Hotel and Motel Association cites $2,500 for direct costs and $1,600 for indirect costs, to total $4,100 to replace a worker making $8.00/hour. This is about 26% of a yearly full time salary.
- Cornell University's Hotel School estimates that replacing a front desk employee in a Miami hotel would cost over $5,600.

These costs may seem insignificant until you realize how frequently you incur them, especially if you're in an industry plagued with high turnover rates like hospitality and retail. According to AberdeenGroup, average turnover can range from over 50% for line-level hotel and motel employees, to 104% for specialty stores, to more than 200% annually in fast food chains.[3]

Risks

Any turnover causes disruption to internal processes. Very high turnover can also result in poor morale which in turn leads to decreased motivation from the employees that remain.

Service companies with high turnover are at risk for poor customer service. In manufacturing facilities with high turnover, efficiencies, productivity, and output will all suffer.

In addition, high turnover can give your company a reputation that you don't want; poor turnover can reflect poorly on your brand.

Why fix it? There's a big bottom line impact

Several studies have shown that being a great place to work is linked to outstanding business results. According to Franklin Research and Development, the 100 Best Companies consistently outperform major stock indices[4]. For example, comparing the performance of the "100 Best" to Standard & Poor's 500 performance from 1998-2006, their Reset Portfolio[5] averaged 14% over 1998-2006 and their Buy and Hold Portfolio[6] averaged 11%, whereas the S&P averaged only 6% for the same time period.

Here's another example: Hewitt researched the best employers in Australia and found that they have stronger three and five year growth (as measured in revenues and profits) than other participants in the study and they out-perform their industry sector[7].

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[3] AberdeenGroup. "Hourly Hiring Management Systems: Improving the Bottom Line for Hourly Worker-Centric Enterprises", June 2002, page 8.

[4] http://www.greatplacetowork.com/great/graphs.php?page=2

[5] The Reset Annually portfolio invests equal dollar amounts (at the beginning of the year) in stock in each of the year's 100 Best publicly traded companies. The portfolio is liquidated at the end of the year and the proceeds are invested in the subsequent year's list of 100 Best.

[6] The Buy and Hold portfolio invests equal dollar amounts at the beginning of 1998 in the stock of each of the 100 Best publicly traded companies and holds these stocks through 2006.

[7] http://unpan1.un.org/intradoc/groups/public/documents/APCITY/UNPAN010023.pdf

Any discussion on this subject inevitably leads to the question of causality. In *The Human Capital Edge*, authors Pfau and Kay[8] definitively proved that good retention practices lead to good business performance, not the other way around.

Let's get started!

The series of articles that we'll publish over the next twelve months will focus on creating and executing on retention strategies for the hourly workforce. This month's article will cover:

- How to build a retention strategy
- What is the best turnover rate?
- How to evaluate your current state and understand the root causes
- How to find best practices for reducing turnover
- What metrics should you examine?
- What is the required investment and the expected return?

Upcoming articles will cover:

- Sourcing for retention
- Hiring for retention
- The role of the manager
- The challenge and opportunity surrounding immigrants
- The role of economics and local demographics on turnover
- Technology as an enabler for deploying best practices in retention

Each article will include interventions you can deploy to mitigate unplanned turnover, examples or a case study, and tools to help you get started. Set up your RSS feed now to be informed when new articles are posted.

How to build a retention strategy

Start at the top

The organization's retention strategy doesn't exist in a vacuum – it springs from corporate strategy. So the first step in creating a retention strategy is to define the context: what is the corporate strategy? Then drill down and determine which workforce strategies and initiatives would support the corporate strategy. Continue to drill down further, and craft HR tactics to support the workforce strategy and then, finally, design supervisor practices that will support the tactics.

> For example, Southwest Airlines is dedicated to "the highest quality of customer service, delivered with a sense of warmth, friendliness, individual pride, and company spirit. … [They offer] employees a stable work environment with equal opportunity for learning and personal growth. Creativity and innovation are encouraged for improving the effectiveness of Southwest Airlines.[9]"

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[8] Bruce Pfau and Ira Kay, *The Human Capital Edge* (New York: McGraw-Hill, 2002).
[9] http://manonamission.blogspot.com/2005/04/southwest-airlines-luv-mission.html

> Whole Foods Market, a leader in the quality food business, aims to take food retailing to a new higher standard. They guarantee 100% product satisfaction and strive for outstanding customer service. They seek employees who are energetic, intelligent and enthusiastic about serving customers. They also provide continuous learning opportunities about company values, food, nutrition, and job skills as part of their commitment to promote from within.
>
> These two companies have envisioned a specific customer experience that they strive to deliver, and they attract, develop, and retain the type of employee who can deliver this experience. Obviously, your retention strategy won't be the same as Southwest or Whole Foods because your corporate goals and your corporate culture are different.

In support of your corporate strategy, your key workforce initiatives might be to build the workforce of the future, remain a union-free workplace, improve utilization, improve bench strength, or lower labor costs. As you further develop cascading goals related to employee retention in particular, the list might include:

- Improve hiring and screening practices to ensure better job fit
- Speed time to hire[10]
- Decrease time to train and mobilize new hires
- Reduce turnover costs
- Reduce hiring expenses
- Improve retention of high performers
- Improve the skill level of the employees that we already have
- Identify and get rid of poor performers faster
- Move supervisors with poor people-management skills out of those positions

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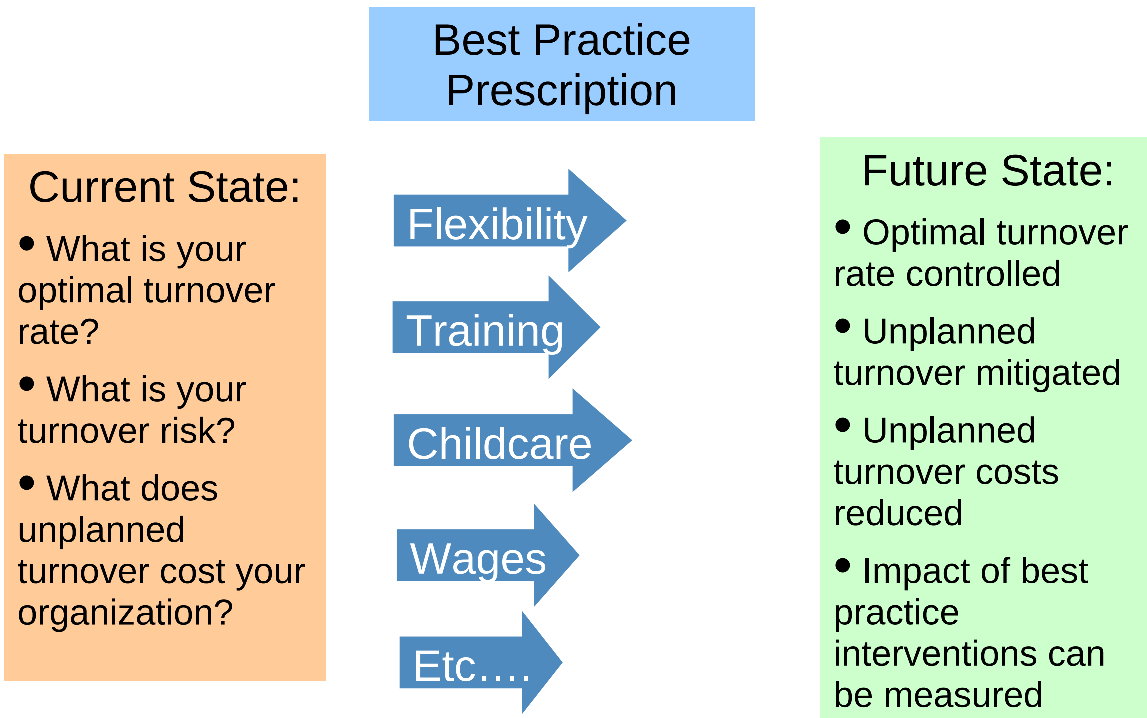
[10] Hourly workers are typically on the job market for an average of five days per AberdeenGroup, "Hourly Hiring Management Systems: Improving the Bottom Line For Hourly Worker-Centric Enterprises". Most of the applicants are walk-ins, so it's important to be able to act quickly or the applicant will move on to the next potential employer.

Steps to build the retention strategy

A retention strategy can move you from your "as is" state to a different, desired state. In describing your desired end state, be as specific as possible (answer the questions who, what, when, where, and how much).

Figure 1: Designing a retention strategy



Here are the steps in building the strategy:

- Define corporate strategy
- Cascade it down to workforce initiatives and then to hiring and retention strategies
- Create a meaningful model in which to classify your hourly employees, whether it is based on skill level, full time vs. part time, seasonal workers vs. year round, corporate vs. the field, front of house vs. back office, etc. See below for a discussion on this.
- Describe the retention landscape as it exists now. For each employee population, what are your current patterns of turnover and retention? What hiring, on-boarding, training, supervisory, and compensation practices do you have in place now? What are the current costs associated with turnover?
- If turnover is higher than desired, determine root causes.
- Envision the desired end state, as determined by the corporate goals and culture and as limited by your macro-environment. Don't be overly ambitious - your target for Year One might be simply to get metrics in place and to start to "move the needle" perceptibly. Ultimately, you want to achieve the "right" turnover target that achieves the optimal balance of productivity and ROI for the organization. See Figure 1 (above) for ideas on how you might envision the future state.

- Examine the gap between the as-is state and the desired state. Define what is required to get from where you are now to the desired state.
- Brainstorm how can you improve results at each step (source, attract, select, hire, on-board, engage, train/develop, deploy, and reward) to incrementally improve overall retention. Develop tactics for each employee population based on best practices and on what each population values.
- Consider the financials – what will it cost to deploy the interventions that you're proposing, and what are the benefits of improving retention?
- Get buy-in from all stakeholders before implementing changes, and get help if your group is not adept at managing change. Determine what tools the front line managers will need to better manage the hourly population.
- Define metrics and motivators, and be prepared to measure results.
- Repeat and refine process, tactics and metrics.

Start with a model of your hourly employees

As we mentioned above, to have a meaningful discussion about the retention of hourly workers, we need a taxonomy of this population. The population of hourly workers is actually very diverse. Some hourly workers, such as nurses, are highly skilled and well-trained, and the competition for these workers can be intense. Other workers may perform entry level jobs which require very little training, experience, or even English language skills. These workers might be seen as interchangeable and the competition for them is less intense.

For our discussion, we'll adopt the four-square model below to classify hourly workers. This model will be more fully developed in a future article by Dr. Steven Hunt.

Figure 2: Model to classify hourly workers

	Work is transactional	***Work is contextual***
Skilled worker	Example: Skilled mechanics and technicians.	Example: Nurse, head chef. Resemble professional jobs.
Unskilled worker	Example: Entry level line job in manufacturing. Language skills not necessary.	Example: Cashier at supermarket. Need English skills.

The transactional worker is engaged with things, like machines or repetitive processes in manufacturing, whereas the contextual worker's job is to deliver an experience to another human being. As one moves "east" along the x-axis, one relies more heavily on skills like communication and empathy. As one moves "north" along the y-axis, one relies more heavily on hands-on skills with machines and processes.

The residents of the upper right quadrant are very similar to salaried professionals in their abilities and skill levels. They might include registered nurses, executive administrative assistants, and legal secretaries.

We recommend that you brainstorm a meaningful way such as the one described above to classify your workers, because you will have different retention strategies for each group of workers. The operating assumptions and interventions for retention will differ depending on which population you are trying to influence.

II. What is the best turnover rate?

Most managers acknowledge that the turnover rate can be too high because, as we discussed, it causes disruption to internal processes and to customer service, and it's expensive to churn employees.

And most managers know intuitively that very low turnover might pre-dispose the organization to stagnation. Without new employees, you aren't getting new ideas and energy. Unless you're growing, low turnover means that existing employees won't see vacancies into which they can move and advance their careers. A department with little or no turnover will be seen as a dead end, and the manager will have difficulty attracting internal applicants when the rare opening *does* occur. Another drawback to low turnover is that, during economic downturns you might be forced to lay people off, which demoralizes the remaining employees.

Very low turnover might be a warning sign that you're spending too much on pay and benefits, especially if the pay has outstripped the value provided by entry-level workers. Or, if involuntary turnover is very low, it may be an indication that your managers are not weeding out poor performers.

The optimal turnover rate is the one that maximizes productivity. The optimal turnover rate is different for different industries, companies, jobs and locations.

III. What is your current turnover rate?

In light of the ambiguity regarding an optimal turnover rate, a good place to start is with an understanding your own current turnover rate and the average turnover for other companies in your region and in your industry.

Your actual turnover rate

To really understand turnover, break out voluntary from involuntary. To calculate your own turnover rate, take the number of voluntary separations over the past year (don't include retirements) and divide by the total number of employees[11]. You might want to calculate full time employees separately from part-time employees, or convert the count of part-time employees into FTEs.

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[11] Some people prefer to divide by the average number of employees for the year as opposed to the total number of employees at year end.

It's tempting to derive a formula that captures aspects of turnover that are unique to your situation (seasonality, for example), but we recommend that you use the same formula that your peer group or your industry uses, so that you can make meaningful comparisons to them.

Compare to industry averages

To find industry averages, you can turn to many sources:

- The Bureau of Labor Statistics provides turnover information by region and by industry sector but doesn't break out hourly versus salaried employees.
- See the Job Openings and Labor Turnover Summary produced by the Department of Labor.
- General business associations such as the American Management Association, the American Payroll Association, and the American Staffing Association can provide high level statistics.
- Magazines and trade associations in your industry might publish timely metrics. Your marketing and public relations firm can help you find both associations and magazines that specialize in your industry.
- Human resources magazines often have information broken out by industry sector, but not to the SIC or NAICS level. Your HR department probably subscribes, or you can find online versions.
- Human resource management associations, such as the Society for Human Resource Management (SHRM) are good sources but you have to join the association for access to their databases. It's very likely that someone in your HR department is a member.

See Appendix I for other sources.

When you are benchmarking, consider carefully how you define your industry and your competitors. Of course, you'll want to look at your peer group within your geography. But also ask yourself who you compete with for labor, not for customers. Your factories might be competing with a fast food franchise, a hotel, or a drug store chain for hourly workers. Your local Chamber of Commerce might be able to provide statistics to help you compete and succeed in your local market.

Your target turnover rate

To determine your target state, you can conduct web searches for information about specific companies in your area or your industry that have been successful at reducing turnover. Consider information from the Great Place to Work Institute, Inc., which supplies the data for Fortune's "100 Best Places to Work" list. Their list below demonstrates the retention gaps between top companies and the industry averages. At a high level, this gives you both a standard and an ambitious target. Since the best places outperform other companies financially, you might want to mimic their tactics.

Figure 3: Turnover at Best Places to Work vs. Industry Averages. Note that this is full time, hourly and salaried workers.

	Best Places	Industry Average
Computer/High Tech/Wireless	5%	16%
Construction/Building Materials	10%	26%
Financial Services	11%	13%
Hospitals	8%	20%
Hotels	20%	49%
Industrial Service/Manufacturing	10%	15%
Retail	18%	33%
Transportation	4%	17%

Number of full time voluntary separations over the past year (excluding retirements) divided by the number of full time employees. Comparative data provided by BLS.

Use these numbers for guidelines but remember, only you and your management team can determine what your target should be.

What are the root causes of turnover in your organization?

If your turnover rate starts to soar, perhaps the economy is improving and employees are quitting in order to make a bit more money, try a different type of job, or shorten their commute.

The economic environment plays a large role in determining your turnover rate. Full employment in your region will make it harder for you to retain employees. In tight labor markets, retention suffers and wages go up. Raising salaries is a knee jerk reaction, and not a good practice. If there is full employment, you’re just going to have a harder time retaining people. Although some of your tactics might change when economic conditions improve, your basic **strategy** should not change.

If your turnover rate is much higher than industry standards or local competitors, then you can’t blame it on the economy. Figure out the root causes by conducting interviews and looking for trends in your data. Consider external as well as internal factors that might explain the patterns that you see. Here are some questions to research:

- When did the rates start to climb? Was there something else external to the company that occurred at the same time, for example, did the public transportation schedules change? Did a new employer arrive on the scene, offering higher wages? Is this a seasonal pattern?
- Do new hires quit or are the people with more service quitting?
- Are employees of a certain age quitting? For example, are your Generation Y hires quitting but your Gen X hires are settling in fine? Maybe your corporate culture is a better fit for the latter.
- Are many of your workers reaching retirement age?
- Are higher rates associated with individual managers? Many surveys indicate that the manager is a very important factor in how long employees stay. Are higher rates associated with specific facilities/stores, or regions?

- Is there a correlation between quit rates and the shift that the people work? Many people quit because the work schedules create friction in their lives, and their managers can't easily accommodate employees' needs.
- Is there a correlation between quit rates and the training and on-boarding that employees received?

Once you identify the root causes, you can start to formulate strategies for conquering the problem. See Appendix II for a list of risk factors and possible interventions.

IV. How to find best practices for reducing turnover

Watch your assumptions

Volumes have been written about retaining salaried workforce. And many surveys such as the study by Towers Perrin[12] which surveyed over 40,000 employees, roll the results from hourly and the salaried employees together. So it's hard for supervisors to research retention tactics for the subset of hourly employees.

Since hourly worker are more likely to be young, entry-level, and maybe not English-speaking, the retention tactics that you deploy for them may differ from than the tactics that you'd apply to increase the retention of older, more established workers.

However, be careful about your assumptions with regard to hourly workers. Surely, some of them have opted for part time or hourly jobs so that they can pursue other interests and obligations outside of work. For them, the job is a means of putting food on the table and paying bills. But don't assume that all hourly workers fall into this category. Some are just starting a career, and others are in transition. Many hourly workers are very dedicated to their profession, and they identify proudly with their chosen line of work. Good examples of this are described in a recent article by David Creelman, "**Are Hourly Workers Professionals?**", in which the author explores the qualities that differentiate professionals who happen to be paid by the hour from those who are merely punching the clock to earn a living.

[12] Working today: Understanding What Drives Employee Engagement: The 2003 Tower Perrin Talent Report

How to find out where you should invest

In which retention practices should you invest? The answer to that question will depend on many factors, including your geographic location, your current "as-is" state, which employee population you're addressing, and what results you desire. Future articles will address this topic more fully. However, here is a list of steps you can take to discover what tactics would work.

- Look at what successful companies do, especially those in your industry
- Look at departments and managers that excel at retaining good people
- Ask what motivates your workers
    - Use exit interviews and compile reasons for voluntary terminations
    - Use pre-exit interviews to find out why employees stay
    - Compile a list of tactics that your company might consider and ask your employees to rank them

For a list of popular tactics, see Appendix II at the end of this article. But be forewarned that there is no one-size-fits-all solution, and we recommend that you conduct the diligence outlined above.

V. What metrics should you examine?

When you build your retention strategy, specify the metrics you'll track. Over time, you'll be able to establish a range of acceptable and unacceptable results. Remember that results will be influenced by exogenous factors, so you should track local unemployment rates and industry turnover rates for context.

Examples of metrics related to retention might include:

- Reduce turnover among desired populations by x% by year end
- Reduce number of quits within the first 30/60/90 days of service by x
- Reduce costs associated with re-filling positions by x% or $y
- Reduce time spent by managers in re-filling positions by x hours
- Employee length of service increases from x weeks to y weeks by year end
- Number of managers who reduce their turnover rises by x%

VI. What is the investment required and what is the expected return?

Some interventions are easy and inexpensive to implement. Others can be expensive to offer on an on-going basis so you should evaluate the costs and the benefits of the interventions under consideration.

If you know the value of retaining an employee for an extra month or pay period, you will be able to weigh that value against the costs of the interventions that might improve retention[13]. But it's hard to make direct linkages between implementing a new retention tactic and financial

[13] There are many tools available on line to help you determine the cost of employee turnover.

results because there are so many intervening factors. One way to cope with this ambiguity is to conduct pilots with a small group of employees or with an isolated facility. Introduce each intervention one at a time so that you can isolate the factors that create an impact on retention, revenue, and profits.

Another issue that complicates your efforts to prove a return on your investment is that many of the benefits of increased retention are “soft”, and they will be difficult to quantify. For example, how do you put a value on an employee’s increased knowledge, experience, or engagement? These are all factors that are likely to improve as turnover is reduced.

Here’s another way to look at the costs associated with turnover; this example is from TJ Schier, a consultant to the restaurant industry. Based on the industry average turnover of 200%, a 30-employee restaurant grossing $800,000 a year, averaging 10% profits could be working up to May 17th just to cover yearly turnover costs. And that's assuming that the costs associated with turnover are only $500/employee[14]. It might make more sense for you to present your case using a similar approach instead of trying to spell out all the direct and indirect costs and benefits. This approach helps people to realize the huge costs associated with turnover.

Summary

Improving retention of hourly workers is not impossible. And the benefits of doing so have far-reaching effects, as the 100 Best Companies demonstrate.

The Workforce Institute recommends building a retention strategy for hourly workers in order to control the costs and risks associated with turnover. There are many interventions that you can deploy that can reduce turnover, but it’s important to understand your unique situation – the economic environment, the corporate strategy, the types of positions that you have, and the demographics of your hourly employee population – before you design your strategy.

Set up an RSS feed to receive the articles that the Workforce Institute will publish on how to build a retention strategy for the hourly workforce, because improving retention of your good hourly employees can save money, increase revenue, and improve the customer experience.

[14] http://tvtrainer.blogspot.com/2007/01/high-costs-of-employee-turnover.html

Appendix I

Additional sources for statistics related to employee turnover.

- Human Capital Institute **http://www.humancapitalinstitute.org/hci/hci.home**
- Institute of Management and Administration **http://www.ioma.com/**
- International Association for Human Resource Information Management **http://www.ihrim.org/**
- International Workforce Management Benchmarking Association **http://www.iwmba.com/**
- Personnel Today **http://www.personneltoday.com/home/**
- The Future of Work **http://www.thefutureofwork.net/**
- Firms that specialize in human capital research such as Saratoga (a service offering of PricewaterhouseCoopers) publish research and case studies. **http://www.pwc.com/extweb/service.nsf/docid/de40ffb0d40981d385256f17005397cd**
- Search the web for your industry. For example, a list of retail magazines can be found at http://www.ecr.ryerson.ca/retin_01.html
- Analysts and experts in your industry, for example, the PeopleReport for casual dining, The Radson study for technology, etc.

Appendix II

Here is a list of factors that should be considered when you evaluate your company's turnover risk. Apart from the first few items (your macro environment), the list can also be viewed as tactics for improving retention. The most effective tactics, would, however, vary for each population, age group, industry, and job (refer back to our four-square model). Ask your employees to share additional ideas with you.

Questions to ask to determine your company's turnover risk

What is the local overall unemployment rate for hourly workers?
What is the unemployment rate for this particular position?
What industry are you in?
What is the company's retention policy?
Are you in close proximity to other companies with whom you compete for workers?
Are you known as a great place to work?
Is there a union?
Are you near public transportation?
Do you conduct stay and exit interviews?
Do you examine retention by manager?
Do you track trends over time and reward managers who achieve retention goals?
Do you identify top performers and have retention plans that encourage top performers to stay?
Do you offer:

- Competitive compensation
- Good benefits (and do you know which benefits your employees value most?)
- Retention bonuses or anniversary bonuses
- Flexible work hours/schedules
- Training
- A realistic picture of the job before people start work
- A low-stress environment
- Special non-monetary rewards and recognition
- Cash bonuses
- Opportunity to earn more money
- Child and/or elder care
- Unpaid leaves of absence
- Jobs for friends and relatives
- Good relationships with co-workers
- Meals at work
- Open communication
- Methods of involving the employee's family, for example, having on-site family picnics and outings, offering donations to the local schools, buying graduation gifts for employees' children, etc.