

Key Metrics for Today's Talent Economy

The best performing companies are measuring the results of the staffing process – workforce quality and retention – in association with traditional staffing efficiency metrics to calculate their return on staffing.

By Yves Lermusiaux and Alice Snell, iLogos Research, a division of Taleo

When it comes to performance, your company is on its game. Company stock has grown by more than 300 percent in the past five years. Your team of devoted financiers makes your balance sheet look impeccable, the sales team has improved its close rate by nearly a factor of two, and production efficiency is second to none. Corporate branding increased its superiority three years in a row and allowed a comfortable increase in margins. In the continuous pursuit of corporate performance excellence, what else could you do?

Intuitively you know that well managed talent drives superior enterprise performance, but the lack of measurable results has prevented your organization from going further. However, there is a simple management tool that can enable you to monitor the investment in the most important asset of your organization: talent. And even more crucial, it gives you the blueprint to impact your talent management initiative quickly.

Too often the “people equation” is left to industrial psychologists to decipher or to the staffing department to evaluate with manager satisfaction surveys. Those two approaches have merits. For corporate management and shareholders, however, a more relevant metric is the ratio of outcome to input. Historically speaking, revenue per employee (RPE) has been the yardstick. Today – in an era of increased use of contingent labor and outsourcing – it is time to review this measurement.

Revenue per Employee Is a Flawed Measure

Every organization strives toward optimum usage of funds, and many benchmarks have been created to optimize performance. For RPE, the traditional metric for labor productivity, there is often a large disparity in the results. Why does there appear to be such a spread in labor productivity? The great variation of this metric across companies in the same industry shows either that many have great improvements to make or that this metric is less than reliable because it ignores other factors. Certainly, some corporations can dramatically improve their labor productivity; yet more significantly, the metric of RPE is increasingly inappropriate.

The problem with RPE is that it does not reflect the investment effort or input required to achieve the output. More mean-

ingful from a business perspective is not the ratio of revenue generated per the number of workers, but revenue generated in proportion to total labor costs. In short, RPE has become increasingly inaccurate for one major reason: Companies have been using more and more contractors, outsourcers and general contingent labor in the last 10 years. Yet simultaneously it is ever more important to measure labor productivity since in this service economy it is the most substantial expense.

Instead of the traditional RPE metric, iLogos recommends determining revenue per total labor spending through a new metric – return on workforce (ROW) – that monitors and best reflects the value the total talent returns to the organization.

Total labor cost reflects the total compensation of full-time employees as well as the cost of contractors, temporary workers and others who do not commonly appear in the standard accounting of labor expenses. Using that total labor cost reduces the distortion that arises from various spending patterns on contingent labor. This helps leaders truly understand their corporate performance.

For instance, consider two competitive healthcare organizations (see Figure 1). Organization 2 has been claiming a better human capital efficiency with a couple of percent advantage

Figure 1 Comparison of Two Competitive Healthcare Organizations

	Revenue per Total Labor Spent	Revenue per Employee	Lead
Organization 1	247	\$145,169	11% on revenue per total labor spent
Organization 2	223	\$149,302	3% on revenue/EE

points on its benchmark. In fact, when we look at the revenue per total labor spent, it has an 11 percent disadvantage. In other words, this new metric better depicts the reality of human capital efficiency and consequently enables you to manage what really impacts your organization.

Sometimes the opposite distortion appears while using RPE in the context of utilizing off shored locations. Often this headcount is not as efficient on a per-head basis but is so much cheaper that

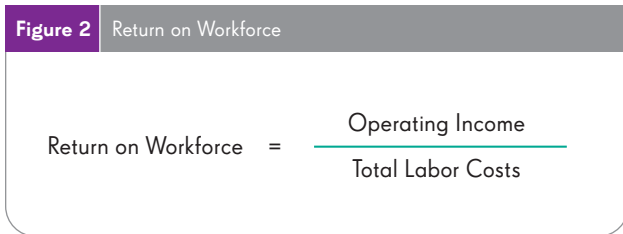
the traditional RPE is again the wrong metric to depend on to evaluate a strategic decision. Therefore the first conclusion for an executive today is to make sure to monitor the total

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cost spent on labor, which includes the traditional payroll data and the total contingent labor spending.

ROW and Workforce Levers

Accordingly, return on workforce can be used to monitor the true operating bottom-line influence of your utilization of your human capital. This ratio looks at the operating income generated compared to the total labor cost (see Figure 2).



Still, benchmarking the ROW among companies even in the same industry requires caution. One factor that must be accounted for is the level of outsourcing employed by a company. Outsourcing moves business functions and indeed whole departments off of the company's rolls. For instance, compare company A, which has all its IT support function in-house, with company B, which outsources all of its IT function.

Alternatively it may turn to workforce management for other ways to affect profitability. Increasing productivity by providing training to develop higher quality workforce skills, and improving motivation and minimizing factors that adversely affect productivity such as talent churn or absenteeism, will increase a company's ROW percentages (see Figure 3).

Low-Hanging Fruit: Improve the Talent Acquisition Function

Monitoring the ROW metric should emphasize that improvements in staffing are key, since staffing is the furthest point upstream in the human capital supply chain. Staffing quality impacts all downstream business functions, from motivation to turnover. The role of staffing is not only human asset acquisition, but also workforce assignment and matching talent to workforce requirements. A better deployment of human capital assets results in a higher ROW.

Unfortunately, though, the staffing function is too often seen as no more than a glorified administrative function, like the other traditional transactional HR functions. According to studies, labor costs as a percentage of revenue average around 40 percent, and in most companies it is the largest expense. Strikingly, less than 0.5 percent is spent to fund staffing initiatives, the single most important influence on workforce quality. It is time for organizations to distinguish talent management that literally

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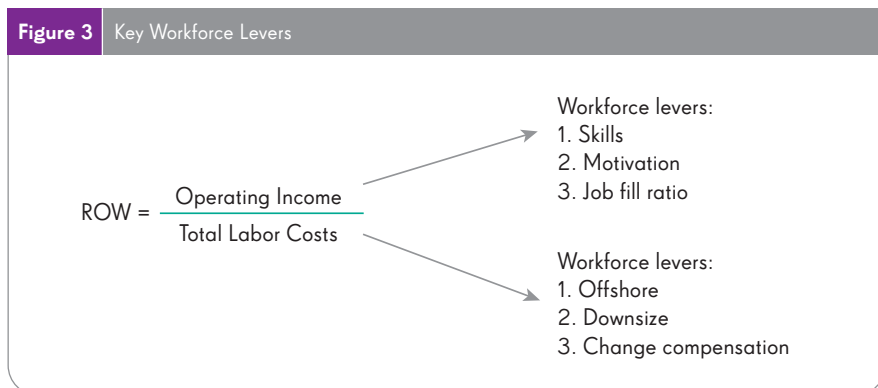
Company A bears all of the labor costs and accounts for them in the ledger as payroll costs, while labor costs for company B are buried within the outsourcing contract. Discrepancies that arise from this kind of organizational difference between enterprises may be introduced in the comparison, incorrectly reflecting a gap in inefficiency. As a consequence, the ROW metric is recommended first as an internal way to monitor progress on labor productivity. It may be used then to benchmark one company against others provided the benchmarks have a similar human capital structure.

To improve ROW percentages, a company may use nonworkforce-related strategies, such as better procedures, defect control and all the traditional efficiency methodologies. It can also employ strictly labor-related levers, by examining ways to decrease labor costs through offshoring or layoffs, or seek wage concessions from the workforce.

drives the organization versus transactional HR management that enables the organization.

Return on Staffing

iLogos Research has created return on staffing (ROS) as a way of measuring the return on an organization's staffing investment. ROS explores the relationship between input and output in the



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staffing process. Total staffing costs break down into fixed and variable costs.

- Fixed costs include recruiters' salaries, staffing infrastructure and overhead.
- Variable recruiting costs are made up primarily of sourcing costs, but may also include agency and assessment fees if applicable.

the number of days from the approval of the requisition to its being filled.

Turnover is another outcome of staffing. Involuntary turnover in the employee's first year of tenure is an indicator of a lack of productivity or a gross lack of fit with the company's culture. Turnover in subsequent years of tenure is an indicator of the loyalty of the company's workforce.

Today the best performing companies are measuring the results of the staffing process – workforce quality and retention – in association with traditional staffing efficiency metrics to calculate their ROS.

Staffing spending has three outcomes:

1. The staffing function's responsiveness in meeting corporate staffing needs;
2. The productivity or quality of the acquired labor; and
3. Retention of the new worker.

ROS is measured with four key metrics:

1. Cost per hire;
2. Time to fill;
3. First-year involuntary turnover; and
4. Productivity or ROW.

Cost per hire is a well-known metric, calculated by dividing the total staffing costs by the number of hires. Time to fill measures the responsiveness of the staffing function to corporate demands for labor. The metrics used to measure costs and cycle time are familiar, but their exact composition can be the subject of some debate. For example, the components included in cost per hire vary widely. Nonetheless each component is quantifiable and can be consistently calculated. Similarly, one has the choice of several key milestones in the staffing process to use in the design of a time-to-fill metric: For example, define time to fill as the number of days from the creation of a requisition to its being filled, or as

Efficiency and Effectiveness

The focus in the past has been on the staffing process itself, particularly on costs and cycle times. To measure the efficiency of a process is to measure its speed, use of resources and cost. Cost-per-hire and time-to-hire metrics are two measures of process efficiency. To measure how a staffing function is performing requires measuring both efficiency and effectiveness. Effectiveness of staffing as it contributes to corporate goals is reflected in the metrics for first-year involuntary turnover and ROW.

Too often staffing has been judged in isolation of its outcomes. Measurement of a corporate staffing function typically has been focused on direct cost savings and reduced cycle time. Today the best performing companies are measuring the results of the staffing process – workforce quality and retention – in association with traditional staffing efficiency metrics to calculate their ROS.

ROS and ROW represent important new metrics not only because talent management is the last area for corporate performance enhancement, but also because labor costs are the first and most important spending in this service economy. Studies have shown repeatedly that boards of directors are spending more and more time on people issues. Can you quantify your company's superior talent performance? ■

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