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The Economics of Trust

Trust has measurable financial impact, reflected on the bottom line. That's the conclusion from a study of 7500 workers by Watson Wyatt Worldwide Consulting.

Their research (conducted in 2000) documented the positive correlation between high levels of employee trust and the payback to shareholders. In companies where trust was high, shareholder returns were 43% higher than in low-trust companies.[8]

Equally striking are findings at the QVC Home Shopping Network. QVC surveys their customers extensively, asking respondents to rate the company in terms of trustworthiness. A seven-point scale is used, with seven being the highest.

Most companies would be pleased with consistent ratings of six. But QVC has learned that people who rate the company at seven are 80% more likely to make repeat purchases than those who give it a score of six.[9]

Similarly, research at Case Western Reserve University shows the decisive power of trust when it's time to buy. The study asked people to identify the most critical factors in their decisions to make a purchase.

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[8] Bruce N. Pfau, "Employee Satisfaction Proves Crucial to Shareholder Value," *Strategy@Work*, found October 25, 2005 at http://www.watsonwyatt.com/strategyatwork/articles/2000/2000_04_ai.asp.

[9] John Hunter, "I Want My QVC," *CIO Magazine* (July 14, 2003), found April 19, 2007 at http://cio.com.au/index.php/id;127536714;fp;4;fpid;1;pf;1.

`For consumers the two most decisive factors were trust and perceived value, with perceived value ranked first by only a slim margin. In business-to-business transactions, however, the same researchers discovered that trust outranks perceived value. Companies are willing to pay more, it seems, to do business with those they trust.[10]

"If you don't have trust inside your company, then you can't transfer it to your customers."

– Roger Staubach

Customer trust, in turn, depends on levels of trust within your organization. In the words of Roger Staubach, the legendary Dallas business leader and Hall of Fame quarterback, "If you don't have trust inside your company, then you can't transfer it to your customers."[11] And research tends to bear him out.

Fortune magazine annually publishes a list of the hundred best companies to work for in America. The Great Place to Work Institute, which compiles the list, has studied the American workplace for over 20 years. They have reached the conclusion that "trust between managers and employees is THE primary defining characteristic of the very best workplaces."[12]

When I cite these kinds of statements and statistics, I get occasional pushback worded like this: "Company X is making a ton of money, and I know for a fact that there is deep, deep distrust in their organization."

Recently, in fact, a highly successful attorney made this very observation to me about his own firm. "Everyone knows there's a lot of distrust among principals in our company," he said, "but we have

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[10] Jeff Beudix, "Can You Trust Customer Trust?", found October 24, 2005 at http://www.case.edu/pubs/cnews/2000/12-14/singh.htm.

[11] Jerry Kavanaugh, "Q&A: Roger Staubach," *Dallas Business Journal* (January 14, 2005).

[12] Great Places to Work Institute Home Page, found June 10, 2006 at http://www.greatplacestowork.com.

never made so much money in our history. It's hard to build the case that distrust is costing us money."

I immediately replied, "And what is your turnover rate? How much of your budget each year goes to replacing key players who walk out the door?" He quickly acknowledged that the defection rate was sobering

"And does the distrust have anything to do with their departure?" I continued. He reflected momentarily, then answered with a nod.

I then inquired, "How much does it cost to replace each person who leaves?" He quoted a number that was fairly close to the national average for major law firms, which is about $300,000 to replace a solid performer.

"So if we multiply that cost by the number of people who are leaving each year," I went on, "then add in the volume of business that follows them out the door, that's how much money you are leaving on the table because of distrust."

Low trust and high turnover love to work shoulder to shoulder.

The reason I moved so quickly to their turnover rate is that low trust and high turnover love to work shoulder to shoulder. When companies are struggling to stay competitive and financially sound, it's easy to show how distrust and excessive turnover are putting them at a competitive disadvantage.

But in settings that are highly profitable, like my friend's law firm, management can blithely ignore distrust, assuming that its impact is inconsequential. After all, cash is flowing in torrents. Only against the backdrop of high turnover costs do we begin to see how just much distrust is draining the bottom line.

Due to shifting demographics, the challenge of limiting turnover costs will grow exponentially in the foreseeable future. With the baby boomers hitting retirement years, a rapidly graying workforce is already giving way to a much younger one.[13] This transition, in and of itself, adds immense turnover costs. But the greater turnover challenge lies elsewhere.

We are quickly learning that today's youngest workers are a breed apart from co-workers twenty or thirty years their senior. Compared to previous generations, the twenty-and-thirty-somethings in our organizations are less willing to sacrifice family life and personal fulfillment to advance their careers.

A high-trust culture reduces the opportunity for dissatisfaction and disillusionment.

They have also entered the workforce assuming frequent job changes over the course of their professional life. Given this expectation, they readily pack up and leave when they become dissatisfied or disillusioned or when work demands impinge on life-balance commitments. Long-term loyalty is a scarce commodity.

A high-trust culture, by its very nature, reduces the opportunity for dissatisfaction and disillusionment. A high-trust culture yields an atmosphere that tends to be healthy, positive, and energizing, the very kind of workplace that younger men and women demand.

Noting this fact, a vice-president for a Fortune 200 company lamented to me, "Our company does not yet realize how vital trust is for holding workers. Because we are one of those rare companies that still offers exceptional pension plans, older workers are sticking around to claim their retirement. They put up with outmoded management styles that won't be tolerated by the younger workers who will replace them. I'm afraid that we are about to be hit squarely in the face with that reality."

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[13] Of the workers between 25 and 54, six in ten are baby-boomers, and in some fields (such as science and technology) more than half the workers are over 40. Richard Florida, "America's Looming Creativity Crisis," *Harvard Business Review* (May 2004), p. 58.

As the workforce "youthens" (to borrow a term from King Arthur in *Camelot*), high-trust cultures will be one of the most important resources for holding turnover costs in line. In these cultures leadership will abandon the final vestiges of those outmoded management styles that impair trust, becoming instead purposeful about trust-building. Otherwise, they will leave themselves at a financial and competitive disadvantage as turnover exacts a needless toll on the bottom line.

Excepted from *Leadership and the Power of Trust: Creating a High-Trust, Peak Performance Organization* by Dr. Mike Armour

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