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The spiral of downsizing: Conceptual insights on organizational impact

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Abstract

The long-term effects of downsizing, as well as the specific impacts of repeated downsizing, remain an area of limited understanding within the existing body of research. This gap is primarily due to the relatively small number of empirical studies conducted on the subject and the often-conflicting findings these studies present. To address this issue, this article systematically reviews the three predominant theoretical perspectives identified in the downsizing literature: economic efficiency, psychological contract theory, and organizational resilience. Through this analysis, the article establishes that downsizing exerts significant long-term consequences for both employees and organizations. Furthermore, the findings highlight that the nature of the downsizing experience—whether it involves direct layoffs, indirect exposure, or structural reorganization—and the sequence in which these events occur play a pivotal role in shaping the outcomes of repeated downsizing. Additionally, the research underscores that employee susceptibility to or recovery from repeated downsizing events is influenced by the specific outcome being examined, such as job performance, emotional well-being, or organizational loyalty. These insights not only enrich the conceptual understanding of downsizing phenomena but also underscore the need for more nuanced, longitudinal studies to unravel the complexities of repeated downsizing in diverse organizational contexts.

Keywords: Downsizing, Repeat downsizing, Organizational impact, Long-term effects.

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1. Introduction

The lack of a dominant paradigm in downsizing literature underscores a field characterized by persistent disagreement on foundational questions—most notably, whether downsizing yields net positive or negative outcomes for organizations and their employees [1, 2]. Competing theoretical frameworks have emerged to explain the complex effects of downsizing, including the institutional perspective (De Meuse, et al. [3]), the well-being perspective [4-6], and the psychological contract theory [7]. While this diversity of perspectives enriches the academic discourse, it simultaneously limits the development of a unified framework that could provide actionable insights for practitioners. The fragmented nature of the field reflects the complexity and multifaceted nature of downsizing, but it also poses significant challenges for organizations seeking to mitigate its negative consequences while leveraging potential benefits.

One of the most contentious debates in the downsizing literature concerns the long-term effects on both organizations and their employees, as well as the compounded impact of repeated downsizing events [8, 9]. The global economic downturn of the early 21st century forced companies worldwide to adopt workforce reductions as a survival strategy. Between 2006 and 2010, the U.S. Bureau of Labor Statistics recorded over 36,000 downsizing events affecting approximately 64.5 million workers. Similarly, the UK experienced a sharp rise in unemployment from 5% in 2006 to 8% in 2010, with the redundancy rate peaking at 15 per 1,000 employees in 2009 [10]. Alarmingly, research indicates that organizations that have downsized once are over 65% more likely to downsize again within the next year compared to those that have never downsized [11]. These patterns make it imperative to assess not only the immediate consequences of downsizing but also its prolonged and cumulative impacts to fully understand its true costs, risks, and benefits.

Three primary theoretical paradigms dominate the discourse on the long-term and repeat effects of downsizing [1]. The rational paradigm, rooted in economic theory, focuses on the risks and benefits of reducing costs and streamlining operations [3] . Psychological contract theory examines the negative consequences of downsizing on individuals, emphasizing the breach of organizational promises and employee expectations [7]. Meanwhile, the well-being perspective explores the physical and mental health implications of downsizing through the lens of stress resilience and vulnerability [4-6]. These paradigms collectively provide a nuanced understanding of downsizing but also highlight significant gaps in knowledge, particularly in understanding the dynamics of repeat downsizing and its intersection with employee vulnerability, organizational performance, and long-term sustainability.

Building on the foundational work of Arzuaga, et al. [8], this article synthesizes insights from existing theoretical frameworks to identify critical gaps and prioritize areas for future empirical inquiry. It provides a rigorous evaluation of the strengths and limitations inherent in prevailing perspectives, addressing unresolved challenges in the field, including the cumulative and multifaceted impact of repeated downsizing events on organizational and individual outcomes. By advancing this analysis, the article seeks to enhance the theoretical understanding of downsizing phenomena and offer actionable strategies for practitioners. In doing so, it aims to bridge the gap between theoretical constructs and practical applications, contributing to a more nuanced and evidence-based approach for managing the complex and far-reaching implications of downsizing in contemporary organizational contexts.

1.1. Perspective #1 - Economic

The extant literature on the effects of repeated downsizing and its long-term impact on economic indicators reveals two dominant assumptions. First, downsizing is often interpreted as a signal of financial instability, with repeated downsizing exacerbating negative stock reactions and other financial metrics [12-14]. Second, some theorists argue that downsizing can function as a continuous improvement process, enabling better planning and operational alignment through iterative learning from previous waves [14-16].

Empirical studies offer mixed insights. For example, an analysis of Fortune 500 companies from 2008 to 2015 found no significant differences in ROE, EBITDA, or other financial indicators between frequent and infrequent downsizers, though firms that downsized repeatedly exhibited worse profitability ratios and market valuations [12]. Importantly, companies that downsized during economic downturns, such as the 2008 crisis, were more likely to downsize again, underscoring the prevalence of repeat downsizing once initiated [17].

Carriger [12] supports the signaling theory, which posits that downsizing sends negative signals to the market, and the "band-aid theory," which suggests that downsizing addresses symptoms rather than underlying strategic or financial issues. While downsizing may offer short-term relief, its long-term efficacy remains questionable. For instance, while some studies (e.g., [18, 19]) found negligible short-term effects on financial performance, a 12-year longitudinal study by De Meuse, et al. [3] revealed that downsizing firms exhibited worse profitability indicators for five years post-downsizing, although these differences faded over time.

Arzuaga, et al. [8] contend that serial downsizers—firms engaging in three or more downsizing events within an eight-year span—generally performed worse than firms with fewer downsizing events. Furthermore, the magnitude of workforce reductions mattered: companies that downsized over 10% of their workforce were consistently outperformed by those implementing smaller-scale reductions. This suggests that while downsizing may stabilize performance temporarily, excessive or repeated downsizing undermines long-term organizational health.

Contrary to the argument that repeat downsizing facilitates organizational learning, studies like Gilson, et al. [14] challenge this view. Their analysis of 67 firms undergoing multiple downsizing waves found no evidence of improved performance from iterative learning. Instead, they observed persistent negative consequences, including deteriorating employee outcomes and diminished financial indicators. These findings suggest that organizations often replicate flawed strategies rather than refining practices, exacerbating negative outcomes over time.

Similarly, Beixin and Zu-Hsu [20] argue that repeat downsizing sends a damaging market signal, raising doubts about a firm's survival prospects. Their research highlights the association between frequent restructuring, large-scale layoffs, and heightened organizational failure risk. While Lin and Yang [16] found that analysts tend to offer favorable forecasts for repeat downsizers due to perceived operational improvements, this optimism contrasts sharply with evidence suggesting that repeat downsizing seldom delivers sustained benefits.

Overall, the evidence indicates that while the long-term financial effects of single downsizing events may stabilize, repeated downsizing rarely fosters recalibration or improvement (Gandolfi [21]). Instead, it amplifies negative outcomes, with firms showing diminished performance and weakened employee morale. The normalization of repeat downsizing within some organizations reflects its institutionalization rather than its efficacy as a strategic tool, underscoring the need for a more nuanced understanding of its economic and human costs [1, 2].

1.2. Perspective #2 - Psychological Contract

The long-term effects of downsizing and repeat downsizing on the psychological contract, as well as employees' attitudes and behaviors, remain insufficiently understood. Existing literature consistently identifies downsizing as a significant source of psychological contract breach and violation, disrupting perceived obligations between employees and organizations [7, 22, 23]. These breaches arise as downsizing undermines the continuation of the employment relationship, truncates intrinsic outcomes, and forces employees to reconstruct their understanding of the work environment. Such disruptions are profoundly unsettling, frequently leading to negative emotions and attitudes [9, 24].

Repeated exposure to downsizing amplifies these challenges. Armstrong-Stassen [25] found that employees with repeated exposure to layoffs, particularly male technicians, reported heightened perceptions of distributive injustice and job insecurity. These employees employed more active coping strategies, such as positive thinking and direct action, compared to those with less exposure. However, repeat exposure also fostered stronger perceptions of unfair targeting, suggesting that cumulative downsizing events exacerbate feelings of inequity and mistrust. Similarly, Grunberg, et al. [26] observed significant negative effects of layoffs on organizational commitment that persisted for at least two years, while Amabile and Conti [27] highlighted that downsizing undermines creativity for up to two years post-event. In extreme cases, repeated downsizing has been linked to increased sabotage, fraud, and embezzlement Gandolfi [13] underscoring the potential for profound disruptions in employee behavior [28].

Despite these negative outcomes, the evolution of work relations over recent decades has reshaped the psychological contract. The rise of job insecurity and short-termism has normalized breaches that were previously perceived as contract violations [23, 29]. As long-term employment security has diminished, employees have shifted their expectations toward other organizational offerings, such as opportunities for skill development and employability [30, 31]. This shift suggests that employee reactions to downsizing may be less negative in the long term than previously assumed, as downsizing becomes an accepted reality of modern employment.

Indeed, several studies indicate that the immediate negative effects of downsizing on employee attitudes and behaviors often diminish over time. For example, declines in work environment freedom, supervisory support, and trust among workgroups tend to recover in the years following downsizing events Amabile and Conti [27]; Luthans and Sommer [32] and Armstrong-Stassen [33]. Armstrong-Stassen, et al. [34] even found evidence of improved performance among employees in downsized departments compared to those in unaffected departments, highlighting the potential for resilience and recovery post-downsizing.

However, the relationship between downsizing, repeat downsizing, and long-term employee outcomes is far from uniform. Contextual factors such as downsizing designation (victim vs. survivor) and individual characteristics like organizational involvement significantly influence outcomes. For example, Armstrong-Stassen [33] observed that survivors who were initially designated redundant but retained experienced a decline in commitment shortly after downsizing but displayed increased commitment over time, eventually surpassing the commitment levels of non-redundant survivors. Conversely, Allen, et al. [35] reported sustained declines in organizational commitment, job involvement, and emotional energy among employees post-downsizing. Interestingly, satisfaction with top management and perceptions of job security improved after an initial decline, suggesting a nuanced recovery process influenced by management actions and individual adaptability.

These findings emphasize that the long-term effects of downsizing are highly contingent and multidimensional. While many negative effects dissipate over time, some attitudes and behaviors—such as organizational commitment and emotional investment—remain negatively affected in the long term. Allen, et al. [35] suggest that organizations can mitigate these effects by reinforcing desirable aspects of the evolving psychological contract, such as opportunities for advancement, social status, and a sense of security. Following perceived contract violations in the context of downsizing, employees may seek alternative reasons to remain engaged and committed to the organization. Strategic reinforcement of these elements can help organizations manage employee attitudes and promote recovery after downsizing events.

1.3. Perspective #3 –Well-Being

One of the most debated issues in downsizing research is whether repeated exposure to downsizing builds resilience in employees or exacerbates vulnerability to its effects. Underlying this debate are several core assumptions: (a) downsizing acts as a stressor impacting physiological and psychological well-being, (b) prior exposure to downsizing shapes subsequent reactions, and (c) downsizing's effects persist long after the events. Given the prevalence of repeated downsizing, understanding its long-term impact and the interaction between multiple downsizing events is crucial.

The well-being perspective frames downsizing as a threat that can have direct or indirect effects on employees, depending on their proximity to the layoffs (Grunberg, et al. [36] and Engidaw, et al. [37]) and the characteristics of the downsizing event, such as its magnitude and frequency [5, 38]. Within the stress resilience/vulnerability framework, Dougall, et al. [39] argue that the similarity of stressor events determines whether resilience or chronic stress develops. They suggest that only similar stressors allow individuals to adapt and build resilience, whereas varying types of stressors heighten stress and vulnerability.

The negative impact of downsizing on personal networks within organizations further exacerbates vulnerability among survivors. The elimination of employees weakens communication, social exchange and friendship links such that survivors feel additional stress because of their proximity to downsizing victims Moore, et al. [40] and the feelings of isolation and diminished emotional support available when victims leave the organization.

Empirical evidence overwhelmingly supports the vulnerability perspective, with repeated downsizing contact associated with worsening employee outcomes. For example, Ferrie, et al. [4] found that chronic job insecurity from downsizing led to adverse health effects, particularly self-reported measures like depression, even when physiological indicators showed limited changes. Moore, et al. [5] observed that employees exposed to multiple downsizing waves, especially direct layoffs, experienced significant declines in health, attitudes, and behaviors. Mixed contacts (direct and indirect) further exacerbated these effects, underscoring that the nature and order of exposure play critical roles. Similarly, Armstrong-Stassen [41] found that managers with repeated layoff experiences reported diminished affective commitment and increased continuance commitment, suggesting they stayed out of necessity rather than loyalty. She concluded that the psychological damage from the initial downsizing event was so significant that subsequent experiences had a limited incremental impact.

Moore, et al. [6] further explored the temporal and sequential effects of downsizing. Their findings revealed that recent layoffs had a greater influence on outcomes like job security, depression, and intention to leave than past experiences. Notably, employees who initially experienced indirect layoffs and later faced direct layoffs reported worse outcomes compared to those with two direct exposures, suggesting that dissimilar layoff experiences intensify stress and hinder resilience.

While the vulnerability perspective dominates, there is some evidence for a resilience effect under specific conditions. Armstrong-Stassen [25] found that employees with greater exposure to downsizing demonstrated stronger action-oriented coping and positive thinking. Kalimo, et al. [42] identified that the type of downsizing event—such as layoffs versus cutting temporary contracts—shaped employee reactions. They noted that while past downsizing experiences had limited impact on survivor well-being, repeated or anticipated downsizing activities increased emotional exhaustion, cynicism, and psychological distress.

The long-term effects of downsizing are complex and vary depending on the outcome measured. Emotional exhaustion and general health are highly sensitive to downsizing exposure, whereas organizational commitment, intention to leave, and satisfaction with management often return to baseline levels over time [35, 42, 43]. These findings highlight the importance of considering individual and contextual factors, such as the type, frequency, and order of downsizing events, when evaluating its long-term impact.

In summary, the evidence suggests that repeated downsizing exacerbates employee vulnerability more often than it fosters resilience. The mixed outcomes underscore the nuanced nature of downsizing effects, with some employees adapting while others experience lasting negative consequences. Organizations should prioritize strategies to mitigate the psychological and health impacts of downsizing and foster a supportive environment to reduce its detrimental effects over time.

2. Implications for Theory and Practice

Literature on the long-term effects of downsizing and repeated downsizing was initially dominated by economic perspectives [1]. More recently, the incorporation of psychological contract and well-being perspectives has provided a more comprehensive understanding of the phenomenon [37]. While financial metrics are critical, they fail to capture intangible losses such as diminished corporate reputation, erosion of organizational knowledge, skill depletion, reduced creativity and innovation, and declines in employee commitment and morale [44]. A holistic assessment of downsizing effectiveness must therefore integrate both financial and non-financial outcomes [1, 45].

3. Emerging Themes in Downsizing Research

The three dominant strands of downsizing literature—economic, psychological, and well-being perspectives—reveal two key insights. First, downsizing has enduring impacts on organizations and employees, necessitating consideration of both short-term and long-term outcomes when evaluating its efficacy. The cascading effects of repeated downsizing waves, now commonplace in modern organizations, underscore the importance of understanding their cumulative impact on employee attitudes and behaviors. Second, downsizing outcomes are highly contingent on a range of factors, including downsizing methods, strategy, and employee experiences. Methods such as layoffs, non-renewals, and unfilled vacancies result in distinct long-term effects, with proactive downsizing strategies producing different outcomes compared to reactive ones [46, 47].

The nature of downsizing contact (e.g., direct vs. indirect exposure) and the order of exposure further influence the duration and magnitude of its effects. For instance, employees directly affected by layoffs report greater psychological trauma than those indirectly exposed. Moreover, the similarity between downsizing events determines whether employees develop resilience or heightened vulnerability [39]. Repeated exposures with varying characteristics—such as transitioning from indirect to direct contact—often intensify stress and hinder adaptive responses [6].

4. Complexity and Heterogeneity of Outcomes

Research consistently demonstrates that the effects of downsizing are neither homogeneous nor universally predictable. Some outcomes, such as emotional exhaustion and general health, are particularly sensitive to downsizing, while others, like organizational commitment and satisfaction with management, often return to baseline levels over time [35, 43]. This variability suggests that a single "resilience or vulnerability" model is inadequate. Instead, downsizing's impact depends on the specific outcomes analyzed and contextual factors such as industry, organizational function, and cultural context [42].

Despite advances, significant gaps remain. The overrepresentation of layoffs in downsizing research limits understanding of other methods, such as attrition or role elimination, which may yield different effects. Additionally, existing research disproportionately focuses on single national contexts, often overlooking the interaction between country-specific factors and downsizing outcomes. Expanding research to multinational environments and diverse industries, including knowledge work and the gig economy, is essential to capture the complex dynamics of downsizing.

5. The Psychological Contract and Repeat Downsizing

Efforts to differentiate the effects of downsizing contact types Grunberg, et al. [36] and survivor categories [5, 6]. Have enhanced understanding. However, the concept of "indirect contact" remains overly subjective and challenging to operationalize in practice. For instance, managers may struggle to distinguish between employees whose "friends or close colleagues" were downsized versus those whose connections were not. Arzuaga and Gandolfi [1] address this limitation by introducing a contextual proximity perspective, which accounts for similarities between employees' environments and those targeted for downsizing. This approach eliminates subjectivity and enables the application of segmentation strategies throughout the downsizing process.

Another gap lies in the lack of multilevel analysis. Most studies focus on strategic-level decisions or individual-level outcomes without bridging the two (Arzuaga, et al. [8]; Brauer and Vandepoele [48]). Sahdev [49] linked downsizing strategies, implementation, and employee perceptions, demonstrating that factors such as downsizing frequency and control significantly influence individual outcomes like perceived job insecurity and autonomy. This line of inquiry should be expanded to align strategic decision-making with effective survivor management.

6. Concluding Thoughts

Despite its limitations, the downsizing literature offers several important conclusions:

1. Enduring Effects: Downsizing constitutes a significant psychological shock with effects that persist for years after the event. This "legacy effect" suggests that downsizing remains a salient factor in employees' psychological field long after its occurrence [48, 50-52].
2. Recency Dominance: In cases of repeated downsizing, the most recent exposure often overrides previous experiences. This implies that the immediacy and salience of recent events place greater demands on employees' psychological and physiological resources [37].
3. Mixed Outcomes: Combined past and recent downsizing exposures yield mixed effects. Psychological outcomes, such as stress and job insecurity, often worsen with repeated exposures, while some organizationally desirable attitudes, such as satisfaction with management, may recover to pre-downsizing levels over time [9].
4. The "New" Psychological Contract: Although some authors argue that a new psychological contract, emphasizing adaptability and employability, has made employees more resilient to downsizing [7, 29], empirical evidence supporting this claim is limited. In practice, negative outcomes remain prevalent [53].

7. Future Research Directions

Despite the prevalence of repeat downsizing, it is a field that has received limited attention from the academic community. Future studies should endeavor to explore whether the effects discussed above still apply, considering today's rapidly changing workforce where job hopping and frequent downsizing have become normalized. The gig economy, flexible work agreements, and zero-hour contracts have altered the job security paradigm, changing the terms of the psychological contract. Similarly, the increased prevalence of quiet quitting (Arzuaga, et al. [54]) and reduced employee engagement at work (Wilson Fadiji and Lomas [55]) may influence the effect of repeat exposure to downsizing.

Other priorities in the field of repeat downsizing include the exploration of alternative downsizing methods, multinational contexts, and diverse industry settings to provide a richer understanding of downsizing dynamics. Greater attention to multilevel analyses and segmentation strategies, such as contextual proximity, can bridge the gap between organizational strategy and individual-level outcomes. By integrating these perspectives, researchers can develop a more nuanced and actionable framework for managing the complex consequences of downsizing.

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