

Creating a Great Workplace: An ethical or economic duty?



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There is no doubt that the employer-employee relationship involves an *ethical* responsibility, as managing people has a direct impact on their welfare and happiness. But managers also have an economic or professional duty to maintain a positive working environment, as doing so may lead to improved profits for the organization.

Yet even though few would deny that organizational culture is important for the performance of a company, many leaders hesitate to take the steps necessary to improve the culture, as they worry that it will require significant time and resources. Adding to the challenge, it is often difficult to prove that an investment in the organizational culture will pay off, as effective tools for measuring the impact are hard to come by.

Multiple studies have measured the financial benefit a trust-based workplace culture, including an annual survey conducted by the consulting firm Frank Russell, which indicates that stock shares in the Best Companies to Work for in the United States have been between two to five times more profitable than those on the S&P 500 and Russell 3000 benchmarks. Another study, completed by Alex Edmans of the Wharton School (University of Pennsylvania), arrives at the same conclusion, even building in controls to ensure that the differences in profits are not related to size, financial performance, industry, or other characteristics shared by the best companies.

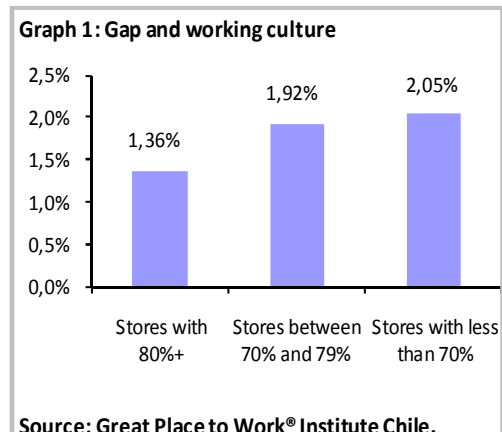
These studies show that a great culture can have a direct impact on the bottom line. But why is this the case? In an initial analysis, one might look at such factors as reduced staff turnover or decreased absenteeism. But while these variables are important, they do not tell the whole story. In reality, there are several reasons why establishing trust can improve profits, and these vary by industry. Please allow me to illustrate this with a real example, a retail business.

At the Great Place to Work® Institute Chile we have worked with a particular retail client for a long time, measuring its progress to improve its culture and evaluating the impact on financial indicators. The most recent study involved segmenting the stores of this large company into three groups: those with a score of more than 80% on the Great Place to Work® Trust Index® survey (which we will call *good stores*¹), those with results between 70% and 79% (which we will call *moderate stores*), and those with results below 70% (which we will call *deficient stores*).

¹This classification is not fixed and varies according to the variable of analysis and the company researched.

For each of these groups, we calculated the "gap," or difference in inventory, caused by theft (internal and external), as well as the products damaged during handling. Graph 1 shows that while the *deficient stores* experienced a gap of 2.05% in sales, the *good stores* had a gap of just 1.36%.

As this company has sales of approximately US\$1,2 billion per year, the gap across the company amounts to about US\$21 million annually. If we assume that the difference between the gaps is entirely accounted for by the organizational culture (an assumption that is unfortunately not verifiable), we can calculate that, by getting all the stores to have the same gap as the "good" stores, this company could generate savings of approximately US\$15 million per year. Even if we factor in a degree of uncertainty related to the cause-and-effect relationship between the workplace quality and the gap, we would still arrive at substantial savings for the organization.



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This same exercise can also be applied to the costs related to staff turnover: in this case, the outcome of making all the stores "good" stores would lead to an estimated savings of about US\$4 million. If we combine both effects, and assume that 50% of the gap is related to workplace culture, the total benefit for the organization would be approximately US\$58 million, if we calculate the net present value of the savings using a discount rate of 20%.

One might wonder about the cause of the dramatic difference between the "good" and "deficient" stores' gaps; given that theft is a substantial part of this issue, one explanation could lie in people's need for justice. In other words, theft may be a compensatory mechanism when employees do not feel a sense of trust in their workplace, and they steal merchandise in attempt to equate the conditions that they feel the company offers them (emotionally, psychologically, and economically) compared to what they feel they give in return.

A positive organizational culture can have a range of other benefits for the bottom line: for example, it can help attract better talent, improve customer service, reduce failures in the products delivered, generate more innovation, etc. In each industry, and even within each company, the effect of an improved culture will be realized in a different way, but there is no doubt it will have a favorable economic impact.

Best of all, it is usually not necessary to make a large investment in order to improve the working environment: simply changing the behavior of the company's leadership can make a significant difference. However, even if a company does decide to make a financial investment in an effort to improve the culture, the returns – both economic and ethical – will undoubtedly justify the costs.