CAHRS ResearchLink

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What's HR Got to do With it? A Look at its Effects on the Bottom Line in Service-Based Organizations

The Challenge

For a long time it was assumed that service-based organizations could compete on the basis of differentiation or on the basis of low prices, but not both. Great customer service was thought to require customized offerings that were necessarily time-consuming and costly to provide, whereas low prices could be achieved only by offering standardized services delivered in high-volume. More recently, however, spurred on by the Total Quality Management movement in manufacturing, an increasing number of service providers in hospitality, retail, healthcare, and other industries have rejected the conventional wisdom and adopted a so-called hybrid marketing strategy aimed at delivering personalized products and services at very competitive prices. In the telecommunications industry, for example, representatives in service and sales centers (hereafter call centers) are called upon to deliver great customer service by being highly responsive to each caller's particular concerns while also generating revenue by offering a range of add-on services to meet individual's particular needs or preferences. At the same time, though, these reps are expected to be highly efficient by minimizing the amount of time they spend on each call thus increasing the volume of calls handled per shift. Companies then put in place various HR practices intended to facilitate the simultaneous pursuit of these two seemingly contradictory outcomes. Research shows that this often results in relatively high levels of employee stress, burnout, absenteeism, and turnover. Thus far, though, no study has parsed the effects of existing HR practices on the attainment of the hybrid model's two key operational outcomes – service quality and labor efficiency – or, ultimately, on the bottom line.

The present study aims to fill this gap. As shown in Figure 1 on page 2, it examines the full range of linkages across four HR practices under the control of call center managers (discretionary work design, training, and two forms of compensation), the two operational outcomes (service quality and labor efficiency), and the firm's preferred measure of profitability (net revenues per call). More specifically, the study addresses two basic questions. First, in call centers pursuing a hybrid marketing strategy which operational outcomes makes the greatest contribution to units' financial outcomes? Are both equally necessary or is it better to excel at one while being simply okay on the other? Second, which locally-determined human resource practices – either singly or in combination – are most likely to result in the best blend of operational outcomes and, thus, the highest levels of unit profitability?

The Major Results

Here, in brief, are the study's major results:

- The call centers varied widely in their overall profitability. Across a six month period, average net revenues per call ranged from $50.40 to $117.25.

- With respect to service quality, center scores on a multi-item customer survey conducted by an independent outside vendor ranged from 3.85 to 4.50 on a 5-point scale. Labor efficiency, the average number of calls handled per representative per day, varied from a low of 44.00 to a high of 89.50.

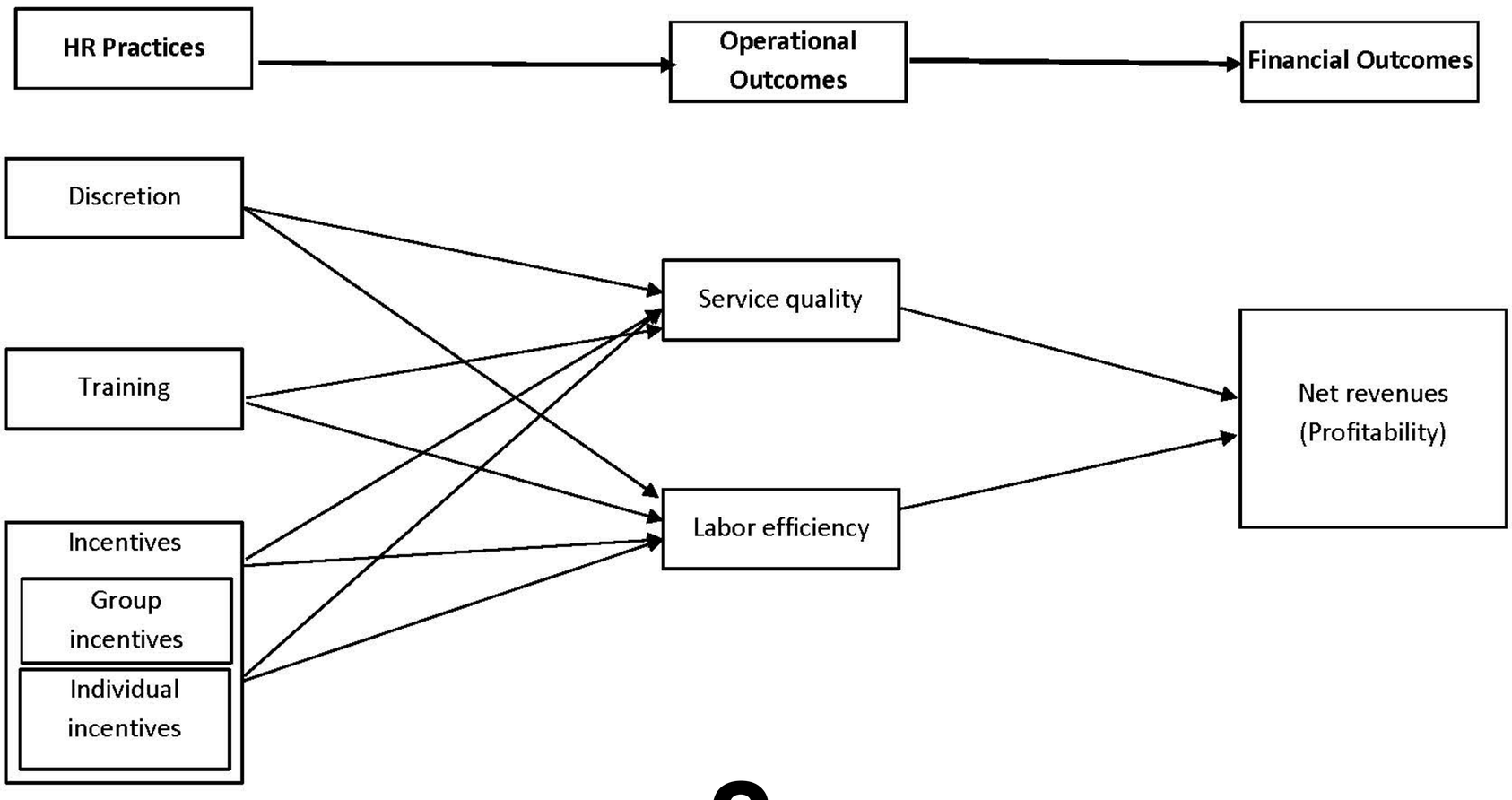
- Managers of the centers made divergent use of HR practices under their control. Discretionary work design usage ranged from 1.57 to 4.25 (on a 5-point scale). Training hours provided during the past six months varied from zero to 228. Incentives were captured by indices showing managers' usage of cash and non-cash awards at the (a) work group and (b) individual levels (both on 5-point scales). The group level index ranged from 1.50 to 3.50, while the individual level index varied from 1.57 to 4.33.

- Service quality made a direct and meaningful contribution to unit profitability but labor efficiency did not (see Figure 2 where solid lines indicate significant relationships and dotted lines indicate non-significant relationships). This is true for both measures of profitability examined.

- Units pursuing a high service quality/low efficiency strategy generated the highest net revenues per call; on average, $7.58 more than centers pursuing a high/high strategy and $19.40 more than those pursuing a low/low strategy.

- Again as shown in Figure 2 on page 4, three HR practices – discretionary work design, training, and group incentives – were positively and significantly related to service quality, while only one – discretionary work design – made even a marginally significant contribution to labor efficiency. Individual incentives had no significant impact on either service quality or labor efficiency.

Figure 1. Proposed Model



Implications For Practice

While a hybrid marketing strategy aimed at delivering superior customer service at low prices may make sense conceptually, research shows that it is devilishly difficult to operationalize. Because there is little evidence to guide managers on the ground, practices and, thus, results can vary widely as the present study shows. One basic question for unit managers is whether to give equal emphasis to the two key operational outcomes – service quality and efficiency – or to go all out for one while easing back on the other. Here, the evidence is clear. From the standpoint of profitability, centers that attained above average scores on both operational outcomes actually performed worse than those that excelled at customer service but lagged a bit on labor efficiency (across a six month period the gap in average net revenues per call was $7.58 – in a center with 100 representatives making the average number of calls per day [60] that's an additional $45,480 per day straight to the bottom line). These data show that great customer service pays off indirectly in the form of customer goodwill and retention, as well as directly in the form of revenues generated by capitalizing on cross-selling opportunities, and that the revenue thus generated exceeds the additional costs incurred by spending a little additional time with each customer.

The second basic question is how best to utilize the available talent to assure the highest possible net payoff per call. Again, the evidence is clear. First, from an organizational standpoint, it is essential that unit managers have some latitude in managing their human resources. Second, unit managers must understand how important it is to use this latitude effectively and how best to do it (i.e., they should read this Research Link). It is critical that subordinates have a fair amount of discretion on the job especially when it comes to making decisions that are particularly relevant to customers (in the present case these pertained to making small adjustments to prices, waiving late fees, switching customers to more suitable products, and extending deadlines). Discretionary work design opens up the opportunity to deliver great customer service and encourages employees to strive to do better. But this works only when employees have the ability and motivation needed to take advantage of the flexibility. This means that unit managers must invest in training their subordinates especially as significant changes are made in marketing strategies, products and features, and technologies. They must also attend to motivation. One way to do this is to provide on-the-spot cash and non-cash awards such as gift certificates and lunches or dinners to acknowledge the contributions of teams that excel in some way. Group incentives are more effective than individual incentives in this context because, in the end, providing great customer service is a team sport. While representatives handle calls individually, they nonetheless benefit from sharing tips about such matters as handling difficult customers, bundling new products and services, and adapting to new processes or technologies. Group incentives encourage this type of knowledge sharing and cooperation; individual incentives don't.

Specifics of the Study

The Setting, the Sample, and the Measures

The study was conducted in a United States-based telecommunications company. The sample consisted of 70 service and sales centers that handle such matters as billing inquiries, new orders and transfers, sales of enhanced features (e.g., call waiting, caller ID, multiple lines, and high speed internet access). The company had long ago adopted a hybrid marketing strategy in its call centers, switching them from cost centers to profit centers with the twin goals of enhancing revenues via improved customer service and direct sales while simultaneously keeping a lid on the duration of calls to maximize the number of calls handled.

Data for the analysis were collected as follows:

1. An employee survey of four HR practices: (a) Discretionary Work Design – a five-point scale indicating the level of discretion employees felt they had over adjusting prices, waiving late fees, switching customers to more suitable products, and extending deadlines; (b) Training – number of hours of on-the job training employees received during the past six months, and (c) Incentives – the level of awards (cash and non-cash) employees had received for their work group performance and for their individual performance during the past six months (both on five-point scales).
2. A vendor administered survey of service quality: a composite measure of customer satisfaction across six dimensions (a five-point scale) – understanding your needs, ability to handle your request, willingness to handle your request, handled call efficiently, was courteous, and an overall rating.
3. Company data on labor efficiency: calculated as the average number of work hours per day divided by the average handling time per call.
4. Company data on financial performance – (a) net revenues per call (the company's preferred measure of profitability), calculated as total revenue per call minus all operational costs per call, including wage costs and (b) net revenues per representative (a measure often used by researchers), calculated by dividing monthly profits of a center by the average number of representatives at the center during the month.

The Setting, the Sample, and the Measures

Based on the model shown in Figure 1, these data were used to test the following hypotheses using structural equation modeling. The results are depicted in Figure 2:

Hypothesis 1(a): Service quality is positively related to profitability
Hypothesis 1(b): Labor efficiency is positively related to profitability
Hypothesis 1(c): Service quality contributes more to profitability than does labor efficiency.

Hypothesis 1(a) was supported, while Hypothesis 1(b) was not. Thus, Hypothesis 1(c) was also supported. These results pertain to both measures of profitability tested.

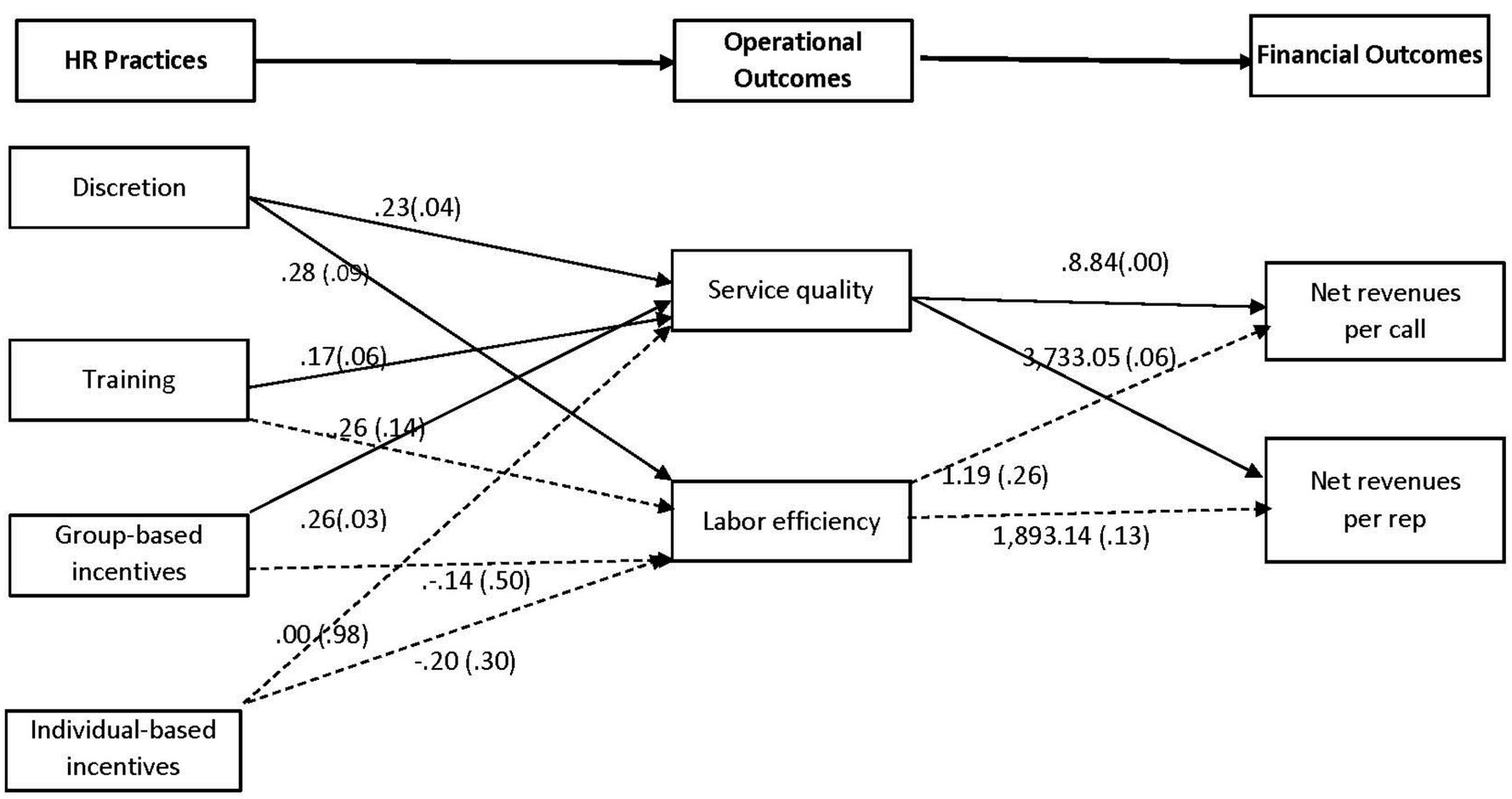
Hypothesis 2: Work designed to increase discretion, investment in training, and greater use of group incentives are positively associated with service quality while individual incentives are negatively associated with service quality.

Hypothesis 2 was generally supported, although there was no significant relationship, positive or negative, between individual incentives and service quality.

Hypothesis 3(a) and (b): Work designed to increase discretion, investment in training, and greater use of group incentives are (a) negatively (b) positively associated with labor efficiency. Neither Hypothesis 3(a) nor 3(b) was supported, although there was a marginally significant relationship between discretionary work design and labor efficiency.

Hypothesis 3(C): Greater use of individual incentives is positively associated with labor efficiency.This hypothesis was not supported.

Figure 2. Estimated Path Coefficients for the Revised Model (SEM-FIML)



a. Standardized coefficients are presented (p-value in parenthesis)

b. Regional dummies are included as control variables for paths from high involvement practices to mediators and from mediators to financial outcomes

c. N=70

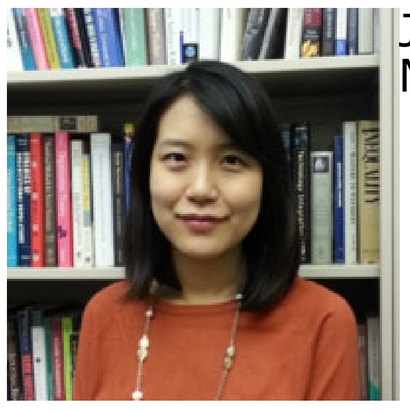
d. Dotted lines indicate insignificant relationships

Conclusion

This study's results play straight into today's dominant narrative with respect to technology and work. They suggest that the "smart play" is for firms to automate the more routine aspects of jobs to increase efficiency and lower costs, while relying on people to perform the high value-added tasks that directly contribute to superior customer service, greater customer satisfaction, and increased revenues. The results further reinforce the notion that local control over key HR activities is critical to the performance of these high value-added tasks. In the organization studied, many HR activities – wages, benefits, internal staffing procedures, and the like were formalized in a union contract and, thus, centralized. Nonetheless, unit managers retained control over three facets that research has long shown to enhance employee performance – opportunity, ability, and motivation. The best of these managers used this leverage wisely by granting representatives a high degree of autonomy over key decisions pertaining to their work, providing extensive training (up to 200+ hours in a six month period in some cases), and allocating team-based, cash and non-cash awards for noteworthy performance. In turn, their units delivered superior customer service and revenues at affordable costs.

All research has shortcomings, of course. In this case, the study was conducted in a single company so it remains to be determined if the results will generalize to other organizations pursuing hybrid marketing strategies. Further, the study was cross-sectional rather than a longitudinal experiment. While it turned up interesting and important findings, it is impossible to say for sure that the causal pattern implied in Figure1 actually holds. Notwithstanding, the study has one overriding strength that previous research lacks. To date, most researchers in this vein have been limited to studying employee affects, attitudes, and behaviors; this one elevates to the organizational level by including not only measures of the two key operational variables, but also unit profitability. As always, then, there is a need for additional research in other companies, cross-sectional if necessary, but preferably involving field experiments where HR activities can be varied and the effects on operational outcomes and profitability observed and measured over a period of time. Thus, we urge CAHRS companies that are pursuing or contemplating the pursuit of hybrid marketing strategies to partner with skilled researchers from Cornell to determine which approaches offer the best results certainly for employees but also for the bottom line of the organizations involved.

Researchers



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Lee, Jae Eun, Rosemary Batt, and Lisa Moynihan. 2018. "Strategic Dilemmas: How Managers use HR Practices to Meet Multiple Goals." *British Journal of Industrial Relations*. Published online first August 23, 2018. https://onlinelibrary.wiley.com/toc/14678543/0/0

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