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The Cost of Replacing an Employee and the Role of Financial Wellness

by iGrad Author | in Employers Organizations

The Society for Human Resource Management (SHRM) (https://lrshrm.shrm.org/blog/2017/10/essential-elements-employee-retention) reported that on average it costs a company 6 to 9 months of an employee's salary to replace him or her. For an employee making $60,000 per year, that comes out to $30,000 - $45,000 in recruiting and training costs.

Employees leave organizations for a multitude of reasons.

Some employees find better paying jobs while others go back to school. Sometimes it's their choice and other times they follow a spouse who's been transferred to another state.

Whatever the reason, it has been well documented that employee turnover is costly and disruptive.

According to Robert Half, an American human resource consulting firm, 38% of employees leave their jobs as a result of "inadequate salary and benefits."[1]

"The stronger hiring climate today means employees who don't feel well compensated may be more willing to look for a new, better-paying job," said Robert Half senior executive director Paul McDonald. "Managers should regularly benchmark salaries against those of other companies in their region and industry to ensure they are at or above market standards. While many factors contribute to turnover, competitive pay and benefits can be the difference when it comes to retaining skilled talent."

With the mounting pressures of everyday personal finances, it's no surprise why better paying jobs can seem more attractive. In fact, a study conducted by the American Psychological Association (APA) cites money as the biggest cause of stress.[2]

It's a no brainer. A higher paying job is the solution to getting rid of all that stress, right? Not so fast.

According to a survey conducted by Bankrate.com, roughly three-quarters of Americans are living paycheck-to-paycheck regardless of income.[3]

In another survey published by Suntrust, one-third of respondents cited insufficient financial discipline as the reason they don't meet with financial goals.[4]

If roughly 75% employees are living paycheck-to-paycheck regardless of income and 33% cite insufficient financial discipline as the reason for not meeting their goals, is it safe to assume that money is not the problem? And if money is not the problem, then how can employers keep employees from leaving for money purposes?

Many companies have turned to financial wellness (http://enrich.org/) as an employee benefit. Not only does a financial wellness program enhance a company's benefits package, it also educates employees on how to manage their money wisely.

Financial wellness is a great option for lowering employee financial stress (https://www.enrich.org/blog/how-financial-wellness-programs-reduce-employee-financial-stress).

Lowering financial stress is a key factor in achieving a happier and more engaged workforce.

Additionally, studies have shown that financial wellness can influence many positive behavior changes (https://www.enrich.org/financial-wellness-behavior-change-data-study).

By helping employees manage their finances and meet their goals, employers can help lower stress and improve their chances at retaining employees who leave for better pay.

However, since financial wellness is a fairly new concept, many employers balk at the idea of adding another expense to their company's overhead.

It's a fair concern but one that can be refuted through simple math.

The Cost of Attrition

High turnover rates impact company culture, productivity, engagement, and overhead. The attrition rate is the term used for the amount of money employers lose due to employees leaving.

Because no two employees make the same amount, the cost of attrition has to be calculated on an individual basis, but using averages can still give you a ballpark estimate of the true cost of employee turnover.

Yearly turnover rates can be calculated by taking the number of separations during any given year divided by the average number of employees during that year.

Example: 100 [(10 employee separations) / (50 average employees)] = 20% turnover rate

Research by SHRM suggests that replacement costs can be as high as 50%-60% with overall costs ranging anywhere from 90%-200%.

Example: If an employee makes $60,000 per year then it costs an average of $30,000 - $45,000 just to replace that employee and roughly $54,000 - $120,000 in overall losses to the company.

Financial Wellness Programs

The cost of financial wellness programs varies depending on scope and size.

Even if an employer spends $50,000 per year to implement a financial wellness program, they are still spending less than what it takes to replace a single employee.

In this case, a successful program would need to retain just two employees to be considered a success.

There's no question that even the most rudimentary financial wellness program can yield a significant return on investment (https://www.enrich.org/blog/how-to-calculate-financial-wellness-roi).

In a world where employee turnover is becoming more and more common, financial wellness programs are a no-brainer.

1 - http://www.prnewswire.com/news-releases/why-good-employees-quit-327434002.html

2 - http://www.apa.org/news/press/releases/2015/02/money-stress.aspx

3 - http://www.bankrate.com/

4 - https://www.suntrust.com/personal-banking

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Contact Info

Address: 2163 Newcastle Avenue, Suite 100, Cardiff-By-The-Sea, CA 92007

Sales: (888) 844-1525

Sales: BusDev@enrich.org (mailto:BusDev@enrich.org)

PEOPLE OPERATIONS

How Much Does Employee Turnover Cost?

January 2, 2020 | By Jack Altman

People are companies' most important assets. While we've known this for a long time, we often do little to back it up.

The technology and the information age has resulted in more companies that compete based on their people. This isn't only true for technology companies like Facebook and Google. As the pace of business increases, companies will live and die by their ability to innovate.

Despite the fact that most organizations know that their long term advantage resides in their people, most don't think critically about increasing employee retention.

In this article, I'll argue that the reason people don't think about employee retention enough is that they don't know how to measure its impact. I'll share tips for how you can associate dollar values with regrettable turnover. Once I've (hopefully) convinced you that retention matters, I'll share actionable ideas for improving it at your company.

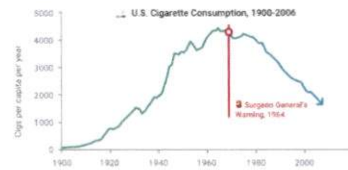
The Problem With Not Measuring Turnover

Employee turnover is expensive. People instinctively sense this. We've all felt the pain of losing a superstar or the cultural challenge associated with the departure of a beloved employee. But most people have no way of quantifying this cost.

The problem is that people tend to optimize what they can measure. Doctors believed that cigarettes were bad for human health as early as the 18th century, and scientific studies about the link between smoking and lung cancer started surfacing in the medical literature as early as the 1920s. Even though people generally knew cigarettes were bad, that wasn't enough. Smoking in America surged during the first half of the 20th century.

So what was the turning point? In 1964, the first Surgeon General's Report on

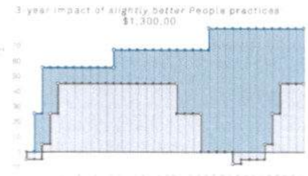
Smoking and Health linked smoking to lung cancer and heart disease. This landmark report laid the foundation for the next 50 years of public education about the effects of smoking, and the results have been dramatic.



Understanding the Impact of Churn

Employee turnover, like cigarettes in the 1920s, is generally understood to be bad. Unfortunately, there's little awareness of its quantifiable impact.

A visual way to gain a sense of this cost is to draw a graph of an employee's value to the company over time. Maia Josebachvili, VP of People at Greenhouse, produced a case study where she argued that retaining a salesperson for three years instead of two, along with better onboarding and management practices, yields a difference of $1.3 million in net value.



More conservatively, Josh Bersin of Deloitte believes the cost of losing an employee can range from tens of thousands of dollars to twice their annual salary. These costs include hiring, onboarding, training, ramp time, lower engagement, more errors, and general culture impacts.

Bersin also argues that employees are appreciating assets that produce more value to organizations over time, which explains why losing them is so costly.

Other sources peg the cost of regrettable employee turnover even higher. A study from the Center for American Progress determined that the average cost to a company of losing a highly-skilled employee is 213% of their annual compensation.

How to Calculate Your Turnover Costs

No matter how you slice it, turnover is costly. But how high is it for your company? To help you quantify this, we've put together a simple formula. Your company's **turnover cost is equal to the number of regrettable departures, multiplied by the average cost of those departures.**

The number of regrettable departures will simply equal your number of employees times your annual turnover percentage.

While we can't capture every single expense or even some of the intangible costs like impact on employee morale, we can get a good sense by analyzing four major buckets:

- Cost of hiring
- Cost of onboarding and training
- Cost of learning and development
- Cost of time with the unfilled role

With that, we can now describe your annual cost of turnover to be:

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(Hiring + Onboarding + Development + Unfilled Time)
x (Number Employees x Annual Turnover Percentage)
= Annual Cost of Turnover
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For example, consider a 150-person company with an 11% annual turnover rate. If you spend $25k per person on hiring, $10k per person on development, and lose $50k of productivity when refilling a role, then your annual cost of turnover would be about $1.57 million.

Reducing this by just 20% would immediately yield over $300k in value. That says nothing of the emotional headache and cultural drain felt from losing great people. You can use this spreadsheet to plug in your own numbers to get a sense of what the costs look like for you.

How to Address Turnover

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First, acknowledge that while there are problems that you can solve with money, employee satisfaction isn't one of them. Multiple studies show that overcompensating employees can't solve workplace culture issues. Your well-paid but unhappy employees will simply leave and make their money elsewhere.

View market-rate compensation as table stakes and spend your energy focused on the next level of Maslow's hierarchy of employee happiness: opportunities for growth, the ability to have an impact towards a purpose, and a caring environment that makes them feel valued.

1. Invest in growth.

Growth is fundamental to human happiness. The hedonic treadmill was built into all of us, and humans constantly seek growth and change. Giving your employees authentic opportunities for growth is something you have to build into the fabric of your company. Here are a few questions to ask yourself to check whether you're on the right track or not:

- Have you had conversations with employees about their long-term personal goals?
- When a capable person on your team wants a role bigger than their past experience, do you give them a shot?
- When people need to acquire new skills to advance their careers, what

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does your company do to help them?

If you don't build a culture that deliberately provides good answers to these questions, it'll be a matter of time before employees start looking for a workplace that does.

2. Lean into your mission.

Impact applies at two levels: the impact your company is having on the world, and the impact an individual is having on your company.

People want to know that what they're working on matters. Articulating a clear and purposeful mission is important not just because it helps people prioritize, but because it helps them to push through hard times and know they're part of something that matters.

To give a tangible sense of impact, they need to know that what they're working on is contributing to a mission that matters. If someone builds and launches a new product they will certainly feel some satisfaction. But if they can say, "I built a new product that helps our company accomplish its broader mission," that will mean much more to them.

3. Build a culture that cares.

Feeling cared for and recognized addresses another basic human requirement: the need for human relationships and for others to acknowledge that we matter to them.

You need to build a culture where people respect and appreciate each other. A culture of care and appreciation doesn't mean throwing around constant, meaningless praise. Instead, it's authentic care for others' best interests, which can't be faked and has to be built over time.

An environment where people feel like their coworkers have their best interests in mind comes with all kinds of benefits. Critical feedback will be more easily accepted. Frank conversations about what's required for employees to make it to the next level will happen naturally. Managers will want to see their teams succeed and work hard to empower them.

And, of course, employees will feel happier on a day-to-day basis knowing they're surrounded by people who don't just want something out of them but want something for them.

Final Thoughts

In a world where people are organizations' most essential assets, leaders need to be more strategic about how they think about employee retention to remain competitive. Employees are just humans who happen to be at work. You've likely learned a few ways to make other humans happy in your personal life, so take that knowledge and apply it to your workplace.

Once the basic needs of sufficient income and job security have been met, move up Maslow's hierarchy of needs and create a culture that enables growth, impact, and care. It'll save you a ton of money, help you stay competitive in your industry, and make the place you spend most of your waking hours so much more enjoyable.

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