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Building Assets to Ensure That the Lowest-Level Employees Are Not Left Behind

Create Value by Investing in Your Workforce

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Profit at the Bottom of the Ladder: Creating Value by Investing in Your Workforce

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4

Building Assets to Ensure That the Lowest-Level Employees Are Not Left Behind

THE PRESS HAS PAID attention to the rapidly rising inequalities in income between the rich and the poor. Although it has received less attention, the gap in wealth—which encompasses all assets, including home ownership, stocks, bonds, and pension plans—is actually far greater and is increasing more rapidly than the gap in income. The wealthiest 2 percent of adults own more than 50 percent of all global wealth, with the richest 1 percent owning 40 percent of global assets; in staggering contrast, the bottom 50 percent own barely 1 percent. North American households account for 34 percent of global assets, while 30 percent is enjoyed by Europe, and 24 percent by the rich Asia-Pacific countries. African households are the poorest, owning only 1 percent of assets. Latin American and Caribbean households are not far ahead of them, with a share of only 4 percent. Although China and India comprise 75 percent of the global population, they own only 3 percent and 1 percent of assets, respectively.[1]

While large inequalities in income exist all over the world, they are particularly grievous in the United States. In 2001, the richest 1 percent of the U.S. population accounted for 20 percent of total income, while the poorest 40 percent received only 10 percent. Inequalities in wealth were even more pronounced—the top 1 percent of the population held 33.4 percent of wealth, while the bottom 40 percent held only 0.3 percent. Over the course of the 1990s, the top 1 percent saw their average wealth increase by 63 percent, while the middle quintile gained 24 percent. In contrast, the average wealth of the poorest 40 percent of the population actually declined by 44 percent.[2] The enormous gap in assets has contributed to the gap in home ownership in the United States and the country's vulnerability to the subprime mortgage crisis of 2008.

In a study on wealth distribution in twenty countries, the share of assets owned by the richest 20 percent of the population ranged from 39.3 percent in Japan to 71.3 percent in Switzerland.[3] The share of the assets owned by the richest 1 percent ranged from 10.4 percent in Ireland to 34.8 percent in Switzerland. Meanwhile, the poorest 30 percent held 5.8 percent of assets in China but only 0.3 percent of assets in Germany. The share of assets held by the bottom 50 percent ranged from 14.4 percent in China to 2.8 percent in the United States.

The enormous gap in assets has serious implications. Currently, in the global economy, a lack of savings and financial assets leaves hundreds of millions of people without resources to fall back on when they face personal crises such as serious illness or job loss. The risks are equally profound when low-asset employees and their families endure economic downturns.

Should companies help address asset deficits? There is compelling evidence that companies stand to gain when they share their profits with employees. A British study of ninety-three randomly selected manufacturing companies showed that profit-sharing firms were more productive than their non-profit-sharing counterparts; profit sharing increased productivity by 6 percent over a three-year period.[4] Allowing workers to participate in their companies financially acted as an incentive for them to work harder and more efficiently, thus increasing productivity.[5] In Japan, a study of very large firms (more than ten thousand employees) found that the adoption of profit-sharing programs increased productivity by 9 percent.[6] Similarly, a study using data from a survey of five hundred U.S. public companies to examine the relationship between productivity and profit sharing found that the adoption of a profit-sharing plan was associated with a 4 to 5 percent increase in productivity.[7] This effect was also found for employees of Canadian financial institutions,[8] workers in U.S. chemical industries,[9] and employees in U.S. firms in general.[10] Companies stood to gain through improved employee recruitment and retention as well as higher productivity. Empirical studies in the United States have evidenced these advantages. U.S. companies that participated in profit-sharing schemes from 1988 to 1994 were found to have lower turnover and greater productivity.[11] Finally, a review of different studies on the relationship between profit sharing and productivity concluded that although a range of different techniques was used in the studies, nearly all showed that profit sharing led to increased productivity.[12]

Having interviewed representative samples of workers in cities and towns in the Americas, Africa, and Asia as part of our study on global working families, we were aware of the rarity of asset-building opportunities for men and women with limited levels of formal education. Beyond pensions, none of the workers we interviewed in each setting spoke about any profit-sharing or asset-building opportunities. Many of these workers barely earned sufficient income to survive on and received no protections in the form of paid sick leave or parental leave, creating periods during which they were likely to be without income. National data from several countries upholds our global research findings on employed men and women.

While many companies have established asset-building initiatives for their high-skilled and high-income workers, very few companies have done so for their lower-level employees. The disparities are marked even between low- and moderate-income employees. In Canada, for example, 17.7 percent of workers earning C$20 an hour or more participated in stock-purchase plans, in comparison to only 3.2 percent of workers earning C$12 an hour or less.[13] Is this omission of asset-building policies for the least-advantaged workers inevitable? It is often argued that to attract highly skilled workers, companies have to offer extras such as stock options in addition to higher salaries. But is there less economic incentive to offer asset-building programs to employees at the bottom of the corporate ladder?

We examined this issue in our recent five-year study of businesses in nine countries. In each of the companies we visited, we examined the extent of their asset-building opportunities as well as their wages and other forms of compensation. This chapter looks in detail at two of these companies; they were selected because of the ways in which they were able to translate profit sharing into increased productivity and profitability. Jenkins Brick implemented a common form of asset building—retirement savings plans—uncommonly well, and also set up a more unusual form of asset building for its least-advantaged workers—profit sharing. While both forms of asset building were also available at Dancing Deer Baking Company, the emphasis was shifted to profit sharing. The extent to which asset building had an impact on performance was examined from the perspective of both line workers and senior management.

Jenkins Brick: Traditional and Uncommon Approaches to Asset Building

Mike Jenkins V's level of personal investment in his family's company was evident in all aspects of his work.[14] Son of the current CEO and next in line to take over the business upon his father's retirement, Jenkins V showed us around the Jenkins Brick factory in Montgomery, Alabama. Following his father's example, he was spending time working on the factory floor in order to gain a better understanding of the company's daily operations, of the working lives of its employees, and of what it would take to achieve success. He had grown up around the factory and knew it as well as his own backyard. He strode through the plant with ease, past 1000-degree kilns and flatbeds that each carried sixteen thousand bricks.

Establishing Asset-Building Programs

Three Mike Jenkins preceded the current CEO. In the late 1800s in Wetumpka, Alabama, Mike Jenkins I developed a passion for apiaries. Endeavoring to build some newly designed beehives, he decided to make the bricks himself using the clay that was readily available on his property. Chance intervened when a fire burned his town to the ground, and he became the closest thing to a brick manufacturer in the area. By the time he had made enough bricks to rebuild the town, he had changed the focus of his production from honey to brick manufacturing.

His great-grandson, Mike Jenkins IV, unpretentiously described his own journey to become CEO of the company in 1974 and to take over ownership in 1985: "I think 1974 is when I really took operating control of the company . . . I was thirty-two and I didn't have a clue . . . I always wanted to do what my grandfather did, and when I was in junior high I worked out here. And in high school and college . . . I had a job [here in the summers]. When I . . . got out of the army I worked here a year as a salesman. Then I went to graduate school and got a masters in ceramic engineering."[15]

Jenkins IV had two goals when he took over the company: the first was to make the company economically successful again, and the second was to make working at the company advantageous for both management and line employees.

> In '85, we consolidated the ownership [and] bought the other shareholders out. And really from that point forward we were able to begin [working] on two issues: one of course was that we wanted to create the type of economic environment that would allow us to attract top-flight folks for our work, and to be able to [grow], . . . we had to do a lot better than what we were doing. And the other was a matter of equity. It didn't feel right . . . it felt lousy to see the old fellas who'd been here forever leave and have [nothing but] social security and literally not have health care.[16]

He was embarrassed to run into elderly people in the community who had worked their whole lives at the factory and yet were nearly destitute because they had so few resources for their retirement. Jenkins IV also saw that equity went hand in hand with economic growth, and that by providing employees with better benefits, the company would attract and retain better, more productive employees:

> I think we've matured to the point where we realize that if you work hard at recruiting the right people and you compensate them very well, it's one of the best investments you can make. So you can be entirely mercantile about it, or you can be philosophical. Philosophical meaning [that] it's the right thing to do, mercantile meaning [that if] you invest in "quality" people, you get "quality" output. And I believe it.[17]

Mike Jenkins IV established two distinct asset-building programs: the first was retirement savings in the form of a pension plan, and the second was profit sharing. Both of these benefits were available to all employees. Jenkins Brick provided these benefits in the context of an industry that was very susceptible to downturns in the economic cycle; when the economy was strong, families and companies did more building and brick was in high demand, but during recessions, building markedly declined, as did the demand for brick.

A Clear Vision: The Link Between Investment and Growth

Jenkins Brick is a medium-sized company in a competitive industry. It produces approximately 190 million bricks a year, and at the time of our first visit in March 2005, it employed 523 people. Its labor force was ethnically diverse: one in seven workers were Latino, the majority of whom were immigrants from Mexico, and one in five were African American.

Jenkins IV wanted to do well economically *and* do well by his employees, and he understood the link between these two goals. The quality of the company's products was essential to its ability to succeed in an increasingly competitive market. If the bricks were better in shape and structure, if their delivery was speedier and more reliable, then he would be able to sell more. Jenkins recognized that the company's ability to attract and retain the best workers was deeply influenced by the return it offered its employees. Better employees could produce better bricks and run the production more efficiently.

Jenkins IV wasn't the only one to recognize the link between the economic success of the company and that of its employees. Wyatt Shorter from the board of directors was also concerned with their ability to retain the best employees:

> [Management has] a solid appreciation of what it costs to train someone. I don't think we've ever had a directors meeting where we haven't discussed turnover.[18]

It was in the company's best interest to help employees build assets, since employees were more likely to stay out the year if they knew it would guarantee them a bonus. Similarly, employees would be motivated to work harder if they saw a return on their efforts by earning bonuses that increased in relation to their productivity. Finally, turnover would decline even more if employees knew that the longer they stayed with the company, the more savings they would accumulate for their retirement.

The 401(k) Pension and Profit-Sharing Plans

All Jenkins Brick employees have the option of participating in the pension plan, and their investments are matched by the company; the company contributes 50 cents to the plan for every dollar contributed by the worker, up to 6 percent of their wages. This money is invested in a tax-deferred 401(k) plan. The company is committed to making this plan accessible to everyone—not just to executives, but to forklift operators and plant workers as well.

Although the firm's costs increased with each additional associate who took out a retirement plan, the company wanted participation to be as widespread as possible. It held quarterly pension-education sessions for employees, explaining how the plan worked and how much money they could save. Tommy Andreades, executive vice president and chief financial officer, explained how the company tried to encourage employees to participate in the pension plan in a way that ensured that they accumulated assets for retirement:

> We just recently changed some things to try to motivate associates to start participating more [effectively]. We ha[d] a loan feature in our plan [so] that you could borrow any of the money that was in the plan, whether it came from profit sharing or your contributions to the match. We changed that now so the only money you can borrow from the plan, going forward on new loans, is money that you put in yourself. We're not allowing [employees] to borrow money that the company put in for them. We also just recently lowered the waiting period to get in. It used to be that some people, depending on when they were hired, had to wait up to eighteen months to get into the plan. Now they can get in every quarter.[19]

The same plan covered the company's CFO, a factory worker who had been with the company for less than two years, and a forklift driver with an eleventh-grade education who had been working there for seventeen years. Victor Fuentes, the forklift driver, earned enough money to keep investing in his 401(k) while his wife stayed home to raise their four children. Midlevel employees invested as well, including Melissa Coleman, who had been working in sales at the Birmingham yard for two years.

By March of 2005, 60 percent of Jenkins Brick employees had invested in the 401(k) program. In 2006, the company made another change to its regulations for plan participation, implementing an automatic enrollment program. Going forward, instead of having to actively enroll in the program once they became eligible, employees would automatically be enrolled. To be excluded, they would have to actively withdraw their participation. As of August 2007, the 401(k) participation rate was 95 percent.

The pension plan was not the company's only asset-building initiative. Jenkins Brick also established a defined contribution profit-sharing program for all of its employees. The company decided how much to put into the profit-sharing accounts on a yearly basis. Employees were fully vested in the program once they had been with the company for six years, at which time they could either take their money with them if they left or keep saving until their retirement. The six-year waiting period to vest encouraged longer employee retention, which in turn benefited the company economically.

Profit-sharing outcomes vary yearly since they are dependent on the company's performance. Prior to 2007, profit sharing had averaged approximately 5 percent of wages and salaries for the past five years, for a total of $1,095,000 in 2006. The company reported that its profit sharing was generally two to three times higher than the national average. Even more noteworthy was the fact that the profit-sharing program affected the lives of every employee; it was neither a stock-option plan limited to professionals nor a reward system solely for top management.

Jenkins Brick managed to contribute to asset building through these programs while keeping its benefit costs at 23 percent of total compensation. It was not outspending other companies, staying very close to the U.S. average of 25 percent. Its programs concentrated on long-term investments, and the firm leveled the playing field by providing the same benefits to line workers and executives. Moreover, these plans were weighted toward asset building; of the $4.5 million the company spent on benefits each year, $1.2 million was committed to employee retirement funds.

Linking Asset-Building Programs to Improved Performance

In establishing the pension and profit-sharing programs, Jenkins IV was concerned with equity and with making employment at Jenkins Brick financially advantageous for every worker. He was equally concerned with the company's financial success, for the sake of his family and his employees. Without improving the company's finances, it was clear that Jenkins IV could not ensure stable jobs for his employees, let alone provide them with good working conditions. The firm was not on solid financial footing when he took over in 1985; its productivity and earnings were paling. Brick manufacturing is difficult and labor-intensive work. The company had been having difficulty hiring workers, and the employees were not very productive, requiring two people to complete the work of one.

Jenkins IV turned the company around by creating the financial incentives that enabled him to hire better employees, motivate them to perform well, and retain them. Higher wages attracted better employees, and wages linked to productivity boosted performance, as discussed in chapter 1. Profit sharing allowed employees to reap the benefits of everyone's increased productivity. Both programs for asset accumulation encouraged retention since workers had to stay with Jenkins Brick for six years in order to fully vest in the profit-sharing program, and their pension savings increased the longer they remained with the company.

As a result, Jenkins Brick saw a marked decline in employee turnover. CEO Jenkins took this matter seriously: "We found that turnover can be a proxy for how well we're doing as leaders."[20] He noted that their investment in employees had helped them to cut their turnover rates in half—from a high of 41 percent down to close to 20 percent. The remaining turnover was largely attributable to immigrant workers who returned to their countries of origin, bringing with them the savings they had accumulated at the company.

The turnover rate in 2005 was 25 percent overall (19 percent from resignation and 6 percent from termination). This was not only lower than other brick manufacturers, but it was also lower than other factories in the region—furniture laminating factories faced a 38 to 39 percent turnover rate and chicken-processing plants faced a turnover rate of 75 to 80 percent. Turnover at Jenkins Brick further decreased over the following two years, and the company saw this as a significant achievement. Its turnover in manufacturing through May of 2007 was 17 percent, and the company estimated that the rate for the entire business was about the same.

The company reaped substantial financial gains from the low turnover, since it lowered accident rates as well as recruitment and training costs. Jenkins summarized: "Turnover is directly related to safety . . . People with less than one year [of experience here] in general have a higher incidence of accidents than people who [have been here for more than one year]. And of course it's very expensive to recruit and to train."[21] Providing benefits that encouraged workers to stay with the company was therefore as much a matter of economics as it was of principle.

Attracting the best employees had been one of the managers' goals when they implemented their new policies. As they had hoped, their new policies had facilitated employee recruitment. Jenkins Brick's financial rewards and asset-building programs led employees to recommend the company to their family members and friends. Because its workforce was partly made up of immigrant workers, there was often movement as workers returned to their native countries. However, because these jobs were highly valued, immigrant laborers often recruited people to fill their positions before they left. Anita Barrera, the controller, explained: "The reason they leave is to go back to Mexico. It's not to leave and go to another job in Montgomery. They leave to go home, and usually they've got people lined up [to replace them]: family members, friends, or whatever, who say 'So-and-so's leaving,' and we're like, 'What? We haven't heard that yet.' "[22]

As is the case at most companies, at Jenkins Brick, many departments and employees influenced the quality of the company's products and overall performance. The laborers who worked at the kilns and on the factory floor determined the quality and quantity of bricks produced, and the sales team influenced consumers' experiences in the store. At Jenkins Brick, everyone received economic benefits from the pension and profit-sharing plans, and everyone was therefore equally invested in the company's success and in the quality of its products. Improvements in efficiency and productivity resulted from employees' increased motivation to maximize the firm's profits by increasing their own productivity, as well as that of their peers.[23] Jenkins Brick's board believed that investing in their employees was also central to maintaining the quality of their products. Wyatt Shorter shared his own philosophy as well as that of the board: "This is something I've noticed over the years. A company that makes a high-quality [product] generally treats its employees well because they know the employees have such a huge influence over what the product is."[24]

Product quality was particularly important to Jenkins Brick because the company's competitive strategy entailed filling a niche in the market by providing some of the highest-quality bricks and service available, and charging a higher price for them. Its quality bricks were easily identified by their color, texture, and durability. The firm sought to fully and promptly meet its clients' needs; its high-quality service affected the prices it could charge for its products.

Jenkins Brick's Competition and Strategic Vision

Jenkins Brick had little competition from international shipments, but substantial competition from international firms. While high shipping costs had prevented the brick industry from facing significant competition from production in distant countries such as China and India, international firms had invested heavily in the industry in the United States. Jenkins IV described the dominance of international firms in the market:

> Now the brick industry itself is, I think, about 80 to 85 percent . . . owned by offshore people. The largest is Boral, who is the largest brick manufacturer. And I think they produce something like a billion or 600 million bricks a year. Compare that to us: this year we'll produce something like 190 million. There's a huge gap between the top four [manufacturers in the United States]; we're probably somewhere around tenth in size as a manufacturer in the country, and probably second or third maybe in distribution. So the Australians with Boral are number one; number two would be the Austrians [with] Wienerberger; and three is Acme Brick, Warren Buffett's outfit. Four would be Hanson, which is English. From there you drop down to a handful of folks like us, who . . . are really American-owned.[25]

In addition to competing based on quality, Jenkins sought to diversify in ways that might protect his firm from changes in customer preferences and some of the worst impacts of the building cycle. In an industry that is very susceptible to economic downturns, Jenkins Brick has differed from most companies in its approach to diversification and self-protection against economic fluctuations. The company manufactures and sells its own bricks, but what is unusual is that it distributes bricks from its competitors as well. Moreover, Jenkins Brick sales agents are not given any incentives that would lead them to sell more of their own company's bricks. As a result, distribution only performed poorly when no bricks from any manufacturer were selling. At the same time, the manufacturing arm does not rely solely on its own sales team to sell its products; Jenkins Brick products are also distributed by other vendors across the country. As a result, if construction was occurring anywhere in the country, the firm had an opportunity to sell bricks.

The distribution arm of the business has grown and the company has maintained good relationships with its competitors, who trust Jenkins Brick to sell their products fairly. In the end, the relationships it has fostered have given the firm access to far larger and more diverse markets, and this has ensured a consistent demand for its products. When a particular market experienced a downturn at a given time, there was likely to be activity in one of the other markets it had tapped into. Moreover, the wide range of products carried in the showrooms continued to attract new customers.

Jenkins Brick's belief that investing in its employees brings financial returns is representative of its overall long-term vision, which has been reflected in other company initiatives as well, such as its investment in environmentally clean energy. Jenkins Brick was one of the first companies to recognize the potential of using landfill gas to meet its energy needs. Landfill gas accounts for about 60 percent of the fuel used by the new $56 million plant near Birmingham. The company sees its investment in environmentally sound technology as having both national and economic value. Experts have contended that similar projects generate savings of between 20 and 50 percent of the cost of natural gas. According to Mike Jenkins V, "It benefits us and it benefits the world."[26]

There is little doubt that as a privately owned company, Jenkins Brick had greater flexibility to pursue paths that managers thought would be financially beneficial for their investors and senior executives as well as their employees. Although they had to convince senior management and the board of the value of their plans, they did not have to convince stock analysts. Tommy Andreades recalled:

> I came from public accounting and was in a public company for ten years. And what's very much enjoyable about being private is that we can sit around and think about what's best for the company as opposed to what our shareholders are going to think about our decision and the short-term benefits of it. Personally, we take some pops. We're building a new plant. Everyone who's on bottom-line incentive—there's four of us—we're going backwards for two or three years. And that's fine. We know that it's the right thing for the company and what the rewards will be down the road if we do a good job of it. So we don't have to worry about what our shareholders think about it. And we make good decisions more times than not.[27]

Of course, Jenkins Brick was not immune to the general economic climate. The downturn in the housing market brought about a new set of challenges and resulted in cutbacks in production. However, as the following chapters will show, companies with lower turnover rates and greater employee loyalty are better at weathering economic downturns.

Dancing Deer: Profit Sharing as a Way for Small Firms to Increase Compensation and Productivity

From the outside, the company's main building looked much like the other two-story warehouses in its relatively poor Boston neighborhood.

Inside, however, it was completely different. The building's ground floor housed the clean and well-lit bakery, and the second floor was where all the sales and management staff workstations were located, from entry-level administrative staff to the CEO. There were no walls or partitions between the desks.

The company's CEO, Trish Karter, had experience working at other firms and she knew that she wanted something different for her company. She was convinced that she could make a larger profit by treating her employees better.

The Challenge of Operating Within the Constraints of a Small Business

Though the company was born out of chance encounters, its long-term success stems from business acumen and commitment. CEO Trish Karter left college one semester short of completing her BA in order to help her father with his recycling business. She later received an MBA from Yale and gained business experience working in Coca-Cola's marketing department, in satellite television, in commercial real estate development, and in consulting. She explained the path to Dancing Deer Baking Company's opening:

> Actually, I [had been] a businessperson in the entrepreneurial world, and then [I] quit and I was painting pictures . . . We had a house-painter whose wife, [Suzanne], was a baker and she came to us for business advice. She was carrying her pots and pans to a rented kitchen facility at night. So the genesis of it was really a hobby investment; we put $20,000 into setting her up in an old pizza parlor on the corner of Grove and Washington in West Roxbury. Originally the concept was to put all-natural baked goods in coffeehouses because the coffee craze was coming east from California; you could buy these incredible brews of coffee but there wasn't anything good to eat with them. Everyone who [tasted one of Suzanne's baked goods] said, "Wow, it's wonderful! I'll buy that!" And in about a year and a half she was overwhelmed with business. She could barely hold herself up. She was doing great things and everybody loved it, but she was exhausted. I volunteered to go in for a few months and hire some people and put some systems in place and clear off the foot-and-a-half tall stack of unprocessed CODs on her desk . . . That was ten

> years ago. And we had fun together. I never left . . . One thing led to another, and we made a great partnership . . . We knew we wanted to have a brand from it. The business was building in a strategic direction . . . and we brought in an old friend of mine with talent to help us create an identity for the company. You know, just spadeful by spadeful, we built it up.[28]

But the development of Dancing Deer had by no means been a fairy tale free of personal and professional challenges. As Trish Karter explained, "In . . . 2000, we nearly blew it up because my ex-husband and I got a divorce. That year . . . was kind of a near-death experience for many of us. But at the end of it all, I ended up staying and buying [Suzanne and my ex-husband] out."

Dancing Deer's founders shared a vision of how to make the company profitable for the management by making it profitable for the employees. They were committed to creating a quality workplace for all of their employees, based on the principle that "if bakers like what they do, it shows in the food." As Karter described:

> We all wanted to have the company be better than what . . . we saw around us, and that meant better in every way, including personnel policies. And we believed in everybody having a piece of the value that's created. Everyone that participates in creating value should have some upside. It shouldn't be just about collecting a paycheck. We also wanted everyone to be knowledgeable about what we were doing because we believed that the more people understood the business, the better thinking we'd get on how to improve and grow the business.[29]

As a small business, Dancing Deer had always faced challenges in providing well for its employees. Starting wages were low ($7.25 per hour for packers and $7.50–$8.00 per hour for bakers), but they were higher than the minimum wage and equal to or higher than food production jobs elsewhere. Nonetheless, these wages were low for an individual to live on in an expensive city like Boston, and they were lower still for a family. From the company's standpoint, they were also low when it came to employee retention. It all boiled down to economics: because the baked goods they produced were already being sold at the top end of the market, the company executives worried that they would go out of business if they raised prices further to allow for higher wages. They felt their best long-term prospects for survival lay in increasing their productivity, their sales, and their share of the market. Karter explained how they dealt with these constraints:

> I would love to be able to tell you that everyone who walks through the door gets $12 an hour, but we can't do that. In the world we live in, with a huge component of our product being the manual labor that goes into it, and being challenged and very pressured competitively, we're at the top end of the market in terms of pricing. What we have to do in order to make it all work is to manage our numbers so [that] as we raise wages, it's in lockstep with raising efficiencies and getting smarter about running the business.[30]

They were looking forward to the time when their fixed costs would go down and their production would go up, leaving more room for wage increases without increasing the prices of their products. But what could they do in the meantime? Small businesses often find it harder to offer benefits such as health insurance coverage in countries like the United States, since large companies are able to negotiate better deals with insurance providers. Yet this does not mean that small companies are incapable of providing benefits. While recognizing its limitations as a small business, Dancing Deer sought to provide all of its employees with good working conditions and asset-building opportunities.

In start-up companies, executives often take the calculated risk of receiving stock options in exchange for lower salaries, based on the belief that they will make more money in the long run that way. CEOs and top management can afford to defer their income gains, since their earnings and assets are still more than sufficient to live on and tide them over. But hardly any companies have offered stock options to their line workers. Companies have assumed that line workers won't understand or value these options. Moreover, low-income workers clearly can't afford to defer their income in the same way as managers.

In 1996, Dancing Deer defied tradition and put stock options in place for everyone, from bakery and factory floor workers to senior management. The company ensured that it paid its line workers wages that were at least as high as those paid for similar jobs elsewhere. Unlike management, line workers were not asked to accept lower salaries in exchange for stock options; that would have been utterly unrealistic since there was no way they could have lived adequately on reduced salaries. It was also unnecessary for them to do so, since the company was able to price its goods in line with similar products from other companies.

Management believed that providing stock options would be good for employees since it would allow them to grow assets and share in the company's financial success. The company would benefit from employees' increased sense of ownership. The stock-option program provided a way to distribute the benefits of everyone's hard work while ensuring that employees felt the importance of increasing the company's productivity.

Providing Stock Options

It is extremely rare for a small business to provide stock options to its lowest-level employees. According to the U.S. Bureau of Labor Statistics, only 1 percent of employees in small businesses receive stock options as part of their employment package, and those who do are overwhelmingly professionals.[31]

At Dancing Deer, all employees enter the stock-option program when they are hired. There is a four-year vesting period, and at the end of each year an additional 25 percent of stock is vested. The amount of stock that employees are entitled to is determined according to five employee categories, starting with nonsupervisory workers, who are entitled to a thousand shares. The second incarnation of the plan began August 15, 2006, at which time the company closed the original plan and paid those with stock options, with amounts ranging from $1,000 to $10,000. How much are Dancing Deer stock options worth? Karter did the calculations: "Stock options are tied to the sales of the company. Employees get one thousand to ten thousand shares. There are 3 million shares outstanding. The goal is to get one year's annual wages out of the market transition (in approximately four years) . . . Eventually there will be a merger or a strategic acquisition. If Dancing Deer [gets] to $100 million in five years, even with only a thousand shares, it's a lot of money."[32]

This was their vision, but were they able to make it happen? Like many rapidly growing companies, Dancing Deer periodically needed to seek venture capital to enable and stimulate growth; in exchange for venture capital, investors received stock options. Dancing Deer had to raise capital when it moved out of its facilities in the old pizza shop into the commercial production facility in Roxbury. Every time the company had to raise more capital for growth, it ran the risk of a decline in the value of employee stock options unless its productivity and sales outpaced the dilution of the stocks. Thankfully, company growth was rapid, and it was significant enough for employees to notice it. Between 2005 and 2006, sales increased by 74 percent and stock options increased in value by 40 percent.

Even if the company's value grew to only half of Trish Karter's aspired $100 million—either because the company itself did not grow rapidly or because of the downturn in the overall economy—and even if this more limited growth required bringing in more capital, employees' assets would still be significant. Keith Rousseau, the controller, calculated: "So if . . . [we were up to] $50 million, and I'm assuming 4 million shares . . . that might get you to $10 an option, which would leave you about eight or nine grand for a thousand [options] for a four- or five-year period."[33]

Dancing Deer was aware of the stereotypes about so-called low-skilled employees not understanding the stock options, but their experience contradicted these generalizations. Management developed clear tools for explaining stock options to employees who had never owned stock and who did not know anyone who had ever received options. The employee handbook explained what the payout would be for stock options after the $40 million valuation point and it gave a straightforward explanation of the link between employees' efforts and the worth of the stock options: "These options are a valuable part of your earnings and are an incentive for you to use your best efforts, every day. We believe this program is one of the key reasons why we are a healthy and growing company. We also believe it's the right thing to do . . . The increased value is tied directly to the increased sales level of the company. Since each of you impacts our ability to grow, we think you each should share [in the] upside."[34]

Employees were clearly aware of the stock-options program and of its potential to benefit them. Keith Rousseau described how the stock options became much more concrete for all the employees when they saw other employees cash in their options. He gave the example of Carlos Cardoza, a monolingual Spanish-speaking employee who had been with the company for ten years. Cardoza was about to return to Colombia to care for his elderly mother. His options had vested and he would be turning them in before he left in exchange for a check. Rousseau described the situation: "He doesn't speak English well, but he certainly understands that . . . when he started, they were packing cookies in a little pizza shop, and he knows [the company's growth] is worth something . . . I think people understand that they have ownership."[35]

Trish Karter further elaborated on employees' sense of ownership:

> I would say the minority of [employees understand] the technical functionality of the shares. But how many of them get the sense, understand that they've got some piece of it, and that they're all valued, that it's not just a meritocracy, but there's an egalitarian sense that there is no unimportant work? [They all understand that] whether you're a dishwasher or you're running the marketing of the company, your job is important and you have a say. It might not be a huge say, economically, but your voice is just as loud.[36]

Crucially, these stock options did not replace retirement benefits. In companies where all of line workers' pensions have been invested in the company's own stock, employees face far too great a risk if the company fails. The stock options at Dancing Deer gave employees a chance to earn from the company's profits while still receiving wages consistent with the industry and pension benefits to live on once they retired.

TRANSLATING ASSET BUILDING INTO RETURNS FOR THE COMPANY

Dancing Deer had two main motivations for implementing the stock-options program, one of which was a sense of fairness. Management believed that employees should receive some share of the growth resulting from their hard work. The other motivation was economic, based on the notion that enabling employees to have a stake in the company would result in higher earnings.

INCREASING PRODUCTIVITY

When employees were hired, they were told that they would be getting stock options and they would therefore have a stake in the company. But this alone was not enough for ownership to translate into economic performance. In practical terms, translating partial employee ownership into increased productivity required two crucial steps.

First, all employees had to be made aware of how the company was faring against its target outcome measures. Rousseau described how they accomplished this by holding a series of meetings with employees:

> We have a flash group which [consists of] pretty much all the senior management. We went through [this with them] last Tuesday and

> then what we're going to do is have two or three different meetings [with all the employees] . . . We'll bring everyone up, show them the sales, show them the expenses, show them the profits; explain to them what looks good compared to last year and what looks good compared to our budget, and what doesn't look good compared to last year, what doesn't look good compared to our budget; [show them] our strengths and weaknesses; and try to explain the best we can—without giving them an accounting course—how we're doing. And that seems to be one of the things that people really enjoy hearing . . . Since I've been here we've certainly had great quarters of sales and great quarters of earnings and we've had poor quarters of sales and poor quarters of earnings. And people take it to heart if things aren't going right, or if things are going great. It's the same as with a sports team . . . Everyone feels very [involved] . . . There's a good deal of ownership.[37]

The second step was more complicated. It required ensuring that the whole staff—from production to sales—participated in improving outcomes and understood the reciprocal relationship between their performance and the quantity of sales. Rousseau explained:

> You're just not going to continue to grow your sales at a 30 to 50 percent growth rate if you don't have a good product, if you don't have good customer service, if you're putting the . . . cookies in the wrong boxes . . . Because a lot of times . . . there's a mentality with the operations folks that they don't have any control over the sales, and there's the perception that we're always trying to fight. [They say,] "How can I affect how much sales you bring in?" And the sales guys have the also misguided perception that they have no control over operating margins or that kind of stuff. Where in fact, it's a continued conversation. The operations team very much has an effect on sales based off of the product and the experience that the customer's going to get. If operations is just mixing up boxes and giving out stale cookies, that's going to hinder the sales [team's] ability to sell. And the flip side, if the sales guys are continually creating these low-margin items that are difficult to manufacture, they're gonna impact the manufacturing operations and margins. So trying to have one common theme throughout . . . How do you increase your sales? It's [by having] better sales, better operations, better customer experience. I think that's what we've

proven. It's one of the major contributors to why we've grown so fast . . . Really having a great customer experience, really pushing to have the highest quality, [the] best product out there.[38]

Encouraging involvement and input from workers at all levels of the company was essential to the success of employee ownership. Management had to be willing to listen to the production staff. Trish Karter made frequent visits to the bakery, during which she listened to employees' suggestions. Employees at all levels felt that their input was valued and influential. Marta Sánchez, a mother of two, had been with the company for six years. Originally from El Salvador, she had worked at a restaurant in a neighboring town before coming to Dancing Deer to pack cookies. She summarized the company's openness to suggestions: "Good ideas are appreciated."[39] This was not the case for many workers at the bottom of the ladder in other companies. Keith Rousseau explained how the company benefited from employees' suggestions:

> One of the things that we love doing and that Trish loves talking about is being able to ask any of the employees: "What is working about this particular line or this particular process? What can be improved?" And we've had a bunch of things come up. We had one [situation] recently where one of the packing supervisors was playing around with one of our machines and packed cookies differently and brought it upstairs and said, "You know, this is a lot faster than the way we're doing it and it looks kind of cool." And of course one of the sales guys gobbled it up and said, "You know, we're looking for new packaging for one of our other customers. This would be perfect." And so there's a good chance that [it] . . . might show up as one of our new product lines. So we're continuously trying to . . . get feedback from everyone in the organization. One of Trish's great mottos is that some of the best ideas come from the people that you typically wouldn't ask first-off. So that's one of the reasons we've grown so quickly and the processes have increasingly gotten better.[40]

Receiving quality input from employees was an essential ingredient in ensuring that Dancing Deer's investments in its employees at all levels led to improved performance and profits.

LOWERING TURNOVER AND RECRUITMENT COSTS, AND OTHER ECONOMIC BENEFITS

Two of Dancing Deer's rewards for its efforts to provide good working conditions have been its low turnover rate compared to other companies in the industry, and its ease of recruitment. Like at Jenkins Brick, management was aware of the fact that the length of an employee's stay with the company had an impact on productivity. They also knew that they had to outdo their competitors, for whom turnover was a big issue. When we spoke with Lissa McBurney, the production manager, she noted that only one baking employee had left in three and a half years. Apart from the temporary employees they hired only for high seasons, only two packers left per year out of a staff of twenty-two.[41] Of those who left, very few did so due to dissatisfaction with their jobs; most left to pursue better opportunities, such as starting their own businesses.

The company's low turnover rate was achieved through the financial incentives offered to employees and the overall commitment to good working conditions. Keith Rousseau explained:

> I think the folks that really understand where Dancing Deer is going and really have a good understanding of what the potential upside is [are] more inclined to stay and wait it out, you know, and hope for this big payout . . . Being able to keep people here [also] tends to be something that's a result of people being happy, people feeling like they're respected, and the ability to have equal communication throughout the company.[42]

In addition to fostering low turnover, Dancing Deer's reputation as a good place to work has made it easy for them to attract good employees. Karter delineated how they had gathered a large pool of applicants to choose from:

> What we have going for us . . . We have a great pool of people that want to work here. We put an ad on Craigslist or Monster . . . or we put a word out to the network—just my network of people in the business—and we're swamped with [applicants]. And we [hear] the same thing, largely, which is: "I love your company. I don't exactly have the qualifications you're looking for, but I'd really love to

> figure out a way to work with you." And so you have options [of whom to hire].[43]

Outside observers commented on the impact. Referring to her conversations with a management consultant, production manager Lissa McBurney said: "He is . . . amazed at how well our people perform . . . That people want to do well. In working with him over the past six months I've realized [how much the investments do] pay off for us economically."[44]

Most companies offer asset-building programs only to their highest-level workers, in spite of the greater financial risks an absence of assets presents for their lowest-level employees. The companies profiled in this chapter clearly demonstrate that there are both ready means and strong benefits to companies offering asset-building opportunities to all employees. Dancing Deer's stock-option program was formulated in such a way as to provide incentives for employees to remain with the company, which in turn contributed to a reduction in turnover rates. The company had lower recruitment and retraining costs, as well as higher productivity from highly motivated employees. Jenkins Brick chose to contribute to employees' asset building by establishing a pension plan and a profit-sharing scheme. Like Dancing Deer, Jenkins Brick had benefited from these programs by experiencing reduced turnover, since employees' gains increased with the duration of their stay with the company.

Both companies offered programs that greatly benefited their workers by providing them with rare asset-building opportunities, and both companies also gained from these programs. Profit sharing and stock options linked employees' productivity to the companies' financial returns, since employees' assets increased alongside the company's improvements in performance. As a direct result, both companies experienced gains in employee productivity and product quality.

Beyond reaping the direct economic benefits, these companies also had the advantage of having a harder-working, more engaged, and lower-turnover workforce. Dancing Deer's overall commitment to providing good working conditions has brought them reputational advantages.[45] Trish Karter saw Dancing Deer's reputation as an important asset to the business: "Our social activism builds consumer loyalty and attracts highly motivated employees."[46]

Challenges of an Asset-Building Approach

Despite profit sharing's demonstrated ability to improve productivity among professionals when it is structured correctly, three perceived obstacles have kept many companies from expanding profit-sharing programs to workers at the bottom of the corporate ladder: first, the misconception that profit sharing does not motivate everyone across the economic spectrum; second, the concern that many of the usual ways to profit share are too complex to be readily understood by line workers; and third, the concern that it is difficult to find the right incentives.

We hope this chapter and the experiences demonstrated by Jenkins Brick, Dancing Deer, and others have convincingly laid to rest the misconception that economic incentives function so differently across the corporate spectrum that they are not transferable to employees at the bottom of the ladder. Clearly, there are differences across income levels. Everyone needs to earn enough to survive, and employees earning lower salaries cannot be expected to defer compensation in exchange for profit sharing. That being said, the knowledge that they will share in the company's profits motivates line workers just as it does vice presidents.

Dancing Deer demonstrated the feasibility of implementing complex forms of profit sharing such as stock options by making them both comprehensible and tangible to employees with limited formal education. The company developed materials that explained their stock options, guided workers through concrete examples, and talked in clear terms about what the money would mean for them. Jenkins Brick as well as Great Little Box (a company that will be discussed in chapter 7) are examples of companies that have found straightforward ways to share profits on either an annual or a monthly basis without requiring workers to understand the concept of stock options. Setting such programs in place requires one of two things: either using a transparent mechanism or developing materials that translate complex mechanisms into straightforward explanations of their impacts on individuals.

Perhaps the most complex—but still solvable—dilemma is how to get incentives on profit sharing right. Clearly consideration needs to be given in any particular setting to the advantages and disadvantages of profit sharing done on a monthly basis as it has been at the Great Little Box Company, so that workers can receive immediate rewards for progress;

on an annual basis to encourage intermediate-term thinking as done at Jenkins Brick; and longer-term vesting, be it through profit-sharing plans such as the one at Jenkins Brick or the stock options offered at Dancing Deer, which reward longevity in the company but provide far less immediate returns. Most successful companies in our research found a way to structure asset building so that workers both experienced immediate rewards—either in the form of immediate payment or of up-to-date notification of asset accumulation—and had long-term incentives to stay with their firms, either because vesting required them to do so or because they wanted to stay long enough to reap the investments that the company had made as a whole.

Notes

Chapter 4

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13. J. Luffman, "Taking Stock of Equity Compensation," Statistics Canada *Perspectives*, March 2003, http://www.statcan.ca/english/studies/75-001/archive/2003/2003-03-03.pdf.

14. Senior managers are referred to by their real names since they are identifiable through their positions at each company. Middle managers and low-level employees were ensured confidentiality and are therefore referred to by pseudonyms.

15. Interview conducted with Mike Jenkins IV, CEO, Jenkins Brick, March 2005.

16. Ibid.

17. Ibid.

18. Interview conducted with Wyatt Shorter, member of the board of directors, Jenkins Brick, March 2005.

19. Interview conducted with Tommy Andreades, executive vice president and CFO, Jenkins Brick, March 2005.

20. Interview, Mike Jenkins IV, March 2005.

21. Ibid.

22. Interview conducted with Anita Barrera, controller, Jenkins Brick, March 2005.

23. The experience of Jenkins Brick has been shared by other companies. Research has demonstrated that incentives for manufacturing sector workers lead to marked increases in performance. J. C. Sesil, "Sharing Decision-Making and Group Incentives: The Impact on Performance," *Economic and Industrial Democracy* 27, no. 4 (2006).

24. Interview, Wyatt Shorter, March 2005.

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26. D. Cusick "How One Energy-Hungry Company Learned to Love Landfill Gas," *Greenwire*, October 2007.

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29. Ibid.

30. Ibid.

31. U.S. Department of Labor, Bureau of Labor Statistics, *Employee Benefits Survey*, Statistics Data, generated tables. 2007.

32. Interview, Trish Karter, July 2007.

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35. Interview, Keith Rousseau, February 2005.

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37. Interview, Keith Rousseau, February 2005.

38. Interview, Keith Rousseau, July 2007.
39. Interview conducted with packer, Dancing Deer, July 2007.
40. Interview, Keith Rousseau, February 2005.
41. Interview conducted with Lissa McBurney, production manager, Dancing Deer, February 2005.
42. Interview, Keith Rousseau, July 2007.
43. Interview, Trish Karter, March 2005.
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45. Dancing Deer has received the Smaller Business Association of New England's New Englander Award for Innovation (2000), Awards for Excellence from the Greater Boston Chamber of Commerce (2001 and 2004), and a Small Business Leadership Award for Innovation from FleetBoston Financial Corporation (2002). The company was included in *Inc*. magazine and the Initiative for a Competitive Inner City's Inner City 100 list for four years (2001, 2002, 2003, 2008).
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