

The New Zealand Labour Market Is Horribly Imperfect



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Recruitment costs are very high.

We have buyers (companies) and sellers (people seeking work) finding it very hard to find each other.

Employers say its hard to find good people.....

Skilled people say its hard to find a new job and it takes a long time

Getting improved business returns from your dealings in the labour market is critical

The difficulty of employers and skilled employees finding each other is demonstrated by large responses to advertised vacancies (typically 50-200 CV's per position) whilst at the same time, employers often commenting that it is difficult to find good people.

There are various factors which have contributed to this including:

- A mismatch between output from the education system and employer requirements. e.g. for the last two decades, way too few graduates in technology, engineering and IS/IT.
- NZ is a long, thin country making market-matching between a buyer and seller of a skill-set difficult. Roughly the population of Sydney is spread out across 268,000 sq km's.
- Speed of change makes it easy for skills to become less relevant e.g. technology and product lifecycles are shortening.
- Increasing staff turnover has meant existing market-matching mechanisms (e.g. 'who-you-happen-to-know', high reliance on recruitment firms, newspaper advertisements) are not coping as they did previously.
- Leaving one's employer after only two years has become acceptable.
- 'Talent wars' is certain 'scarce-skill' areas where there are more jobs than people.

RECRUITMENT INDUSTRY CHARACTERISTICS

New Zealand organisations are amongst the highest users of recruitment firms in the world

A far higher percentage of recruitment in NZ is done via recruitment firms than in Australia, USA and UK. In addition to the above, NZ has a high proportion of employment in small and mid-sized businesses so recruitment is contracted out. Similarly, NZ has only a small number of large corporations which provide a lot of internal vacancies. Thus, employees often look externally to find advancement and recruitment firms can provide the market forum.

Cost and fee drivers in the recruitment industry: *A high risk, high return business*

For successful firms, sales margins and overall profits can be very substantial. Conversely, unsuccessful firms come and go quickly. It has been the fastest-growing part of the professional

services sector for the past 20 years. Various factors drive the high risk, high return nature of the recruitment business and in turn, fee levels:

- It costs little to start a recruitment business and there are few entry barriers. Competition is significant; there are approximately 600 recruitment firms in New Zealand.
- Although a recruitment firm may receive a retainer, if offer/acceptance does not work and the exercise has to be repeated (or no candidate is appointed), then the firm is out-of-pocket. In other forms of consulting, there is very rarely the need to have to repeat a project and do so for no extra fee.
- Contingency fees e.g. 'no-fee-unless-there-is-a-placement' is high risk and keeps fees high. Conversely, a file search placement, where the firm searches files and collects a fee if their candidate is successful, is windfall profit.
- Clients can switch suppliers easily and at little financial, contractual or asset cost which makes long-term customer retention risky.
- As a consulting business, "the main financial assets walk out the door and go home at night". Voluntary staff turnover is a major business risk.
- Intense, urgent customer demand. When an employee resigns, a client usually wants immediate replacement. This means that unlike other consulting services, recruitment service becomes non-discretionary. As a result it is unusual for fees to be negotiated downwards.

Percentage fee approaches: *Mostly these result in large, built-in price & margin increases*

Percentage fee approaches allow for significant price and margin increases for similar services. e.g. the costs associated with recruiting for a \$60k salary position and a \$90k salary position are very similar, yet with percentage fees the latter service costs 50% more, most of which is profit direct to the recruiter.

Percentage fees insulate pricing against inflation and enable pricing to go up with salaries each year. Notably, salaries over \$45k have increased ahead of the rate of inflation in NZ every year for the last twelve years in succession.

For salaries over \$60k, fixed fees or hourly rate approaches will noticeably reduce the total fee for the client and risk to the recruiter.

Paying a fee (or a portion of the fee) only if you hire the candidate: *A conflict of interest*

Contingency fees are an incentive for the recruiter to close the sale. Any portion of the fee being contingent provides this. Yet, with the internet radically changing how organisations keep in touch with talent and collect CV's, the primary value-add of a recruitment firm is shifting. Increasingly, it's about adding value by assessing good candidates including culture fit, not persuading you to hire someone to collect a fee. In any supply contract, financial incentives should be structured to support the desired behaviour of the supplier.

This conflict is potentially most apparent at the time of verbal reference checks, when it is essential to understand the development needs or weaknesses of the person you are near to hiring. Yet, how many times do we read the transcript of verbal references and it says "Weaknesses: None." ?

Contingency fees were useful when the recruitment industry was young and proving its value. But in a labour market which now requires a range of different tactics and a wider range of modular recruitment services, it is time to scrap percentages and shift to fixed fees and/or hourly rates.

Executive search firms/'headhunters': *Why are fees up around 33%?*

Mainly because of demand from their clients. Senior executives who use search firms very often value search consultants who

have extensive previous senior management experience. To hire these people as consultants, search firms need to pay executive-level salaries. Furthermore, the search process is usually more time-consuming and complex than advertised recruitment. The bigger the job, the greater the impact on the organisation of getting it right or wrong.

Search firm fees vary considerably, from about 18% to 35%. There is a rough correlation between the global track record of the search firm and the fee level.

RECRUITING SUCCESSFULLY TOMORROW - COMPETITIVE ADVANTAGE BY TAKING ON SOME NEW TACTICS

Much has been talked about the changing nature of work-we've got Knowledge Workers, Talent Wars, Knowledge Waves, Employer Branding, The Networked Organisational Model, Change as a Constant, etc. But in practical terms, how does this effect recruitment?

It means taking on a wider range of tactics to get good people and developing a wider range of channels to improve access to the labour market. This can include:

1. Preferred Supplier Agreements: *Better quality and lower costs for both your company and the recruitment firm*

The Value Proposition

Providing or outsourcing all of the organisation's recruitment to one or two suppliers has taken off in the last four years. The quality of candidates improves. The recruitment firm takes on less risk & cost and prices drop significantly as a result. Assessment on which candidates best fit the culture becomes more reliable. Performance is much easier to assess and agreements include standards, measures and reviews. A win-win partnership can be created.

Small & Mid-Sized Businesses

Small and mid-sized companies can also benefit from the improved recruitment quality and reduced costs of a PSA. Any organisation that recruits externally 5-10 times per year or more may find this approach worthwhile.

How Much? Fee Levels Under a PSA

How much a company pays per placement in a PSA varies depends level of service, types of service, nature of exclusivity, risk and volume. Notwithstanding the problems with percentage-based fees, fees in PSA's typically range from 10% to 13%, (in dollar terms, savings of 15% to 33% on previous pricing). One large organisation which recruits very large volumes of semi-skilled employees has a PSA fee of 8.5% including full assessment.

Fees mentioned above exclude search/'headhunting' services. As a rough guide, PSA fee levels for search services are likely to be 18%-25%.

2. Taking advantage of the technology: *Much better contact with the skills you want, faster, for longer and at lower cost*

For skilled labour, the internet provides tremendous opportunities to improve the reliability of bringing buyers and sellers of labour together. Advertisements last for longer and can be seen by more people. Companies can market themselves directly to high value employees over a sustained timeframe via job fairs, searchable job banks and auto-notification of vacancies. Candidates are easily provided with value-add services such as CV builders & storage, advice on interviewing, news & trends. Recruitment cycle times and costs are reduced.

The internet also provides the opportunity to unbundle recruitment firm services and take a modular approach. e.g. you

advertise yourself and collect CV's but then pay the firm to undertake short-listing and appraisal.

A key issue is whether or not to take advantage of the potential scale and size of a recruitment firm's technology, by utilising that firm's candidate database storage capability and internet technology. Again, this can be a useful feature of a preferred supplier agreement.

3. Everyone is a recruiter: *Maximise your company's knowledge of labour supply to improve results*

All of your organisation's employees will know people who have skills that you will need. e.g. employees often have excellent knowledge of which companies and individuals are good performers within their field within the labour market. This information can be systematically captured and used to great advantage.

To make this channel to the market work effectively, it is essential to establish a culture of encouragement for employees to initially record the information. A generous 'Reward & Recognition' programme can be established. For each placement, the 'Reward & Recognition' programme will cost a fraction of otherwise paying recruitment fees.

4. Labour supply plans: *Working out where the replacement skills are before you need them to improve candidate quality and reduce costs*

This requires a commitment to develop a detailed understanding of the labour market niches pertinent to each area within an organisation. Line Managers should have detailed understanding of the supply markets that make for competitive advantage, including labour.

In almost all organisations, people are the biggest financial investment the company makes each year (30%-75% of annual expenditure for most organisations is on personnel costs). As such, more time and effort should go into understanding, planning and effecting the supply of people than any other supply-related activity.

Labour Supply Planning means identifying skills/qualifications required for all roles; where those skills exist, (likely current employers, job functions, tertiary education); and what is the best channel to reach those skills.

5. Create a 'Networking Association' for former staff members: *Increase your knowledge about good candidates*

Keeping in touch with former staff members on a regularised basis enables an organisation to retain contact with key skills. This makes it easier for the organisation to tap into their knowledge of their particular labour market niche and perhaps, re-hire good people either permanently or for a project.

In return, the association enables previous staff members to expand their own networks, keep abreast of commercial developments and keep in touch with colleagues.

6. Do-it-Yourself

The internet provides an excellent opportunity to recruit your own staff with greater reliability of candidate quality than traditionally, particularly for skilled labour positions where candidates have access to a PC. DIY means that slick, efficient administrative processes are needed to save line managers' time. Training for managers in interview & reference checking techniques may be useful.

ITS MISSION-CRITICAL TO CHOOSE A STRATEGY FIRST

The key is to choose the right mix of recruitment tactics for the parts of labour market you deal in. Hypothetical examples:

1. 'Company A, Mid-sized Hi-Tech Business'

This company has a highly-skilled workforce, which is reflected in a median salary of \$70,000. It decides to do its own recruitment for 80% of its vacancies. Efficient processes are developed and line managers are trained in recruitment techniques. It adopts a 'Everyone is a Recruiter' tactic including a Reward scheme for staff members and sets up an 'Networking Association' for departing employees. The other 20% of vacancies are 'scarce-skill' positions which are contracted to an executive search/headhunting firm.

2. 'Company B, Large Retail Service Business'

This organisation has a mainly semi-skilled workforce with a median salary of \$30,000. A large ratio of the workforce have broadly common job descriptions in retail & customer service. It decides to outsource its recruitment to one preferred recruitment supplier, who also develops an assessment centre for the company to ensure consistent high standards across the country of incoming retail & customer service staff. The company utilises job fairs and labour supply planning to improve reliability of intake.

THE BUSINESS CASE-FINANCIAL

A successful recruitment improvement programme will often have a Return on Investment of several hundred percent. This is excellent investing given that typical investments in capital such as IT, plant or machinery have ROI's of 10%-40%.

There are a range of measures that can be adopted to help assess the impact of recruitment programmes and justify expenditure on improving results, including:

- productivity lost from voluntary staff turnover
- recruitment cost & productivity loss per each hire
- time to recruit per hire

THE BUSINESS CASE-NON FINANCIAL

In any organisation, culture is no more than the behaviour of all the individuals, all added up. Thus, whilst changing culture is a many-faceted task, if there is one big lever to pull then it is recruitment. The higher the strike rate on hiring good people, the better the culture; by definition good individuals en-masse will make it so.

Some important qualitative, non-financial measures can include:

- Correlation with customer satisfaction.
- Improving company culture survey results, employee commitment & satisfaction, etc.
- Performance rating of new recruits, before versus after the programme.

SUMMARY

The changing nature of the labour market means organisations need to develop a more diverse range of tactics than has traditionally been necessary. The mix of tactics will depend very much on the nature of the business and labour markets it interfaces with. The returns on investment of better recruitment from a financial & non-financial perspective can be outstanding.

About The Author ...

Martin Price is Director of HR Equations Ltd, a human resources management consulting firm he established in 2001.

The firm's philosophy is that human resources management activity exists in commercial organisations to help create improved total returns to shareholders. This means prioritising and implementing those HR-related practices which are known to drive improved financial results better than other practices.

In government and non-profit organisations, the philosophy is the same but the stakeholder goals are different. Instead of financial returns to shareholders, HR activity should be prioritised by its impact on factors such as service delivery, service quality and cost-effectiveness.

As such, services are offered in:

- HR strategy, audit, measurement and business cases
- Recruitment improvement and labor supply chain effectiveness
- Remuneration strategy, design and Performance Management
- HR content of Mergers & Acquisitions, Outsourcing and Divestment

Prior to establishing HR Equations, from 1993 to 2001 Martin worked as Head of Organisational Development, Head of Remuneration and General Manager Human Resources for one of the largest public-listed corporations in Australasia. Before this he spent eight years in the executive recruitment industry with two 'big brand' recruitment firms, including responsibility for regions and company profit.

FURTHER INFORMATION

If you would like more information or have any feedback, please contact Martin Price, on tel (09) 638-3368 or email mp@hrequations.co.nz