Managing Talent Risk

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Abstract

Talent Management is one of the most exciting topics in Management, and coincidentally, the same can be said about Risk Management. Additionally, it is worth mentioning that one of the most interesting features of Risk Management is the firm’s ability to attract and retain the most talented individuals. This article tackles this interesting problem by blending both topics into a single framework, and discusses the importance of achieving a superb management of the risk of losing talent in the organizations. The authors combine their knowledge and expertise in both topics and provide a model that helps understanding the basics of managing the risk of not being able to attract and retain the most talented individuals for the organization. The article is grounded on the identification of the likelihood of the person leaving the firm, and the importance of this loss, but moves beyond this discussion analyzing the determinants of the risk of losing talented people in the organization, by studying the causes for the employee’s willingness to leave and the reasons for the importance of this loss. This model allows us a better talent management by helping us identifying the critical variables that we need to control for each category of employee in order to minimize the probability of losing valuable talent in the firm.

Key words

Talent risk, talent, risk management, managing talent risk.

Resumen

La gestión del talento es uno de los temas más relevantes en el management en la actualidad y, coincidentemente, lo mismo puede decirse de lo que llamamos Risk Management (gestión del riesgo). Adicionalmente, es importante mencionar que uno de los temas más interesantes en Risk Management es la habilidad de atraer y retener a los individuos más talentosos. Este artículo discute esta problemática fusionando ambos temas (la gestión del riesgo y la gestión del talento) en un único marco conceptual. Los autores combinan sus conocimientos y expertise en ambos temas y generan un modelo que colabora en la comprensión de las consecuencias de no ser capaz de atraer y retener a los empleados más talentosos para la organización. El modelo se basa en la identificación de los determinantes del riesgo de que una persona talentosa deje la organización y en la comprensión de la importancia de su pérdida para ella. Este modelo nos permite tener una mejor gestión del riesgo de pérdida de talentos ya que nos ayuda a identificar cuales son las variables críticas a monitorear para cada tipo de empleado.

Palabras clave

Riesgo del talento, talento, gestión del riesgo, gestión del talento.
1. Introduction

There was a time when organizations and organizational theorists could easily explain what was expected of employees: organizations were hierarchical systems or mechanisms in which status were both important and a symbol of recognition (Hatch, 1997). Employees respected this hierarchy. Homogeneity and stability in the workplace were paramount and job stability shaped organizational life.

The equilibrium firms achieved during that era provided employers and employees with clear benefits and responsibilities. Employers needed to guarantee stable jobs and, in many cases, jobs for life; while this might be unrealistic today, it was feasible in the era of organizational stability. In turn, employees were expected to be loyal towards the organization and recognize the firm’s hierarchy. Most employees were happy with this fairy-tale arrangement. They got jobs. They could expect to retire from the company they first started to work with. They respected their bosses. Any position they achieved would have been earned.

Fairy tales do not last long, however. The outer context, within which firms were operating, became both more competitive and more complex. Firms’ inner context then followed suit. Organizations needed to adapt quickly to the changes posed by the business environment and they also needed to transform radically. Thus, the era of stability was replaced by an era of rapid changes and turbulence. Moreover, the old homogeneous workforce became a heterogeneous one in which, as Gladwell (2008) points out, various generations worked and overlap. Talent issues not considered previously now demanded attention.

These changes transformed the importance of talent management. Before, talent could be considered largely part of human resources’ domain. Now, in an era characterized by workforce heterogeneity and fast-changing, fast-paced environment, talent has become an organizational issue of concern to top management, line managers, and human resources alike. Everybody is, or should be, involved in managing talent. Talent management is now an important part of the firms’ strategy.

2. Time of revenge: the employees’ golden era

After years of an ever-changing context, already described in the opening paragraphs, companies started implementing a number of procedures aimed to ensure their survival over time. In particular, delayering, outsourcing, rightsizing, and downscoping, were the “solutions” that organizations employed at that time. The results of these procedures were flatter structures, new forms of organizing, and a large quantity of consultants, who flocked into companies with grand ideas that made employees tremble with fear. Today, skilled employees are becoming a scarce resource for many organizations. Because of this, companies are investing in recruitment, searching for the best talent they can find in today’s slim market.

Formerly, when companies evaluated production locations, not only were costs considered but also proximity to different markets. Today, companies are also regarding talent as a key element in their location decisions; clusters of firms seeking similar talents appeared. Silicon Valley is probably the easiest example of a cluster based on availability of talent, but the city of Austin (TX), the so-called Research Triangle in North Carolina, and the city of Bangalore in India, are other powerful examples of how talent became a driver for firms to cluster around. The demand for highly valued and high-caliber managerial talent is high and still growing (Michaels, Handfield-Jones & Axelrode, 2001). The best people are constantly offered new
Talent is then a resource that is valuable, rare, and hard to imitate jobs, making it difficult to retain them over long periods of time. Talented people know they are at an advantage when it comes to negotiation, in contrast to the suffering they were put through during the 1980s. This is the game firms are obliged to play today; a game of stakes, which affects companies’ operations and, in turn, can have a significant effect in their structure and in their bottom lines.

Table 1 points out the main transformations the business and talent realities have been through. The previous stability is now characterized by complexity, which includes crises and market jolts. The long-term career path has been replaced by people changing jobs frequently to mould their careers according to their wishes. The increasing in labor market mobility has decreased the commitment of employees to the organization, with a shift towards self-commitment. Moreover, today’s employees, mostly millennials, do not value job security as they did before; rather they feel powerful because they are aware of their importance to organizations (Hatuma, 2013).

Table 1
Business and talent realities: trends over time

<table>
<thead>
<tr>
<th>Business and talent stability</th>
<th>Next generation talent management</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business stability</td>
<td>Business complexity</td>
</tr>
<tr>
<td>Raising people from within</td>
<td>Searching from outside talent</td>
</tr>
<tr>
<td>Career development in a few companies</td>
<td>Job-hopping</td>
</tr>
<tr>
<td>Commitment to the organization</td>
<td>Self-commitment</td>
</tr>
<tr>
<td>Negotiation power: the company</td>
<td>Negotiation power: the person</td>
</tr>
<tr>
<td>Job security: critical</td>
<td>Job security: an old-fashioned value</td>
</tr>
</tbody>
</table>

3. The concept of risk

Risk is about uncertainty, is about events that can happen in the future, and the outcomes that can be different from original expectations. People tend to have a negative attitude towards risk, considering it as something dangerous that might affect them in a negative way. As discussed in Preve (2009) risk entails the possibility of obtaining a result that is better or worse than originally expected. The assumption of risks is the reason why firms make profits, but might also be the reason why firms generate losses and eventually go bankrupt. Not taking risks, on the other hand, is not an option; a company that does not take risks has no reason to exist. Profit is the reward obtained by a firm because of the risks it face. To compete, as stated by Buehler, Freeman and Hulme (2008), and Apgar (2006) among many others, is about choosing which risks to assume and how to be rewarded for that. It is also about deciding which risks not to assume, and how to eliminate them adequately. In other words, risk management, as suggested by Coleman (2011) is about “controlling the downside and exploiting the upside”, or about making profits with favorable volatility avoiding the extreme losses associated with unfavorable volatility.

The first step towards a modern risk management strategy is to identify all the relevant risks affecting a firm. We use the Risk Mapping, a process that allows the identification, listing, classification and measurement of all the relevant risks that might affect the firm. Risks are then identified, and usually classified into categories (i.e. strategic, operational, financial and political).
‘Talent Risk’ as one of the most fascinating risks to manage in the corporate world

Risk measurement is a tricky concept. It requires the estimation of two parameters: (i) the volatility of the variable or probability of occurrence of the event, and (ii) the effect that the volatility or the occurrence of the event might have in the company. The latter is quite straightforward, whereas the former is a bit more controversial: calculating the effect of an event in the company is relatively simple, whereas estimating the volatility of a variable or the probability of occurrence of an event needs some discussion. It is mathematically possible to measure the past volatility of a variable or the probability of occurrence of an event; we can find the best functional form that explains its past behavior, the question is, however, whether this is what we need! Is this past measurement really useful for measuring its future outcome? This has been stated in the literature, one of the most famous discussions about this topic is provided by Nassim N. Taleb (2007) in his best seller The Black Swan. Interestingly, the answer to this question is yes and no. The main problem is related to our ability to identify the determinants of the volatility of a given variable. Do we really know why the variable has had the observed behavior? We need to know the impulses that affected the variable’s behavior in the past, and those who did not affect it in the past but might affect it in the future. This means that we need to know which are the theoretical determinants of the movement of a variable under study, independently of whether they really affected the variable in the past or not. This happens because these determinants might appear causing a variable to have some unexpected behavior at some point in the future. This last point will become crucial when dealing with talent risk.

After we have identified and measured the risks, the risk map (some authors call this the heat map) will look like the one in picture 1 presented below, in which we observe all the relevant risks located into the Severity of the Impact/Probability of Occurrence framework. Notice that each risk falls into a risk space, with specific policies and procedures related to it.

Picture 1
Risk map
4. The talent risk

One of the relevant risks of most organizations is Talent Risk; the risk of “attracting and retaining” the talent needed to compete. Companies capable of attracting and retaining the most talented and suitable individuals can provide a sustainable competitive advantage to its stakeholders. Talent is then a resource that is valuable, rare, and hard to imitate. And talent management is a strategic activity aligned with the firm’s business strategy that aims to attract, develop, and retain talented employees at each level of the organization (Hatum, 2010, 2013).

Additionally the market for talent is far from being an efficient one; talent is not publicly traded, nor listed; rather, it tends to be hidden and difficult to find. We would argue that one of the single most important characteristics of successful firms is their ability to attract and retain talented people (Hatum, 2010); this situates Talent Risk as one of the most fascinating risks to manage in the corporate world.

While attraction and retention are both critical for firms’ success, in the remainder of this article we will mainly focus on the retention aspects of talent risk management, considering that retention is a way of daily attraction to the current employees. In order to consider talent retention risk we need to address the probability that each talented individual leaves the organization, and the severity of the problem caused by this defection. Notice that the two-dimensional space framed by these two considerations is similar to the risk map presented in Picture 1 above.

Top management tends to assume that talented individuals are going to stay in the company, but when they leave, sometimes unexpectedly and without previous warning, sometimes even to join a competitor, they find out—the hard way— that talent risk should be considered seriously. Additionally, sometimes, the person who is leaving carries a portion of important knowledge that might not be left in the company, since knowledge is, most of the times, packaged in people.

As stated above, in a standard risk mapping all risks are accommodated into a bi-dimensional space; (i) probability of occurrence and (ii) severity of the problem caused by the event. Considering talent risk, and in order to effectively manage it, we need to fit this risk in a two-axis space, where we consider the probability of this person leaving the company and the severity of the loss if the person effectively leaves the company. Picture 2, below, shows the basic talent retention map as explained above.

In an attempt to keep the model as simple as possible without losing the opportunity of capturing the complexity of the organization, each axis has been divided into two segments; high and low. As we can see this divides the chart in four areas, we have two areas in which we locate people that would generate a large problem in case of leaving the company; one includes people with low probability of leaving (area I), the other includes people with high probability of leaving the firm (area II). We also have two similar areas for people that, in case of leaving the firm would generate a small problem; some of them are very likely to leave (area III), and some others have a low likelihood of leaving (area IV).

Picture 2 suggests the importance of a clearly established set of talent management policies according to the risk threat proposed in each of the four areas of the chart; after all, people in each area generate a different risk for the firm, both, regarding the probability of the person leaving the firm, and the reason why this person leaving constitutes a problem. This
Hot markets constitute also relevant reasons why people might leave a company.

**Basic Talent Map**

<table>
<thead>
<tr>
<th>Importance of the person in the organization</th>
<th>Probability of the person leaving the organization</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low</td>
<td>Low</td>
</tr>
<tr>
<td>High</td>
<td>High</td>
</tr>
<tr>
<td>IV</td>
<td>II</td>
</tr>
<tr>
<td>III</td>
<td></td>
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</tbody>
</table>

Let’s start considering the probability of losing talented people. The relevant question here is, why is that person willing to leave the firm? We propose three potential reasons that might explain that defection: (i) the employee is unhappy with the job; (ii) the person is extremely talented; and (iii) the market is extremely hot, and willing to take any person with that particular background.

Unhappiness in the workplace is among the first causes of attrition in organizations and has been associated with decreased work performance, relationship conflicts at work, burnout, and increased job turnover rates, among others. A global Gallup Survey (The State of Global Workplace) reported that on average, only 13% of the employees are engaged at work, which means that about seven out of eight employees are not engaged! Due to the consequences of lack of happiness, firms have emphasized both, addressing the role of person-organizational fit in their recruitment processes, and building a consistent Employee Value Proposition (EVP) to convey individuals’ feelings and experiences at their workplace. The emotional bonding created by the EVP can help companies retain talented people (Rueff & Stringer, 2006).
Talented people usually have higher probabilities of leaving the firm; this new quest for talent in the market increases the probabilities of somebody asking a talented individual to join another company. In this highly interconnected world, spotting talented people becomes easier and cheaper, as talented individuals are easily put in the showcase. While there has always been some mobility of talent in organizations, the new generations are imposing a new paradigm to companies; they will leave if they find a better offer in the market. With a less committed workforce, job-hopping is viewed as a normal decision in people’s careers paths, and talented employees are in pole position (Frank, Finnegan & Taylor, 2004; Aselstine & Alletson, 2006).

Hot markets constitute also relevant reasons why people might leave a company. At some point in time, a given ability might be in short supply in the market, and this will spark a quest for recruiting all the persons of a given profile. The most talented individuals will get the first offers, but eventually most of the people fitting that profile will get offers. Consider for example the Oil or Information Technology (IT) job market. There is a dearth of specialist in a world of generalists. The more specific is the job, the more difficult is for firms when the market becomes demanding of such professions. Sometimes the same analysis can be made based on geographical considerations, in certain markets, the pool of qualified people is just not sufficient. Small markets usually generate good examples of this. In November 2007 the Finnish paper producer UPM (previously called Botnia), started the operations of a large pulp mill in Uruguay, a small country with 3.25 million people. During the construction period, several of the skilled technicians needed for the construction were not available in the country, so the company brought in a significant portion of the 900 steel welders needed for the construction, generating a small revolution in the sector; almost every firm that had a steel welder in the payroll lost it to this new venture.

As we can see, Picture 3 presents a three-dimensional space in which an employee can have a higher probability of leaving the firm, because of completely different reasons. Some highly talented individuals might be very happy with their jobs, and, even in the case of an exceptionally hot market for people with their competencies, they might be willing to stay in the company. Different settings could be built based on these three dimensional framework, on the one extreme, we can have a low talented person whose skills are not seek after by the market and is extremely unhappy in his job; on the other extreme, a very talented individual, is unhappy in his or her job, and with a very hot market to hire him/her. In between these extremes we can build all sort of combinations using these three variables. Interestingly, the market characteristics that affect the individuals’ probability of leaving tend to change over time. The happiness of the employees with their jobs might change over time; for example, a new boss, new responsibilities or a new location can spark a new level of dissatisfaction that alters the equilibrium. Market heat, as the willingness of the market of hiring people of certain skills, has shown significant changes over time. New technologies tend to change the relative importance of certain positions; for example, employees with IT skills have increased their employability in the last few years. Another reason that fosters a change in market heat is related to macroeconomic considerations. A country that receives a large wave of foreign investment is usually short of talent in certain –usually high skills- positions. Additionally, people change over time; most of the people tend to improve and show progress in their career, so, as they grow and become more skilled, they move higher in the talent axis of Picture 3.

As we consider each of the different areas, we can see that, not only it is crucial to determine the reason why the person is likely to leave the organization, but also, how is he or she located...
Knowledgeable people are those who bear the most influential information, know how, or feedback that contributes directly to the performance or success of the firm.

Picture 3
Reasons for people leaving the organization

<table>
<thead>
<tr>
<th>Market Heat</th>
<th>Dissatisfaction with job</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low</td>
<td>Low</td>
</tr>
<tr>
<td>Low</td>
<td>High</td>
</tr>
<tr>
<td>High</td>
<td>Low</td>
</tr>
<tr>
<td>High</td>
<td>High</td>
</tr>
</tbody>
</table>

in the other axis of Picture 2; i.e. Is this particular person very important for the firm or not? And most importantly, what explains this importance?

In order to complete our understanding of this analysis, we need to consider the reasons why somebody is considered important for the organizations.

Therefore, we propose that the severity of losing somebody in the firm is a function of: (i) the complexity of the job performed by the employee; (ii) the difficulty of replacement; and, (iii) the sensitivity of the knowledge that the firm loses in case the employee leaves. This generates another three-dimensional space; we show it in Picture 4 below.

Our markets and technologies get more complex. With digitization, interconnectivity between people and things has jumped by leaps and bounds. Jobs then are becoming more cognitively complex. Some of the features defining complexity are: (i) more team-based and collaborative tasks; (ii) higher dependence on technological competence; and, (iii) a faster pace of change.
Strategic talent management includes the identification of pivotal talent positions that causes technologies and business models to become obsolete almost without previous warning (March, 1995; Beechler & Woodward, 2009). Workers need to know more, not only to do their jobs and tasks, but also to work effectively with others on teams. Many knowledge-based tasks require sound analytical and judgment skills to carry out work that is more novel and context based, with few rules and structured ways of working. And on top of that, what seemed to be working fine until today, might not work tomorrow. Although demand for high cognitive skills is especially prominent in professional, technical, and managerial jobs, even administrative tasks require more independent decision-making.

While complexity is critical to today’s job market, we can also find a dearth of professionals in some highly competitive industries. Retaining professional talents is as difficult as trying to replace them. In emerging economies talent is sometimes scarce, expensive and hard to retain. A recent article by Dewhurst, Pettigrew and Srinivasan (2012), mentioned that in China barely 2 million local managers have the managerial and English-language skills needed by multinational firms. Additionally, the same study, reports that one of the leading world’s

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**Picture 4**

**Reasons why somebody is important in the organization**

- **Importance of the person in the organization**
  - Low
  - High

- **Job Complexity**
  - Low
  - High

- **Difficulty of Replacement**
  - Low
  - High

- **Sensitivity of the Knowledge**
  - Low
  - High
In some emerging economies, it is difficult to attract talent

banking institutions are paying top people in Brazil, China, and India almost double what it pays for the same position in the United Kingdom.

Executives in China, for example, must develop a nonmarket business strategy, as well as the usual market strategy. The nonmarket strategy includes plans for building a network that intersects with the government, business partners, suppliers, customers, and other industry and public stakeholders. On top of that the talent challenge for multinational companies in China has intensified since the generation born in the 1980s began to take on managerial responsibility. As a result of the government’s one-child policy and the uneven pattern of higher education, many businesses are facing a shortage of capable young executives. This is just an example of the difficulty of replacement of executive in emerging economies.

India, for example, is leading the Asia-Pacific region in turnover rates at 26.9% in 2013, the highest global attrition rate. This figure is expected to increase, and expectations stand at 27.5% for 2014. The IT industry is suffering the most with these high attrition levels. The cases of China and India suggest that replacement of good professionals is difficult in emerging markets and growing industries (Dewhurst et al., 2012).

Knowledge is, then, becoming critical. Knowledgeable people are those who bear the most influential information, know how, or feedback that contributes directly to the performance or success of the firm. The importance of knowledge motivated organizations to focus into creating a range of strategies and practices to identify, create and distribute insights and experiences, to avoid relying on one person or group of people who got the knowledge. There are, however, experts, managers or employees with sensitive knowledge, that companies do not like to lose. Parise, Cross and Davenport (2006) report that, when in the mid-nineties Delta Airlines was able to reduce labor cost by replacing several expensive and experienced mechanics, the lost knowledge, generated several operational problems whose cost exceeded the labor savings. When the firm had to reduce the workforce after 9/11, the knowledge maps were a critical driver for the decision regarding workforce. Thiele (2013), reports that Knorr-Bremse, a german manufacturer of braking systems for rail and commercial vehicles, considers that capability and knowledge building is a critical factor to have a stable operation in their China venture. In a similar fashion, in Lancaster and Stillman’s When Generations Collide, (Lancaster & Stillman, 2002), Mark Bailey, Director of Staffing and Recruitment at General Mills, explains that marketing managers take up to five or six years to “get to the top of their game”. He reports that losing one of them causes losses of millions of dollars for the firm. The loss of valuable knowledge is a serious issue in talent management, it is not easy to measure but its effects might be crucial for the sustainability of the firm.

Any successful talent risk management strategy has to relay on the dimensions defined in Pictures 3 and 4. Every employee of the firm should be plotted in its correct location in each graph. It is crucial to understand that these systems have an unstable equilibrium, and considering its own dynamics becomes of paramount importance, since an employee can change its own situation in each of the graphs in a short time and without previous notice. A highly skilled, very satisfied person, in a firm operating in a hot market can easily change its incentives to leave the company if some action weakens its satisfaction with his or her job. Additionally, the effects of his or her departure, has a different impact on the firm, depending on where is he or she located in the spaces in Picture 4. As we can see it is of crucial importance considering both graphs and its intersections in a coordinated manner when managing talent risks.
5. Concluding remarks

An interesting application of this analytical framework for managing talent retention risk is the fact that an organization should start locating its players in the quadrants determined in the charts presented in the article. A company that finds that most of its talented individuals are at risk of leaving and are critical for the future of the firm, would learn that it faces a high risk of losing valuable human capital and, in turn, a high operational risk that might affect its ability to compete in the market and its stakeholders satisfaction. This should motivate the senior management to work towards improving its ability to attract and retain certain profiles of talent, and maybe improving its talent mix according to the firms’ capabilities.

In a similar fashion, strategic talent management includes the identification of pivotal talent positions. Indeed, such identification should be the first step in any strategic talent management system. Pivotal positions are those that have the potential to differentially influence the firm’s competitive advantage.

The issue of managing talent risk is crucial for the firm, but in the reality of emerging economies, it becomes also a matter of national policy, allowing countries to dramatically affect its competitiveness. In some emerging economies, it is difficult to attract talent; the talent pool shrinks, and when crisis flare-up, a typical issue in some developing countries, good professionals seek job opportunities abroad. In such a context, talent risk management strategies become critical. In the seventies and the eighties, many argentine professionals fled the country seeking for a future. In the nineties, when the economy boomed, there was a severe scarcity of the professional human capital, urgently needed to seize the growth opportunities. Other emerging economies are considering the quest for talent as a critical stance for their national policies. Brazil, for example, as pointed out by The Economist (2012), has invested US$1.65Bn to send over 100,000 Brazilians to study abroad, at the world’s best universities around the world, specializing in subjects such as biotechnology, ocean science and petroleum engineering, deemed as essential for the nation’s future. Chile has followed a similar policy for students in economics and finance during the last decades, pursuing an active policy favoring doctoral students applications to the world’s best Universities. Both countries seem to be harvesting the results for their investments in talent generation.

Talent risk management supersedes the realm of the firm, becoming a national concern, being most critical in the case of emerging economies where talent pools are not efficient and fully developed, and were—in some cases— it is difficult to attract talented applicants.

This article is the first one, upon our knowledge, to discuss the importance of jointly understanding the determinants of the probability of the employee leaving the company and its importance in the firm. Additionally, it opens an interesting avenue of research; the need to study the best human resources strategies for each intersection of the two graphs. Each particular quadrant intersection has its own best HR practices; this, however, will be the topic of future research.

6. Bibliography


