software industry productivity

material minds

improving productivity

The software industry, long credited for helping other industries improve productivity, is itself enjoying the results of its own increased productivity. Long gone are the days of mindless spending and large losses. The post-bubble era is seeing dramatic increases in productivity for software companies. It looks like the software industry is really maturing. Our little baby is growing up.

- The average revenue per employee has increased from $195,000 in 2003 to $287,000 last year.
- The average Net Income per employee is now $3,700 (which sounds anemic but represents huge improvement over the average net loss of $61,600 per employee back in 2003.)
- 62% of the companies are now profitable versus only 46% back in 2003.
- This increased productivity has increased the average market cap per employee from $600,000 to $1,129,000.

The industry as a whole has also expanded. We looked at last year's financial results for 284 publicly traded software companies in North America, comparing them with a similar study done in 2004 of 342 public North American Software companies. Since both studies are post-bubble, we get comparable results over the time period, unaffected by unusual economic factors.

- Total revenue for these public companies increased by 316% from $113 billion to $470 billion even though the number of companies in the study declined.
- The total number of employees increased by 248% from 447 thousand to 1.6 million.
- The total market value of these firms increased from $654 billion to $1.7 trillion – an increase of 163%
- And best of all, total net income increased by 477% to $75 billion. 2003's total net income of $13.9 billion could all be accounted for by the top three firms.

The story behind this growth in revenue and profits is one of productivity. Companies in the software industry have figured out how to drive greater revenue per employee along with reduced expenses per employee and that is being translated into much greater levels of profitability.

productivity drives profit and value

Improved productivity, measured in revenue per employee is driving improved profitability and market value. The following chart tells the whole story, Average revenue per employee is now $287 thousand and this has brought average net income above the break-even point. This chart shows the average and median levels of revenue, net income and market cap per employee. It also shows the net income and market cap results for companies whose revenue per employee falls into each quartile.

While firms in the middle two quartiles are still not very profitable, this chart shows the strong link between revenue per employee, and the resulting net income per employee and market cap per employee. In essence, firms that were more productive in their ability to drive revenue per employee ended up with better profitability and market value.

Per Employee	Revenue	Net Income	Market Cap
Average	287,192	3,737	1,129,427
Median	231,617	7,384	585,405
Top Quartile average	560,234	51,367	1,866,154
2nd Quartile average	274,804	4,398	1,215,784
3rd Quartile average	197,142	3,519	759,745
Bottom Quartile average	112,744	-45,007	665,648

Results for 2011-2012 were obtained from Google Finance in February of 2013. They represent full year results for the last fiscal year for 284 public North American Software companies. The last fiscal year would be for calendar 2011 up to October 2012.

where do you fit?

The following chart shows results for every decile in the study and will enable software companies to evaluate their own results as well as set objectives for future growth that will be in line with industry norms.

2011 - 2012		
Per Employee	**Revenue**	**Net Income**
Average	287,192	3,737
Median	231,617	7,384
Highest Firm	1,474,000	309,693
90% scored less than	540,774	71,388
80% scored less than	368,252	45,743
70% scored less than	305,676	27,487
60% scored less than	263,167	14,383
50% scored less than	231,617	7,384
40% scored less than	205,551	1,931
30% scored less than	181,737	-6,797
20% scored less than	147,587	-30,734
10% scored less than	109,361	-64,822
Lowest firm	12,222	-557,778

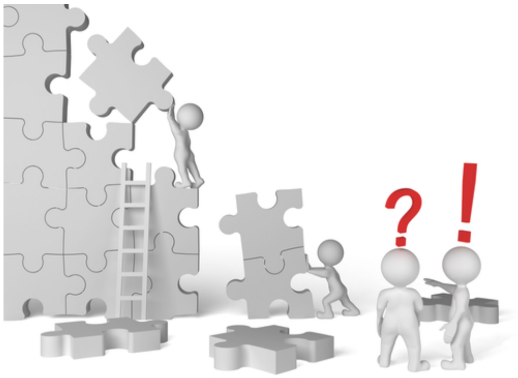
return on people

Chances are, if you're the CEO of a company, you look around from time to time and wonder about all the people you have working for you.

- Do you really need that many people?
- Are they the right people?
- Are they all doing things that are really necessary?
- Are they working effectively?

You probably spend a lot of time trying to figure out how to increase productivity.

In an asset rich environment a company's objective is to improve Return on Investment (ROI). In the knowledge economy a company's objective should be to improve Return on People (ROP). ROP is a new way to measure productivity.



Superior teams, those that are one standard deviation above the mean in production, outperform average teams by 30 percent.

Research on this topic is pervasive and conclusive. If you want better corporate performance, developing your organization, your leaders and your employees is essential to improving your Return on People and thus your productivity.

In the Knowledge Economy your investment is in your people. How then do you go about measuring and improving your Return on People, your ROP?

measuring return on people

The purpose of the ROP concept is to provide a measure that will enable a company to focus on improving the effectiveness of its key resource, that of people, and thus improve productivity.

In the Knowledge Economy your investment is in your people. Unfortunately though, those people are accounted for as an expense and many companies have not attempted to measure and then manage the return they get from those people. Companies often measure revenue per employee, as this study has, but this number is quite often misleading because it includes costs of physical items that are resold or rented out.

The first step is to separate items that are resold from the value that you add when you resell them. If you sell or rent out (SAS) other tangible goods then subtract the amount you paid to purchase these items from revenue. This calculation will show how much value your people add to your products or services. Since the whole purpose of your business is to add value then this a pure number that you'll need to track.

Value Added = Revenue – Cost of tangible goods resold

The next step is simply to calculate the amount you pay your employees before benefits and other intangibles. These are your Personnel Costs.

Personnel Costs = Amounts paid to employees

To calculate Return on People, you simply divide the Value they add by the costs of your people.

ROP = Value Added / Personnel Costs

This very simple equation will give you a percentage that shows the amount of value added by employees in relation to the cost of adding the value. You should measure and report on this number regularly and compare your progress over time. You can also examine how various parts of your organization add value by separating out their value added from that of other parts of the organization.

improving return on people

In order to improve your Return on People, you will need to do three things: Develop and deploy a company wide metrics program, keep people focused on their goals and metrics through performance management, and improve employee engagement through leadership development.

1. Metrics

Instituting a company wide metrics program helps to align strategy to the daily action of all employees. A company needs to have a full set of input and outcome metrics that **translate the strategic plan into actionable measures** for each employee. Goals also need to be established around each of these metrics.

According to a study done by WorldatWork and Sibson Consulting in 2007 entitled "The State of Performance Management", only half of 550 people they surveyed reported that their organization used any kind of goal setting in their performance management process. Even worse than that, only half of them used any quantitative measure. For those that actually set goals:

- For senior managers, goals are completely or largely aligned to the company strategy in 70% of cases.
- For middle managers that number falls to 45%.
- For frontline employees, only 17% have goals that integrate with the strategic plan

2. Performance Management

An effective performance management process helps a company by improving individual performance, deselecting marginal performers, reducing turnover, and creating engaged employees. It keeps people focused on their goals on a monthly basis. This is not just a performance appraisal process but also an ongoing monthly evaluation of goals and results.

According again to WorldatWork, fewer than half of their survey respondents saw their performance management system as helping the organization achieve its strategic objectives.

- 66% identified that reward distribution was a key objective.
- 54% thought that greater individual accountability was a key objective.
- Only 46% selected talent development as a key goal.

3. Leadership Development

A comprehensive leadership development and employee skills training program helps employees develop the behaviors and skills necessary to successfully implement the company's strategic plan. It furthermore develops leaders who can engage employees and as all the research on the subject shows, engaged employees produce superior results.

Development Dimensions International found that "organizations with the highest quality leaders were 13 times more likely to outperform their competition in key bottom-line metrics such as financial performance, quality of products and services, employee engagement, and customer satisfaction."

Development Dimensions International has also determined that:

- **Only 50% of leaders are effective in critical skills**
- **Only 38% of companies have high quality leadership**
- **Only 18% of companies have strong bench strength**
- **Only 31% have effective leadership selection**

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We offer a suite of consulting, training, and coaching services designed to improve employee productivity and Return on People. Our programs help you develop and manage metrics that ultimately improve your employees' performance and increase the value of your company.

Our training and coaching programs improve employee engagement by turning managers into leaders. We combine digital media with articles, videos, exercises along with workshops and team coaching to ensure that your people learn, remember and apply the learning in your company.

We're helping improve Return on People

We believe that if you don't measure it, you can't manage it and so we use a host of measurement techniques to determine whether our programs are effective.

Improve your company's Return on People.

Contact us today to learn about our innovative and cost effective programs.

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