Looking for Answers in All the Wrong Places

Today's human resources leaders face mounting pressure to demonstrate the economic value of HR programs and practices. For many, this proves challenging because they are stuck with outdated, inadequate methods of measurement that are remnants of the "cost center" era of HR management. If HR professionals want to step into the role of strategic partner, they must take bold, new steps to quantify the impact of people-management practices on business results.

Typically, business strategies are based on some form of differentiation. Companies seek to distinguish themselves and deliver value in ways their competitors can’t. Why, then, do these same companies become "copycats" when it comes to developing a human capital strategy to support their unique business strategy?

For the past two decades, HR professionals have relied primarily on external benchmarking and "best practices" to drive their HR strategies. While these tools can play a valuable role in program design, they have no place in strategy development. Companies take a big risk when they rely solely on the successes of others. Take the example of a computer-chip maker that discovered the perils of creating a human capital strategy based on external benchmarking. Historically, the company held a solid position in its industry as an efficient, reliable, low-cost chip manufacturer. Therefore, its work force consisted primarily of experienced engineers who:

• Knew the company’s library of chips and other possible applications
• Forged strong relationships with customers
• Understood the company’s established sales, design and manufacturing processes.

But, after a benchmarking study, the chip maker started mimicking the HR practices of recognized industry leaders — firms that made their money through innovation, not efficient process engineering. The company focused on hiring the "best and brightest" at premium pay, even though the work could hardly be challenging to top-flight engineers. Generous stock options were infused deep into the organization, even though the company’s stringent "command and control" management...
system — designed to ensure process efficiency — precluded the type of entrepreneurial and risk-taking activity that could make such rewards pay off. These “best practices” simply didn’t fit this organization’s business strategy or management style.

The result? Inflated labor costs, declining quality, lower profits and disenfranchised experienced employees who fled in droves. New recruits left, too, because the work didn’t suit their desire to be innovators.

By definition, human capital is an asset. It is the cumulative experience, capabilities and know-how that make up the work force and give rise to productive labor flow. HR’s role, therefore, is a form of asset management. At a minimum, it requires that organizations answer two questions:

• Do we have the right “profile” of human capital assets to deliver on our business strategy?
• Are we managing these human capital assets in a way that optimizes their economic productivity?

The answers form the basis of each organization’s unique human capital strategy. But, while there is growing recognition that an organization can gain competitive advantage through the effective management of its people, there has been little resulting action in this direction. As a result, today’s organizations can measure the costs and returns on their physical and financial capital, but in most cases can’t measure their return on human capital.

How to Change the Situation
First, one needs to understand the people implications of the organization’s unique business design. Get clarity around what the work force needs to become, and then build a blueprint of the capabilities and actions that will create this ideal work force.

Next, new information is needed to forge the critical connection between business and human capital strategies and ensure that practices are aligned and mutually reinforcing. Also, employers need to realize that many of these answers lie inside the organization, not just outside, as benchmarking and best practices have led many to believe.

It’s time to turn the lens inward. Careful examination and analysis of your own employee and performance data produces critical facts and insights about your own work force that lead to smart decision-making and the development of a unique and powerful human capital strategy. Analysis of these data can reveal such critical facts about your work force as:

• Who gets hired
• Who stays and leaves
• Who advances
• Which work force characteristics and behaviors actually are rewarded
• How rewards are distributed
• How talent is developed (e.g., both through formal training and on-the-job learning)
• How new hires perform compared to homegrown talent
• How vulnerable your organization is to changing labor market conditions.

Made possible through recent advances in enterprise software and HRIS technology, this type of disciplined, sophisticated analysis can help identify which human capital factors drive business performance in an organization and which combination of people practices are most likely to optimize value.

Moreover, organizations can measure and anticipate the outcome of specific HR interventions in hard, quantitative terms. They often can answer specific questions such as:

• How broadly should incentives be distributed?
• How long should managers cycle through positions?
• What is the real cost of turnover and what’s the most efficient way to reduce it?
• Do we have the right mix of pay, benefits and career opportunities to attract the right people?
• Is our rewards program doing what it was intended to do?
• If we enact this new training program, how will it likely affect customer service, innovation, turnover, performance, market share and, ultimately, profits?
• What return is the company getting on its investments in human capital?
• Can smarter investments be made?

A successful financial services company recently applied these new approaches. The company determined through market research that customer service quality was the foundation of its competitive position. Achieving targeted growth rates would depend both on acquiring new customers and retaining existing customer relationships.

The company wanted to determine which work force attributes and people practices most contributed to its ability to retain customers and grow market share. Company leaders, accustomed to making data-driven decisions in other areas, knew that credible answers to these questions could not come from conventional benchmarking or best-practice approaches.

The company conducted extensive quantitative analysis using several years
of employee, financial and customer data. The most significant finding was that, all else being equal, locations with the most tenured work force performed best across key customer and financial measures (e.g., customer retention, growth of high-end premium accounts, net income, market share). Millions of dollars could be netted for each year of additional average tenure in the branches, achieved either through lower turnover or more strategic staffing. Expanding incentive opportunities to lower-level employees also had a significant, positive effect on the same measures.

With this new information, the company faced a serious challenge: In an effort to expand its services, the company had been intensively hiring employees with new skills and experiences. In the tight labor market of the 1990s, this meant paying top dollar. As a result, the balance of rewards tipped in favor of the newer employees with general market experience and skills, instead of favoring longer-service employees with the firm- and customer-specific experience and knowledge proven to be key value drivers. Not surprisingly, experienced employees left the company at increasing rates. Inadvertently, the company was undermining its core human capital assets. Could loss of customers be far behind?

The company quickly addressed the imbalances and enhanced the people practices that drive results. That meant focusing on career development and rewards. Specifically, the company began taking steps to:

- Ensure that high performers had a clear path for growth (and longevity)
- Increase variable pay opportunities
- Invest more in training to broaden the capabilities of the existing work force.

Most importantly, the company institutionalized ongoing measurement of human capital assets and practices. Now HR applies as much rigor to understanding work force needs and characteristics as marketing applies to understanding customers. It’s a claim that few organizations can make.

For HR professionals to take advantage of these new approaches to human capital measurement, they need to get comfortable with the notion that context is everything. For many, benchmarking and best practices are familiar tools that offer seemingly silver-bullet solutions. There is great comfort in saying, “Well, G.E. did it,” especially for those who are risk-averse. HR professionals need to accept that “It depends” is the right answer to many human capital questions. The right solutions depend on the company’s unique context: the business environment and strategy, and internal operations.

You can’t simply infer from the experiences of the financial services organization described earlier that all banks should design their rewards program to increase tenure. It all depends on how the organization competes. Other firms — even similar financial services companies — will have different and unique value drivers. For all the talk about “high-performing work systems” and other best-practice models, there simply is no one-size-fits-all solution to human capital strategy.

It comes down to using the right tools in the right places at the right time. Because it is possible to learn from the experiences of others, benchmarking and best practices can be valuable in the actual design of specific programs and practices, but only after a broader strategic blueprint is in place.

If HR professionals are ready to look beyond traditional benchmarking and bring true depth and rigor to the creation and oversight of their human capital strategies, they will see a positive effect on business results and a place for them at the executive table.

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