Impact of downsizing and restructuring decisions and processes on organisational knowledge and organisational effectiveness: Implications for perceived success.

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ABSTRACT

This study examines the impact of downsizing/restructuring decisions and processes on perceptions of organisational effectiveness, together with perceived levels of organisational knowledge after the downsizing/restructuring event in successful and unsuccessful organisations. The study hypothesises that the impact of these decisions and processes on levels of organisational knowledge are a key determinant of effectiveness in successful post-downsizing and restructuring organisations. The findings show, however, that the significance of these variables is to be found in unsuccessful organisations, rather than their successful counterparts.

Key words: strategic change; employee responses; employee perspectives; organisational learning.

Organisational downsizing and restructuring is a common response to changed economic circumstances and other environmental influences, with organisations implementing these changes in order to improve their effectiveness. The reasons why, and how, organisations downsize or restructure has a major influence on perceived outcomes. The impact of decisions made and processes undertaken in downsizing and restructuring organisations are examined in this study, hypothesising that such decisions and processes influence retention of organisational knowledge, which in turn may have a significant impact on perceived organisational effectiveness. Respondents to this study are divided into self-nominated 'successful' and 'unsuccessful' organisations post-downsizing or restructuring, against which the findings are compared and discussed. It will be shown that perceived level of organisational knowledge can be used as a general predictor of organisational effectiveness after downsizing/restructuring; nonetheless, it is the retention of knowledge, rather than its increase, that is necessary for improved outcomes after the occurrence of downsizing and restructuring.

CONCEPTUAL FRAMEWORK

Organisational Effectiveness

One of the primary motivations for organisational downsizing/restructuring is to achieve some form of improved organisational effectiveness (Freeman & Cameron 1993; Littler 2000). Many measures of post-downsizing and restructuring performance which appear in the literature relate to financial indicators, including lower expense ratios, higher profits, increased return on investment and improved share price (Bruton, Keels & Shook 1996; Budros 1997; Cascio, Young & Morris 1997; De Meuse, Vanderheiden & Bergmann 1994; Kabanoff, Palmer & Brown 2001; Mentzer 1996; Worrell, Davidson & Sharma 1991). Organisational performance measures also cover anticipated organisational improvements, such as decreased overheads, improved internal communications and greater productivity (Cascio 1993).

In the management of human resources, however, such measures are not always useful. The perceptions of those who work in an organisation are their reality, regardless of what may appear on balance sheets or share price listings. Attracting key employees is largely dependent on perceptions of the organisation; and retention is dependent on whether employees view the organisation as one in which they wish to remain and positively contribute. Perceptions of organisational effectiveness are therefore a relevant consideration for organisations contemplating downsizing and restructuring. In this study, factors identified by participants as affecting their view of the organisation as an 'employer of choice' are incorporated into the 'organisational effectiveness' measure. These factors include both 'hard' measures, such as financial indicators, as well as 'soft' measures, encapsulating the concept of organisational culture.

Organisational Knowledge

In investigating organisational effectiveness after downsizing or restructuring, this study considers the role of organisational knowledge in influencing perceptions of organisational effectiveness. Organisational knowledge, both explicit and tacit (Grant 1996; Nonaka 1994), encompasses the shared, accumulated knowledge of individuals within an organisation. Such knowledge is embedded in work processes and resultant products and services that evolve over time, all of which develop to incorporate lessons learned from the organisations' past experience. Gregory (1999) emphasises a

key presumption that organisational knowledge inherently involves familiarity with processes or tasks in the organisational context. Thus, knowledge lost through downsizing and restructuring requires recreation through organisational learning. Individuals must share and transfer their knowledge to other employees for organisational learning to occur, and facilitate the creation or recreation of organisational knowledge.

Research in downsizing/restructuring over the past 20 years has consistently identified organisational and individual issues commonly reported as occurring after downsizing/restructuring. It is contended in this study that many of these issues are associated with the loss of knowledge that occurs during downsizing and restructuring. Although much has been written about knowledge in organisations, little attention is paid in the literature to loss of knowledge in this context of downsizing/restructuring. Examples of downsizing outcomes which may indicate knowledge loss include the many reports of replacement of individuals or positions by re-hiring former employees, or engagement of consultants (Appelbaum, Everard & Hung 1999; Cascio 1993). Similarly, the reintroduction of ideas and practices, often termed 'reinventing the wheel' (Gregory 1999), is also frequently apparent, as are reports of inability to locate necessary information sources, both physical resources and people (Cascio 1993). These suggest that remaining employees ('survivors') find difficulty in accessing organisational knowledge. Organisational outcomes suggesting loss of knowledge are also evident in reports of lower productivity levels, inefficiencies, increased errors and falling work quality (Cascio 1993). Additionally, negative feedback from both clients and employees is also often reported (Appelbaum, Patton & Shapiro 2003).

Lack of knowledge may also account for some of the uncertainty experienced by survivors, resulting in decreased job satisfaction, lower motivation and increased voluntary turnover (Appelbaum, Patton & Shapiro 2003; Cameron & Smart 1998; Appelbaum et al. 1997). Increased stress, pressure and burnout are also reportedly experienced by survivors, along with a loss of trust in management and colleagues and communication breakdown (Appelbaum, Patton & Shapiro 2003; Cameron & Smart 1998; Cascio 1993).

Appelbaum, Patton and Shapiro (2003) stress that failing to take into account position-holders' interdependencies, the importance of core competencies, retention of skills, and maintenance of

institutional memory, is likely to result in perceived negative organisational outcomes from downsizing. Williams (2004) also states that downsizing and restructuring remove individuals' knowledge and experience, and break down key relationships between employees and with external stakeholders. He concurs with the underlying premise of this research, that such a breakdown can have significant impact on organisational 'culture, cohesion and cooperation', as well as placing organisational knowledge at risk.

This study investigates the proposition that organisational knowledge plays an important part in determining organisational effectiveness and the following hypothesis advances this proposal:

H1: The higher the perceived level of organisational knowledge the higher the perceived post-downsizing/restructuring organisational effectiveness.

Downsizing/Restructuring

Whilst downsizing is one of a range of strategies that may be implemented to achieve a new structure, it is also a term closely linked with 'restructuring' in the minds of many in the workforce. Anecdotally, some employees in organisations consider the term 'restructuring' to be a code used by managers for the harsher reality of 'downsizing', resulting in job loss. While the terms are theoretically distinct, in the work environment they are often used interchangeably, and have been treated as one term in previous literature (Burke & Greenglass 2000; De Witte, Vandoorne & De Cuyper 2005). The term 'downsizing/restructuring' is therefore used in this study to incorporate the broad concept of change to internal operations of an organisation that may result in decreased positions and/or employees, regardless of the strategies used to achieve the change.

Decisions

Underpinning downsizing/restructuring, are the decisions driving the changes, together with strategies implemented by the organisation to bring about the 'new' organisation. Freeman (1999) contends that decisions and strategies used by organisations vary widely, ranging from those organisations whose primary decision is to downsize radically, and restructure the organisation in response to this decrease in staff numbers; to those organisations that seek to restructure the organisation to improve operations, with downsizing being an incidental, rather than key, focus. The motivation in each case is different, as are the resultant experiences and perceptions of the employees involved. Those who experience

organisational restructuring that necessitates downsizing, may have more positive perceptions of restructuring and downsizing than those who have experienced organisational restructure or redesign resulting primarily from an imperative to reduce numbers (Cameron, Freeman & Mishra 1991; Freeman, 1999; Kozlowski, Chao, Smith & Hedlund 1993).

Decisions made regarding the downsizing/restructuring approach to be adopted will impact the skills and knowledge retained in the organisation, as well as employees' resultant perceptions of procedural fairness (Brockner, Tyler & Cooper-Schneider 1992). For example, an approach that removes significant numbers of long-term employees from the organisation is likely to have a major impact on understanding of corporate history, whilst a strategy that focuses on 'last in first out' may result in loss of current skills and contacts in the industry. An approach that relocates existing staff to other parts of the organisation may retain both history and specific skills but result in less than optimal proficiency in those parts of the organisation. Therefore, decisions made regarding how to reduce a workforce have a variety of potential impacts on organisational effectiveness.

Processes

Strategies used to achieve the reduction in workforce are also influenced by the nature of change to be introduced. Proactive 'downscoping' strategies (De Witt 1998), where organisations re-focus on their core business by narrowing the scope of operation, are part of a medium to long-term change in strategic direction, rather than a response to immediate financial pressure. Time is available to consider the organisation's future needs and achieve required decrease in staff numbers through strategies such as natural attrition, reduced hours, internal redeployment, leave without pay and other low impact downsizing strategies. Such strategies avoid the sudden, radical loss of significant numbers of employees who may possess knowledge and skills that the organisation will continue to need (Bruton, Keels and Shook 1996; Cascio et al. 1997).

The above suggests a planned, intentional downsizing/restructuring approach through process, rather than a 'knee jerk' reaction, is likely to be more beneficial to the organisation. This study examines this consideration; investigating the extent to which employees involved in downsizing/restructuring in the participant organisations perceive that various downsizing/restructuring strategies available to the organisation are actually considered.

The importance, or otherwise, of perceived relevance of downsizing/restructuring decisions and perceptions of downsizing/restructuring processes on organisational effectiveness are tested in the following hypotheses:

H2: The greater the perceived relevance of downsizing/restructuring decisions, the higher the perceived post-downsizing/restructuring organisational effectiveness.

H3: The more positive the perceptions of downsizing/restructuring processes the higher the perceived post-downsizing/restructuring organisational effectiveness

The decisions and processes considered in this study focus on their respective impact on perceived levels of organisational knowledge. In doing so, it is postulated that the way in which decisions and processes affect retention of organisational knowledge may explain the resultant perceptions of organisational effectiveness, as proposed in the following hypotheses:

H4: The greater the perceived relevance of downsizing/restructuring decisions, the higher the perceived post-downsizing/restructuring organisational knowledge.

H5: The more positive the perceptions of downsizing/restructuring processes the higher the perceived post-downsizing/restructuring organisational knowledge

A conceptual framework for this study is presented in Figure 1. In addition to analysing the direct relationship between the dependent variable, *perceived post-downsizing/restructuring organisational effectiveness*, and the independent variables of *downsizing/restructuring decisions* and *processes*, two indirect paths are analysed. Further, the relationship of each of the independent variables is analysed against *perceived level of organisational knowledge* to ascertain whether *perceived level of organisational knowledge* mediates the relationships between the independent and dependent variables.

Insert Figure 1

METHODS

The study was conducted through a two-stage process. The first stage consisted of qualitative focus groups, bringing together people who have been involved in downsizing and restructuring. The focus groups explored participants' views on the decisions and processes experienced in downsizing and restructuring, and the impact of both on organisational knowledge and perceived organisational

effectiveness. The second stage was gathering of data from a questionnaire, developed from review of the literature and themes that emerged from qualitative data drawn from the focus groups.

The dependent variable of organisational effectiveness was used as the basis for separating the data into 'successful' and 'unsuccessful' organisations. Organisational effectiveness scores of 3 or above on the 5-point Likert scale items in the questionnaire indicated those organisations rated by respondents as 'unchanged' or 'better than before', were labelled 'successful' organisations. Data from respondents indicating scores below 3 (that is, perceived to be less effective than before the downsizing/restructuring) were labelled 'unsuccessful'.

Sample

Data were obtained from 646 employees in 81 organisations, representing both private and public sector organisations in Australia. The majority of respondents (n=522) indicated they held 'managerial', 'professional' or 'clerical' positions. A breakdown of sample by gender reflects an even distribution of male (50.5%) and female (49.5%) respondents.

Measures

The questionnaire contained 127 measurement items, and included coverage of the four variables of organisational effectiveness, organisational knowledge, downsizing/restructuring decisions, and downsizing/restructuring processes. The items used to assess the four variables were developed from review of the literature and analysis of content drawn from the focus groups.

Organisational performance measures frequently focus on 'hard' financial indicators, such as return on investment and share price (Cascio 2002; Yu & Park 2006); however, such measures were not considered appropriate for the purposes of this study to determine the effectiveness with which organisations were perceived to operate after downsizing/restructuring. Therefore, 'soft' indicators indicating employee satisfaction, morale and attitudes (Price 2004) were used to measure post-downsizing/restructuring organisational effectiveness. Items measuring organisational knowledge were developed from the focus group process and literature (Grant 1996; Polanyi 1967; Snyder & Cummings 1998; Teare & Raynor 2002) and encompassed both tacit and explicit forms of knowledge. Tacit knowledge was assessed through questions relating to access to people with expertise, and explicit knowledge was canvassed through items indicating the extent participants had access to

necessary sources of information. The measurement of *decisions* was achieved through respondents indicating the extent to which they perceived a range of key issues (such as alternatives to layoffs, retaining key staff, documentation of procedures, training and handover options) had been taken into consideration during the downsizing/restructuring. The measurement of *processes* required respondents to indicate their experience of the actual downsizing/restructuring (including planning, documentation of procedures, handover and training opportunities).

Data Analyses

The validity and reliability of the variables were assessed using the item reliability, construct reliability, and average variance extract, together with Cronbach's coefficient alpha. Four factors measuring organisational effectiveness, organisational knowledge, and downsizing/restructuring decisions and processes emerged from this analysis, the results of which are presented in Table 1. Discriminant validity revealed the higher correlations between items comprising each construct, which were in turn utilised in regression analyses to test the hypotheses.

Insert Table 1

Factor loadings indicate the degree to which items are correlated with the latent variable they measure. Loadings greater than 0.5 indicate a high correlation between items and the latent variable being measured. Cronbach's α is a measure of reliability; the nearer the measure is to 1.0 the more reliable the items are deemed to be in measuring the latent variable.

RESULTS

Organisational knowledge was found to have a significant positive impact on organisational effectiveness (Hypothesis 1) in unsuccessful organisations ($t = 6.272$; $p < .000$), but not in successful organisations. Downsizing/restructuring decisions failed to show a significant positive relationship with organisational effectiveness (Hypothesis 2) in both successful and unsuccessful organisations. However, while downsizing/restructuring processes failed to indicate a significant positive relationship with organisational effectiveness (Hypothesis 3) in successful organisations, such a relationship was found in unsuccessful organisations ($t = 3.019$; $p < .005$).

When the intervening variable, organisational knowledge, was regressed on the independent variable of downsizing/restructuring decisions (Hypothesis 4), no significant relationship was found in either

the successful or unsuccessful organisations. The lack of significant relationship was held between downsizing/restructuring processes and organisational knowledge (Hypothesis 5) in successful organisations, while a positive relationship was found in unsuccessful organisations ($t = 5.151$; $p<.000$).

In order to investigate potential mediation by the intervening variable of organisational knowledge, it is necessary for this variable to have a significant impact on the dependent variable of organisational effectiveness. Since Hypothesis 1 was not found to be significant for successful organisations, organisational knowledge did not significantly affect organisational effectiveness amongst this group. Similarly, the hypotheses relating to decisions (Hypotheses 2 and 4) were not significant in unsuccessful organisations; mediation testing was therefore not applicable in these cases. However, partial mediation by organisational knowledge was evident in the relationship between downsizing/restructuring processes and the dependent variable of organisational effectiveness. The mediation analysis is summarised in Table 2 below.

Insert Table 2

DISCUSSION

Initial testing of Hypothesis 1 was important in order to establish whether changes to perceived levels of organisational knowledge resulted in corresponding changes in perceptions of post-downsizing/restructuring organisational effectiveness, before examining the relationship between the independent variables and organisational knowledge. Hypothesis 1 was supported in unsuccessful organisations; however, organisational knowledge did not prove to be a significant determinant of organisational effectiveness in successful organisations, an unexpected and counter-intuitive finding. Examination of the definition of 'successful' may provide some explanation for the above finding. 'Success' was defined as stability or improvement in perceived organisational effectiveness after downsizing/restructuring. The Hypothesis therefore implies that increased organisational effectiveness results from increased organisational knowledge and, correspondingly, decreased organisational knowledge leads to a decrease in organisational effectiveness, defined as 'unsuccessful'.

Support for the relationship between organisational knowledge and organisational effectiveness in unsuccessful organisations indicates that knowledge loss through downsizing/restructuring results in a negative organisational outcome. Lack of such support for this relationship in successful organisations may indicate that whilst losing knowledge has a negative outcome, increasing knowledge is not essential for a positive outcome to be achieved. For the latter group, knowledge retention may be a more important goal than increased knowledge. Since downsizing/restructuring rarely has the intention of increasing knowledge, this is a logical finding and serves to reinforce the importance of retaining knowledge in order to achieve a 'successful' organisational outcome.

Neither of the Hypotheses (2 and 4) involving downsizing/restructuring decisions was supported, indicating that downsizing/restructuring decisions are not a significant predictor of organisational effectiveness, nor organisational knowledge; these findings are common to both successful and unsuccessful organisations. Nonetheless, seminal researchers in the field of downsizing (Greenhalgh, Lawrence & Sutton, 1988), propose that decision-making factors, such as the context and background of the downsizing/restructure event, are critical issues for consideration in downsizing/restructuring. Whilst apparently insignificant in predicting organisational outcomes in this study, it may be that downsizing/restructuring decisions are only an indication of intended actions, as opposed to the *actual* process of events experienced by the participants. Therefore, respondents' perceptions of their intent and motivation are derived from their downsizing/restructuring experience of processes, rather than the initial decisions.

Nonetheless, where processes are viewed positively, corresponding increase in perceptions of organisational effectiveness are apparent to those respondents in unsuccessful organisations, this is not the case for respondents in successful organisations. As with decisions, the difference between successful and unsuccessful organisations may indicate that poor perceptions of downsizing/restructuring processes have a negative impact on organisational effectiveness. However, improved organisational effectiveness does not require positive perceptions of the processes; rather negative perceptions should be avoided. The general environment of successful organisations may be one where clearly communicated, transparent and open processes are expected and good practices may be the norm. Again this indicates that improved perceptions are not necessary for a positive

organisational outcome, but the absence of clarity and transparency may result in a negative outcome. Poor processes must therefore be avoided if effective downsizing/restructuring outcomes are to be achieved.

The findings suggest that organisations planning downsizing/restructuring need to ensure the processes they utilise promote retention of knowledge within the organisation. The ways in which this may be achieved vary; examples include retaining key employees or allowing time and resources, such as information systems, technology and databases, to facilitate conversion of tacit knowledge to explicit knowledge, through documentation and training. Other processes canvassed include communication to check for understanding of why decisions are made, engaging employees throughout the downsizing/restructuring process and building a supportive culture which recognises the need for and benefit of change.

Employees' interpretation of downsizing/restructuring decisions and processes has a direct impact on outcomes, implying that consideration of these potential reactions may also be relevant. A high degree of honesty, transparency and openness in management of the processes may go a long way to ensuring subsequent positive attitudes and behaviours. Such integrity in process may support maintenance of both job satisfaction and organisational commitment, necessary ingredients in the achievement of improved organisational effectiveness. The lack of significance found in the hypothesised relationships in successful organisations may indicate that these strategies and sound management practices are already in place prior to downsizing/restructuring occurring in these organisations.

CONCLUSION, LIMITATIONS AND RECOMMENDATIONS

Organisations undertaking downsizing/restructuring should consider the culture and climate of the organisation in regard to mechanisms for knowledge retention and how knowledge can be retained, within their implementation strategies. Managers instigating downsizing or restructuring in organisations need to be cognisant of the impact of such initiatives on employees and strive to ensure the experience is as constructive as possible. Inherent in proactive approaches are time to plan the process, as well as communicating openly with staff and involving them in the decision-making as

canvassed in the survey instrument. Time is also required for employees to prepare for the change and make necessary arrangements such as documenting procedures and handing over tasks. Support strategies, such as counselling to assist employees deal with the changes, together with training in new skills required for changed roles, and redesign of jobs and systems are also important in ensuring a positive experience for employees and maximising knowledge retention.

In this study, however, no support was found for hypotheses regarding the relevance of decisions in downsizing/restructuring events, either in regard to perceived levels of organisational knowledge or organisational effectiveness. The study did not, however, distinguish between those making and those implementing the decisions. Examination of perceptions from these two sources of data will lead to further insight into the importance of decision-making and implementation processes in downsizing/restructuring.

Nonetheless, the findings of this study demonstrate a need to concentrate on organisational knowledge during downsizing/restructuring in order to achieve improved outcomes. This can be facilitated by giving attention to the intent and interpretation of decisions and processes from employees' perspectives, and ensuring both are transparent. Assessment of the knowledge present in the organisation, and a focus on retention of key individuals holding such knowledge, is also advisable. The inclusion of employees in planning and implementation, and open communication around those strategies, enable the organisation to use its inherent knowledge in moving theory into practice.

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Figure 1. Impact of Downsizing/Restructuring Decisions and Processes on Organisational
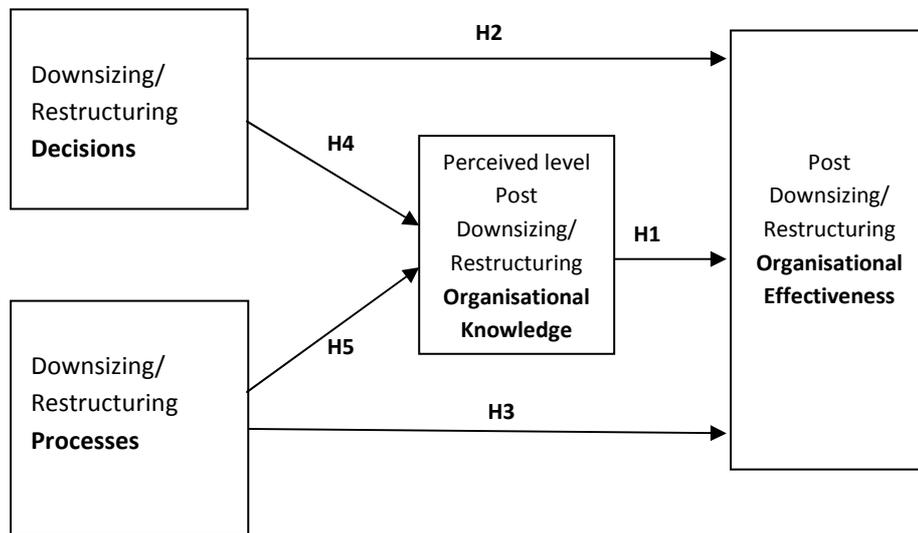Effectiveness and Organisational Knowledge;

Table 1. Factor Analysis and Construct Reliability

Construct	Number of Items (factor loading >0.5)	α
1. Organisational Knowledge	10	**0.910**
2. Downsizing/restructuring Decisions	10	**0.920**
3. Downsizing/restructuring Processes	11	**0.943**
4. Organisational Effectiveness	12	**0.956**

Table 2. Summary of Mediation Testing

Analysis:	Mediating effect of Organisational Knowledge on relationship between Independent Variables & the Dependent Variable (Organisational Effectiveness)	
Population:	Downsizing/ Restructuring Decisions	Downsizing/ Restructuring Processes
Successful Organisations	No	No
Unsuccessful Organisations	No	Partial