

Productivity's Last Frontier

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Achilles Heel of Productivity

“Win or Lose is in the eye of the beholder”

Economists have long held that people in an a monetary transaction or exchange are motivated by self interest, intent on maximizing individual payoff in any exchange setting. Essentially, economists assume that at least one person in a two party transaction will lose. Each party is driven by self interest. When this self regarding behavior results in a worker reducing their effort for a promised wage (to gain a better pay-off), it is often referred to as “shirking”. As an example, shirking is viewed as a “loss” to the employer and a “win” to the employee. The shirker receiving the same wage for less effort. The employer paid too much, and the worker received a better pay-off for their actual effort. However, others suggests a win or loss is defined by the individual perception of the pay-off only after the exchange is complete. On payday, a peer employee may feel cheated after they realize the shirker's pay and their pay is the same, now feeling justified to shirk as well. Because people are different, no two have the same expectation of a winning pay-off. What may be a win to one may be a loss to another. Perhaps it is the interaction of people involved and the framing of the trade which holds the key for understanding how dramatic improvements in productivity can be made.

The Problem with Promising Effort

“The promise of effort is not very sticky”

There are numerous methods for completing a monetary exchange associated with labor. Typically, all exchanges are governed by a set of rules or a contract. In the case of hourly wage compensation, an employer offers a wage for the promise of effort from a worker. Something of value, money, is exchanged for a promise to give effort, work. The challenge for an employer is to make margin (employer wins) even though worker effort may fall short of expectation (worker wins). This problem is not new. Generally, management science is chartered with assuring the effort by an employee is commensurate with the wage offered so the firm can make a profit. Management scientists and economists alike continue to investigate methodologies for improving the efficiency of the business process, Six Sigma and Lean are good examples. Unfortunately, these initiatives deal indirectly with the “promise of effort” challenge, tending to rely on better business process to deliver better outcome. All too often, the promises of Lean and Six Sigma are not sustainable. The fundamental problem with effort is, it is voluntary, one does not always give what is promised.

Research conducted earlier in the decade¹ found that

¹Fehr, E, (2002) Psychological Foundations of Incentives, Working Paper No. 507, University of Zurich, Lazear, E. (2000), “Performance, Pay and Productivity.” American Economic Review, 90, 1346-1361 and Gintis, H. (2005) Behavioral Game Theory and Contemporary Economic Theory, Analyse & Kritik 27/2005 pp 48-72

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employees tend to give maximum effort when a “pay-off” is tied to output; clearly deterministic, verifiable, and immediate but not necessarily within their own control. This notion of believability without full control is, in a sense, quite counter intuitive. Both research and our experience demonstrate an employer achieves “believability” when the very next paycheck reflects actual effort voluntarily delivered by the employees. The effect of immediate feedback tends to reduce the uncertainty associated with perceived lack of individual control.

Accountability through Variable Pay

“People perform better when held immediately accountable for their promise.”

Productiv has re-engineered the employer-employee relationship through new technology. We have successfully tied pay-off for voluntary effort to first quality through-put in any production or service environment. The connection provides a significant incentive for performance; is executable and verifiable within the current pay period. In our approach, the employees of a firm receive a base wage plus a voucher for a share of the margin created by the actual output and aggregated effort of all workers. The result is a variable pay system, each paycheck a function of first quality throughput of the current work week. Production and wage accounting is accomplished through our proprietary software fully compliant with FLSA requirements.

Introducing variable pay as an instrument for accountability is possible because the technology creates objective transparent feedback. The feedback is the paycheck reflecting the work done last week, not three months ago or even last year.

The Bottom Line

“Unleashing the power of people to be better, faster, and smarter”

Our system, in use since 2006 at 6 locations logging more than 50,000 operating hours, is delivering dramatic results: individual worker productivity up by 67%, employee wages up 20%, while labor cost per unit produced is down by an average of 28%. This level of performance might suggest a compromise of product quality. To the contrary, every deployment has seen a dramatic improvement in product quality on the order of halving defect rate every 4 months. In our unique work environment, improvements are pulled by workers as they become stakeholders now able to answer for themselves “What's in it for me?”. The powerful combination of continuous improvement “pull” and improved first quality through-put at lower cost offers a clear advantage over traditional wage rate systems fueling additional profitability otherwise not achievable.

Productiv provides turnkey outsourcing and management services for Digital Media, Furniture, Housing, Health Care, and Consumer Products companies. For more information please contact Rich Boehling rboehling@getproductiv.com