

## Chapter 2

# Human Resources Strategy and Planning

### Learning Objectives

After students have read this chapter, they should be able to:

- Summarize the organization's strategic planning process.
- Explain the key differences between good and bad strategy and suggest a way to force strategic asset reallocation.
- Outline how HR's strategies are merged with organizational strategies and give two examples.
- Discuss how one forecasts for supply and demand of human resources.
- List options for handling a shortage and surplus of employees.
- Identify how organizations can measure and analyze the effectiveness of HR management practices.

### Chapter Overview

Strategic human resource management refers to the use of employees to gain or maintain a competitive advantage. There should be a close linkage between organizational and HR strategies. This chapter starts with a discussion of organizational strategic planning including strategy formulation, the strategic planning process, strategic competencies for HR professionals, and operationalizing HR management strategies.

Environmental analysis, including both internal and external factors, is presented followed by global competitiveness and strategic HR issues. Next, HR planning activities in mergers and acquisitions, before the deal, during integration, and post integration are discussed. Then some strategic challenges are presented: managing a talent surplus, legal considerations for workforce reductions, and managing a talent shortage.

The chapter closes with measuring effectiveness of HR initiatives. The development and use of HR metrics is explored and specific strategic HR effectiveness tools such as benchmarking, the balanced scorecard, return on investment (ROI), and HR audits are discussed.

## **Chapter Outline**

### **HR Headline: Best Buy Cuts 2400 Jobs in Turnaround Strategy**

Best Buy needed a strategy to combat the “showrooming” of its stores. Showrooming occurs when customers go to Best Buy’s well stocked stores to see, compare, and demonstrate its products, but then leave and purchase the products at a discount or on-line store. The big retailer laid off 600 employees in its technical support division called the “Geek Squad” and 1,800 others as it seeks to improve results. That is about 1.4% of its 167,000 employees.

The company further announced the restructuring in which it would close 50 of its United States big box stores, cut 400 corporate jobs and cut costs by \$800 million to be more price competitive. The company plans to open 100 smaller and more profitable Best Buy mobile stores to go with its (at that time) 1,400 existing locations.

Shortly after the strategy was announced (in an unrelated situation), the CEO of Best Buy abruptly left the company. However, the interim CEO reiterated the company’s commitment to the strategy of fundamentally changing its operations to improve results. A spokesman said that the layoffs are a part of the company’s ongoing turnaround strategy.

The **strategy** an organization follows is its plan for how to compete successfully, survive and grow. Many organizations have a relatively formal process for developing a written strategy encompassing a three- to five-year period with objectives and goals for each unit.

Organizations seek to achieve and maintain a competitive advantage in the marketplace by delivering high-quality products and services to their customers in a way that competitors cannot duplicate. Strategies to do so might include revising existing products, acquiring new businesses, or developing new products or services using existing capabilities.

Different companies in the same industry may have different strategies to succeed. Successful strategic management requires:

- Accurately analyzing the situation the company finds itself in
- Deciding what its goals will be
- Coming up with actions to achieve those goals

## **I. Organizational Strategic Planning**

**Strategic planning** is the process of defining a strategy, or direction, and making decisions on

how to allocate the resources of the organization (capital and people) to pursue this strategy. The strategic plan serves as the roadmap that gives the organization direction and aligns resources.

### **A. Strategy Formulation**

The strategic planning cycle typically covers a three- to five-year time frame, and management considers both internal and external forces when formulating the strategic plan. The guiding force behind the strategic planning process is the **organizational mission**, which is the core reason for the existence of the organization and what makes it unique.

The planning process begins with an assessment of the current state of the business and the environmental forces that may be important during the planning cycle. Analysis of the strengths, weaknesses, opportunities, and threats (SWOT) is a typical starting point because it allows managers to consider both internal and external conditions. The SWOT analysis helps managers to formulate a strategic plan that considers the organization's ability to deal with the situation at hand. The planning process requires continuously monitoring and responding to environmental changes and competitive conditions.

Managers then determine the objectives for the planning cycle and formulate organization-level strategies to accomplish those objectives. The strategic plan is re-evaluated periodically because conditions may change and managers must react to the ever-changing business environment.

### **B. Good versus Bad Strategy**

Many companies are generating strategies that by their own admission are substandard. Bad strategy abounds perhaps because it ignores the difficult path to focusing and making choices among alternatives. Instead of making a choice, a strategy may try to accommodate many conflicting demands and interests. Good strategy must involve an accurate diagnosis of the challenge, an approach to overcome the obstacles, and a focus on coherent actions to make the approach work. It must have focus and choice of a way to proceed.

### **HR Perspective: Forcing Strategic Asset Reallocation**

Different units in the organization can be classified into different categories based on their market opportunity and performance. A unit might be labeled “grow”, “maintain”, or “dispose.” Each category comes with clearly differentiated resource investment guidelines. This removes as much politics as possible and focuses on contribution to the strategic goals of each unit.

When Lee Raymond was CEO of Exxon Mobile, he required that 3 to 5 percent of the company’s assets were to be indicated for disposal each year. The divisions could keep these assets only if they could show a compelling turnaround program for that unit. The burden was on the division to prove the asset should be kept. The net effect was a healthy turnover and an upgrading of units. Such a process can force the reallocation of assets inside the organization and a rethinking of how best to achieve strategic goals.

## **II. Human Resources and Strategy**

Regardless of which specific strategies are adopted for guiding an organization, having the right people will be necessary to make the overall strategies work. Strategic HR management entails providing input for organizational strategic planning and developing specific HR initiatives to help achieve the organizational goals.

Although administrative and legally mandated tasks are important HR’s strategic contribution can also add value to the organization by improving the performance of the business. Some businesses are highly dependent on human capital for a competitive advantage; others are less so. However, every business strategy must be carried out by people, so human capital has always some impact on business success.

**Strategic HR management** refers to the use of human resource management practices to gain or keep a competitive advantage. Talent acquisition, deployment, development, and reward are all strategic HRM approaches that can impact the organizational ability to achieve its strategic objectives.

An important element of strategic HRM is to develop processes in the organization that help align individual employee performance with the organizational strategic objectives. When employees understand the relevant priorities, they can better contribute by applying their skills to advance the strategic goals.

### **A. Requirements for Human Resource Contribution to Strategy**

Specific HR management strategies obviously depend on the strategies and plans of the organization. Figure 2-2 highlights some common areas where HR should develop and implement appropriate strategies. To contribute in the strategic planning process, HR professionals provide their perspective and expertise to managers by performing the following functions:

- *Understand the business*—knowing the financials and key drivers of business success are important to understanding the need for certain strategies.
- *Focus on the key business goals*—programs that have the greatest relevance to business objectives should get priority.
- *Know what to measure*—metrics are a vital part of assessing success, which means picking those measures that directly relate to the business goals.
- *Prepare for the future*—strategic thinking requires preparing for the future, not focusing on the past—except as a predictor of the future

## **B. Human Resources Strategies for Global Competitiveness**

The globalization of business has meant that more organizations now operate across borders with ties to foreign operations, international suppliers, vendors, employees, and other business partners. A global presence can range from importing and exporting to operating as a **multinational corporation (MNC)**. An MNC, sometimes called a “transnational corporation,” is an organization that has facilities and other assets in at least one country other than its home country.

Even organizations that operate primarily in the domestic market face pressure from foreign competitors. The supply chain is increasingly internationally dispersed, and foreign business practices influence operations in the United States. Technology advances have eliminated many barriers to operating on a global scale.

For HR to complement the organization’s strategy it has to consider the route to merging HR’s strategies with those of the company. To effectively compete on an international scale, the organization needs expertise to administer all HR activities in a wide range of nations.

Two international HR areas that are frequently the basis for HR strategies to support the organizational strategy are offshoring and staffing global operations. Both actions require merging organization’s and HR’s strategies.

### **Offshoring Strategy**

Competitive pressure to lower costs has resulted in many jobs being moved overseas in recent years. **Offshoring** is the relocation of a business process or operation by a company from one country to another. Product- and software-development projects are increasingly being offshored because of the lack of science and engineering talent in the United States.

The adoption of a strategy of offshoring should strongly consider two points:

- *Reliability*—has to do with the odds that the offshore vendor can deliver and in a consistent manner.
- *Responsiveness*—has to do with the vendor’s ability to make changes if necessary.

Offshoring decisions require merging organizational level and HR department level strategies as does global staffing.

### **Global Staffing Strategy**

Staffing for global operations includes a wide variety of alternatives. The optimal solution is to combine the expertise of local employees with the organization-specific knowledge of employees from the home country. Some countries require that the organization employ a certain percentage of workers from the host country. Each organization will use a staffing model that best fits its culture and strategic goals.

An expatriate is a citizen of one country who is working in a second country and employed by an organization headquartered in the first country. The return of an expatriate (called repatriation) must be well planned and executed for the organization to continue the benefits of the overseas assignment when the employee comes back.

Leadership development is especially important for MNCs. It is becoming more important for individuals in top management positions to have international experience so that they understand the worldwide marketplace. Leading across cultures requires specific skills, and organizations should provide formal training along with expatriate assignments to develop leaders who can achieve results in this demanding environment.

## **III. Human Resource Planning**

**Human resource planning** is the process of analyzing and identifying the need for and availability of people so that the organization can meet its strategic objectives. The focus of HR planning is to ensure the organization has the *right number of human resources*, with the *right capabilities*, at the *right times*, and in the *right places*.

As part of the analyses, HR plans can include several approaches. Actions may include shifting employees to other jobs in the organization, laying off employees or otherwise cutting back the number of employees, retraining present employees, and/or increasing the number of employees in certain areas. Factors to consider include the current employees' knowledge, skills, and abilities (KSAs) and the expected vacancies resulting from retirements, promotions, transfers, and discharges.

### **A. Human Resources Planning Process**

The steps in the HR planning process are shown in Figure 2-4. The process begins with considering the organizational plans and the environmental analysis that went into them. This includes an environmental analysis to identify the situation in which HR is operating. Strengths, weaknesses, opportunities, and threats are considered. Then the possible *available workforce* is evaluated by identifying both the external and internal workforce.

Once those assessments are complete, forecasts must be developed to identify both the demand for and supply of human resources. Management then formulates HR staffing plans and actions to address imbalances, both short-term and long-term. Specific strategies may be developed to fill vacancies or deal with surplus employees.

Finally, HR plans are developed to provide specific direction for the management of HR activities related to employee recruiting, selection, and retention. The most telling evidence of successful HR planning is a consistent alignment of the availabilities and capabilities of human resources with the needs of the organization over time.

### **B. Environmental Analysis**

Before the managers in an organization begin strategic planning, they study and assess the dynamics of the environment in which they operate to better understand how these conditions might affect their plans. The process of **environmental scanning** helps to pinpoint strengths, weaknesses, opportunities, and threats that the organization will face during the planning horizon.

The external environment includes many economic, political, and competitive forces that will shape the future. The internal environment includes the quality and quantity of talent, the organizational culture, and the talent pipeline and leadership bench strength.

Opportunities and threats emerge from the external environment and can impact the outcomes for the organization. Many of these forces are not within the organization's control, but must

be considered in the scanning process because they can affect the business. The external environmental scan includes an assessment of economic conditions, legislative/political influences, demographic changes, and geographic and competitive issues.

Population shifts and demographic changes can affect the organizational strategy. Where an organization locates its operations plays a role in how well it will perform. An understanding of geographic advantages and disadvantages can help managers develop appropriate plans. The strengths and weaknesses of the organization represent internal factors that either create or destroy value. When assessing the internal environment, managers evaluate the quantity and quality of human resources, HR practices, and the organizational culture.

The strength of the talent pipeline is a particularly important internal consideration as the organization plans its HR future. Fulfilling strategic objectives is impossible without sufficient skills and talent. Leadership development and succession planning programs ensure that high-quality talent will be available to carry out the strategy. **Succession planning** is the process of identifying a plan for the orderly replacement of key employees.

### **HR Perspective: Where Is the Workforce?**

Mexico's SIGMA Alimentos made a \$63 million investment in Oklahoma to make hot dogs and hams but cannot find the workforce it needs even with high unemployment. The company got millions of dollars in tax incentives to build a factory near downtown Seminole, a small town with many boarded up and abandoned buildings.

The community was hungry for jobs (10% unemployment) but that hasn't meant that people want to work at Sigma. Turnover at the plant has topped 100% for its first years. A team leader on the ham line says he has gone through 20 workers in a year and a half on shifts that require 5 employees. They complain about the hours emphasizing that they want 9 to 5 jobs in an industry that works shifts that start as early as 4 a.m.

Pay is an issue too—nearly a dozen tribal casinos offer \$9.50 to \$16 an hour for lighter work. Other work is available with a little driving to Oklahoma City to the west. Some do not like working in refrigerated rooms and the constant smell of animal flesh.

Economists say it is natural that workers might prefer service work with better working conditions. A local economic development group spokesman said he would be surprised to see people unwilling to take a \$10/hour job at a meat packing plant. But he would not be surprised to see high turnover—especially if you once worked at one of the sewing plants that left the area. Job creation and securing a workforce even in an area with high unemployment can be challenging.

## **IV. Planning for External Workforce Availability**

When an organization plans to expand its services, it must also identify how many and what types of new employees will be needed to staff the expanded services, locations, and facilities. Those new employees will probably have to come from outside the current pool of employees. Several specific factors affect that external pool of potential employees.

### **A. Economic and Governmental Factors**

The general cycles of economic recession and economic boom in different businesses affect HR planning. Factors such as interest rates, inflation, and economic decline or growth affect the availability of workers and should be considered when organizational and HR plans and objectives are formulated. An organization must consider a wide variety of economic factors and government policies, regulations, and laws during the HR planning process, focusing on specific ones that affect the specific company.

## **B. Geographic/Competitive Evaluations**

When making HR plans, employers must consider a number of geographic and competitive concerns. The *net migration* into a particular region is important. *Direct competitors* are another important external force in HR planning. Failure to consider the competitive labor market and to offer pay scales and benefits competitive with those of organizations in the same general industry and geographic location may cost a company dearly in the long run. Finally, the impact of *international competition* must be considered as part of environmental scanning. Global competition for labor intensifies as global competitors shift jobs and workers around the world.

## **C. Changing Workforce Considerations**

Significant changes in the workforce, both in the United States and globally, must be considered when examining the outside workforce for HR planning. When scanning the potential and future workforce, it is important to consider a number of variables, including:

- Aging of the workforce
- Growing diversity of workers
- Female workers and work-life balancing concerns
- Availability of contingent workers
- Outsourcing possibilities

When assessing these factors, it is important to analyze how they affect the current and future availability of workers with specific capabilities and experience. Many firms have planned for workforce shortages because of the brain drain created by the retirement of existing older workers.

## **V. Planning For Internal Workforce Availability**

Analyzing the jobs that will need to be done and the capabilities of people who are currently available in the organization to do them is the next part of HR planning. The needs of the organization must be compared against the existing labor supply as well as the potential labor supply available outside the organization.

### **A. Current and Future Jobs Audit**

The starting point for evaluating internal workforce strengths and weaknesses is an audit of the jobs that need to be done in the organization. The following are key questions that are addressed during the internal jobs assessment:

- What jobs exist now and how essential is each job?
- How many individuals are performing each job?
- What are the reporting relationships of jobs?
- What are the vital KSAs needed in the jobs?
- What jobs will be needed to implement future organizational strategies?
- What are the characteristics of those anticipated jobs?

## **B. Employee and Organizational Capabilities Inventory**

As HR planners gain an understanding of the current and future jobs that will be necessary to carry out organizational plans, they can conduct a detailed audit of current employees and their capabilities. An inventory of organizational skills and capabilities may consider a number of elements. The following ones are important:

- Individual employee demographics (age, length of service in the organization, etc.)
- Individual career progression (jobs held, time in each job, etc.)
- Individual performance data (work accomplishment, growth in skills, etc.)

All the details on an individual employee's skills that go into a databank may affect that person's career. Security measures must ensure that sensitive information is available only to those who have a specific use for it.

Managers and HR staff members can gather data on individual employees and aggregate details into a profile of the current organizational workforce. This profile may reveal many of the current strengths and deficiencies of people in the organization. The profile also may highlight potential future problems.

## **C. Forecasting HR Supply and Demand**

**Forecasting** uses information from the past and the present to identify expected future conditions. However, projections for the future are subject to error.

## **D. Forecasting Methods and Periods**

Forecasting methods may be either judgmental or mathematical (Figure 2-6). Despite the availability of sophisticated judgmental and mathematical models and techniques, forecasting is still a combination of quantitative methods and subjective judgment.

HR forecasting should be done over three planning periods—short range, intermediate range, and long range. The most commonly used planning period of six months to one year focuses

on *short-range* forecasts for the immediate HR needs of an organization. Intermediate- and long-range forecasting are much more difficult processes. *Intermediate-range* plans usually project one to three years into the future, and *long-range* plans extend beyond three years.

### **E. Forecasting the Demand/(Need) for Human Resources**

The demand for employees can be calculated for an entire organization and/or for individual units in the organization. The unit breakdown allows HR planners to better pinpoint the specific skills needed than does the aggregate method.

Demand for human resources can be forecast by considering specific openings that are likely to occur. The openings (or demands) are created when new jobs are being created or current jobs are being reduced. Additionally, forecasts must consider when employees leave positions because of promotions, transfers, turnovers, and terminations.

An analysis is used to develop decision rules (or “fill rates”) for each job or level. Forecasters must be aware of multiple effects throughout the organization, because as people are promoted from within, their previous positions become available.

### **F. Forecasting the Supply (Availability) of Human Resources**

Forecasting availability considers both *external* and *internal* supplies. Although the internal supply may be somewhat easier to calculate, it is important to calculate the external supply as accurately as possible.

#### **External Supply**

The external supply of potential employees available to the organization can be identified. Government estimates of labor force populations, trends in the industry, and many more complex and interrelated factors must be considered. Such information is often available from state or regional economic development offices. The following items may be included:

- Net migration into and out of the area
- Individuals entering and leaving the workforce
- Individuals graduating from schools and colleges
- Changing workforce composition and patterns
- Economic forecasts for the next few years
- Technological developments and shifts
- Actions of competing employers

- Government regulations and pressures
- Circumstances affecting persons entering and leaving the workforce

### **Internal Supply**

Figure 2-7 shows in general terms how the internal supply can be calculated for a specific employer. Estimating internal supply considers the number of external hires and the employees who move from their current jobs into others through promotions, lateral moves, and terminations. It also considers that the internal supply, among other factors, is influenced by:

- Training and development programs
- Transfer and promotion policies
- Retirement policies

In forecasting the internal supply, data from the replacement charts and succession planning efforts are used to:

- Project potential personnel changes
- Identify possible backup candidates
- Keep track of attrition (resignations, retirements, etc.) for each department in an organization

## **VI. WORKFORCE SUPPLY $\neq$ DEMAND**

Because the objective of strategic planning is to anticipate future events and conditions, managers should evaluate and revise the strategic plan on a periodic basis. Attracting and retaining the right talent is an ongoing challenge as the needs of the business change over time. Organizations need to plan for both the quantity and quality of the workforce over the planning horizon. Having sufficient workers with the right qualifications is essential to achieve the strategic plan.

### **A. Managing a Talent Surplus**

A talent surplus can be managed within a strategic HR plan in a number of ways. The reasons for the surplus will guide the ultimate steps taken by the organization. If the workforce has the right qualifications but the sales revenue has fallen, the primary strategies would involve retaining workers while cutting costs. However, if the workforce is not appropriately trained for the jobs needed, the organization may lay off those employees who cannot perform the work. Managers may use various strategies in a progressive fashion to defer workforce reductions until absolutely necessary.

### **Reduction in Work Hours or Compensation**

In order to retain qualified employees, managers may institute reduced work hours on a temporary basis. Selected groups of employees may have their workweek reduced or all employees can be asked to take a day or week off without pay. Across-the-board pay cuts can reduce labor costs while retaining some skilled employees. HR should closely monitor the situation and reinstate pay and benefits levels when the economic outlook improves to maintain employee loyalty and a sense of fairness.

### **Attrition and Hiring Freezes**

Attrition occurs when individuals quit, die, or retire and are not replaced. Unless turnover is high, attrition will eliminate only a relatively small number of employees in the short run, but it can be a viable alternative over a longer period of time. Therefore, employers may combine attrition with a freeze on hiring.

### **Voluntary Separation Programs**

Organizations can reduce the workforce while also minimizing legal risks if employees volunteer to leave. Often firms entice employees to volunteer by offering them additional severance, training, and benefits payments. Early retirement buyouts are widely used to encourage more senior workers to leave organizations early. As an incentive, employers may offer expanded health coverage and additional buyout payments to employees so that they will not be penalized economically until their pensions and Social Security benefits take effect.

Voluntary separation programs appeal to employers because they can reduce payroll costs significantly over time. Although the organization faces some upfront costs, it does not incur as many continuing payroll costs. Using such programs is also viewed as a more humane way to reduce staff than terminating long-service, loyal employees. In addition, as long as buyouts are truly voluntary, an organization offering them is less exposed to age discrimination suits. One drawback is that some employees the company would like to retain might take advantage of a buyout.

### **Workforce Downsizing**

It has been given many names, including downsizing, rightsizing, and reduction in force (RIF), but it almost always means cutting employees. Trimming underperforming units or

employees as part of a plan that is on the basis of sound organizational strategies may make sense. However, it does not increase revenues; it is a short-term cost-cutting measure that can result in a long-term lack of talent. Best practices for companies to successfully carry out layoffs include the following:

- Identify the work that is core to sustaining a profitable business.
- Identify the knowledge, skills, and competencies needed to execute the business strategy.
- Protect the bottom line and the corporate brand.
- Constantly communicate with employees.
- Pay attention to the survivors.

Severance benefits and outplacement services may be offered by companies to cushion the shock of layoffs and protect the company from litigation. **Severance benefits** are temporary payments made to laid-off employees to ease the financial burden of unemployment. Outplacement services are provided to give displaced employees support and assistance. Outplacement typically includes personal career counseling, résumé-preparation services, interviewing workshops, and referral assistance.

## **B. Legal Considerations for Workforce Reductions**

HR must be involved during workforce adjustments to ensure that the organization does not violate any of the nondiscrimination or other laws governing workforce reductions. Selection criteria for determining which employees will be laid off must comply with Title VII of the Civil Rights Act as well as the Age Discrimination in Employment Act and the Americans with Disabilities Act. A careful analysis and disparate impact review should be conducted before final decisions are made.

There is no legal requirement to provide severance benefits, and loss of medical benefits is a major problem for laid-off employees. However, under the federal Consolidated Omnibus Budget Reconciliation Act (COBRA), displaced workers can retain their group medical coverage for up to 18 months for themselves, and for up to 36 months for their dependents, if they pay the premiums themselves.

Employers must also comply with the Older Workers Benefit Protection Act (OWBPA) when implementing RIFs. The OWBPA requires employers to disclose the ages of both terminated and retained employees in layoff situations, and a waiver of rights to sue for age discrimination must meet certain requirements. The worker must be given something of value (“considerations”) in exchange for the waiver of right to sue, typically severance benefits.

To provide employees with adequate notice of plant closings or mass layoffs, a federal law was passed, the Worker Adjustment and Retraining Notification (WARN) Act. This law requires private or commercial organizations that employ 100 or more full-time workers who have worked more than 6 months in the previous year to give a 60-day notice before implementing a layoff or facility closing that involves more than 50 people.

### **C. Managing a Talent Shortage**

There can be mismatches between the qualifications needed by the employers and the skills possessed by available workers. Companies can use a number of alternative tactics to manage a talent shortage (Figure 2-9).

The existing workers can work overtime. This strategy can work on a short-term basis but is not a solution for a longer-term talent shortage. Workers may appreciate the extra hours and pay for a while, but eventually fatigue sets in and productivity and quality may drop and injuries and absenteeism may increase. Reducing turnover of qualified employees should be an ongoing effort to maintain a talented workforce.

**Alternate work arrangements** are nontraditional schedules that provide flexibility to employees, include job sharing and telecommuting. These are creative solutions to attract and retain skilled employees who want flexibility. Retirees may be rehired on a part-time or temporary basis to fill talent gaps. The advantage is that these individuals are already trained and can be productive immediately. Care must be taken not to interfere with pension payments or other benefits tied to retirement.

The use of contingent employees, who are noncore employees working at an organization on a temporary or as-needed basis, can provide short-term help. Independent contractors can be hired on an as-needed basis to fill talent shortages. The use of independent contractors must be managed closely to ensure compliance with wage and hour, safety, and employee benefit statutes.

**Outsourcing** involves transferring the management and/or routine performance of a business function to an external service provider. Organizations in the United States outsource a wide variety of noncore functions in order to reduce costs or to obtain skills and expertise not available in the organization.

## **VII. Human Resources Planning in Mergers and Acquisitions**

The purpose of a merger or acquisition is to generate growth by combining two existing

companies and creating a more competitive company. Most executives feel merger and acquisition (M&A) is an important strategy for growth through acquiring products, intellectual property, or capabilities. However, research has shown that the majority of M&A fail to deliver on the expected financial, marketing, or product gains. A significant number of failed ventures can trace their roots to HR issues that were not properly addressed such as loss of key staff, culture clashes, and poor communication. To maximize the chances of a successful integration, HR should be involved before, during, and after the deal is completed. Figure 2-10 shows the HR activities and focus during each stage of the merger process.

To determine whether or not the two organizations should combine, a rigorous process of due diligence is conducted. **Due diligence** is a comprehensive assessment of all aspects of the business being acquired. Financial, sales and marketing, operations, and human resource staffs can all be involved before the final decision is made to merge or acquire the company. HR professionals review issues related to legal compliance, compensation and benefits programs, quality of talent, and labor contract obligations. Due diligence is even more complex when the M&A involves companies in different countries. A thorough, objective analysis of the HR-related issues is critical to make good business decisions.

### **A. During Integration**

After the deal has been closed, the focus of HR activity switches to the orderly transition of basic HR processes such as payroll and benefits migration. During the first 60 days after the acquisition, HR must deliver high-quality administrative and operational support to employees and managers. The immediate concerns are often about basic services needed to run the operations. Frequent communication, employee hotlines, and guidance for managers all contribute to employee retention and loyalty during the chaotic early days of the transition.

Integrating HR information systems is important to provide managers with information about employee capabilities, performance, and potential. Gathering all relevant HR information in a single database helps managers to analyze and compare employee skills and to make informed decisions about which employees should be retained.

As the businesses are merged, culture-based conflicts will emerge. Changing the organizational culture depends upon changing behavior in the organization. The four important factors in changing culture are:

- *Define the desired behaviors*—Provide behavioral examples of how people are expected to act and tie these behaviors to the performance management system.
- *Deploy role models*—Select leaders who exemplify the desired behaviors and make them visible throughout the organization.

- *Provide meaningful incentives*—Reward the role models with recognition to reinforce their behavior and to signal the rest of the organization.
- *Provide clear and consistent messages*—Align what you say with what you do and reward.

## **B. Post Integration**

To realize the expected benefits of a merger, the months following the initial integration are important. Culture changes started in the early days must be maintained. Practical issues regarding talent management and development along with combining compensation systems will solidify the new, united organization. Failure to effectively blend the workforces and move beyond the “us-and-them” mentality can lead to inferior business results, a loss of shareholder value, and the failure of the merger. Continued change efforts are needed to bring all employees to the *one organization* mentality.

## **VIII. Measuring Effectiveness of Human Resources and Human Capital**

**Effectiveness** for organizations is a measure of the ability of a program, project, or task to produce a specific desired effect or result that can be measured. **Efficiency** is the degree to which operations are done in an economical manner.

There are many ways of measuring the financial contributions of the HR function in an organization, and many challenges associated with doing so. Return on investment (ROI) is a common measure used by financial professionals to assess the value of an investment.

A long-standing myth perpetuates the notion that one cannot really measure the value of HR practices. That notion is untrue. HR, like all other functions, must be evaluated by considering the results of its actions and the value it adds to the organization. Unfortunately, the perceptions of managers and employees in many organizations are mixed because HR has not historically measured and documented its contributions or communicated those results to them. Further, accounting practices treat expenditures on human capital and talent development as expenses rather than capital investments. This practice encourages top management to view employees as consumers of capital rather than a long-term investment.

A national working group is in the process of developing a standard to report human capital value on the SEC form 10-K because currently there is no agreed-upon method to account for the value that human capital brings to an organization. However, the effort has received some criticism because critics believe that this could fuel acquisitions, talent raiding, or extra competitive pressure.

It is important that HR managers understand financial and operational measures that drive the business and relate decisions to key performance indicators (KPIs). Metrics, benchmarking, balanced scorecards, and audits can help the organization track HR performance and measure the value of HR practices.

### A. HR Metrics and Analytics

**HR metrics** are specific measures of some aspects of HR. A metric can be developed using costs, quantity, quality, timeliness, and other designated goals. Metrics can be developed to track both HR's efficiency and effectiveness.

HR and line managers collect and share the data needed to track performance. Data to track these measures come from several sources within the organization. Financial data are required to determine costs for various HR activities and performance and turnover data can be found in HR and operations records.

Metrics and software have been combined to make analysis easier, but it is still an evolving area. *Analytics* can simply be a way to report certain metrics or a sophisticated predictive modeling designed to answer “what if” questions about HR variables. A definition of **HR analytics** that takes in both extremes is—HR analytics is an evidence-based approach to making HR decisions based on the basis of quantitative tools and models. The following characteristics should be considered when developing HR metrics and analytics:

- Accurate data can be collected.
- Measures are linked to strategic and operational objectives.
- Calculations can be clearly understood.
- Measures provide information valued by executives.
- Results can be compared both externally and internally.
- Measurement data drive HR management efforts.

### **HR Perspective: Using the Right Analytics**

HR managers rate retention and employee satisfaction first followed by training and development, recruiting costs, productivity and overall revenue, as the most important metrics for valuing HR's contribution to the organization. Certainly these items are important but it is not until you get down the list a ways that you get into the things the CEO and CFO care most about costs, open positions, revenue and productivity. Focusing on the wrong things in analytics can be as costly as doing no analysis at all.

The capability for providing operating managers with the information they want about human capital in the organization is beginning to emerge. HR can provide actionable information like—your turnover rate is X% and here is what it is costing you and here are some things you can do about it. For example at Superior Energy Services in New Orleans the HR VP calculated revenue lost for each job type when someone quit. Nearly half the people who quit were skilled operators that had a big impact on revenue. Using predictive modeling an action to reduce turnover in that group was implemented and turnover dropped significantly.

Over time analytics can help answer some of the questions for which the answers are not entirely clear in every case such as—does employee engagement relate to financial outcomes?

### **B. Human Resources and Benchmarking**

**Benchmarking** is the process of comparing the business processes and outcomes to an industry standard or best practice. Benchmarking is focused on external practices that the organization can use to improve its own processes and practices. When implementing benchmarking, managers should be careful to find organizations with similar contexts, cultures, operations, and size. Using benchmarking, HR effectiveness is best determined by measures on a year to year basis. In that way, the organization can track improvements and results from implementing specific HR practices.

### **C. Human Resources and the Balanced Scorecard**

The **balanced scorecard** is a framework organizations use to report on a diverse set of performance measures. It balances financial and nonfinancial measures so that managers focus on long-term drivers of performance and organizational sustainability. The balanced scorecard measures performance in four areas (Figure 2-12):

- *Financial measures*—Traditional financial measures such as profit and loss, operating margins, utilization of capital, return on investment, and return on assets are needed to

ensure that the organization manages its bottom line effectively.

- *Internal business processes*—Product and service quality, efficiency and productivity, conformance with standards, and cycle times can be measured to ensure that the operation runs smoothly and efficiently.
- *Customer relations*—Customer satisfaction, loyalty, and retention are important to ensure that the organization is meeting customer expectations and can depend on repeat business from its customers.
- *Learning and growth activities*—Employee training and development, mentoring programs, succession planning, and knowledge creation and sharing provide the necessary talent and human capital pool to ensure the future of the organization.

Organizational results in each of these areas determine if the organization is progressing toward its strategic objectives. Using the balanced scorecard requires spending considerable time and effort to identify the appropriate HR measures in each of the four areas and how they tie to strategic organizational success. The balanced scorecard should align with company goals and focus on results.

#### **D. Human Capital Effectiveness Measures**

Measuring the benefits of human capital is very challenging but equally important. Assessing the value of human capital demonstrates the importance of implementing effective HR practices to maintain a high-quality, workforce.

Human capital refers to the collective value of the competencies, knowledge, and skills of the employees in the organization. This capital is the renewable source of creativity and innovativeness in the organization but is not reflected in its financial statements.

Revenue per employee is a basic measure of human capital effectiveness. The formula is Revenue/Head Count (full-time employee equivalents). It is a measure of employee productivity and shows the sales revenue generated by each full-time employee. If revenues increase but employee head count remains constant, productivity would increase.

A widely used financial measure that can be applied to measure the contribution and cost of HR activities is **return on investment (ROI)**, which is a calculation showing the value of investments in human capital. It can also be used to show how long it will take for the activities to show results. The following formula can be used to calculate the potential ROI for a new HR activity:

$$\text{ROI} = \frac{C}{A + B}$$

where:

*A* = Operating costs for a new or enhanced system for the time period

*B* = One-time cost of acquisition and implementation

*C* = Value of gains from productivity improvements for the time period

ROI is stressed because it is used in most other functions in an organization and allows managers to choose from among various investment opportunities to determine the best use of funds

**Human capital value added (HCVA)** is an adjusted operating profitability figure calculated by subtracting all operating expenses *except* for labor expenses from revenue and dividing by the total full-time head count. It shows the operating profit per full-time employee. Because labor is required to generate revenues, employment costs are added back into operating expense. The formula for HCVA is:

$$\frac{\text{Revenue} - (\text{Operating Expense} - (\text{Compensation} + \text{Benefit Costs}))}{\text{Full-Time Head Count}}$$

**Human capital return on investment (HCROI)** directly shows the amount of profit derived from investments in labor, the leverage on labor cost. The formula for HCROI uses the same adjusted operating profitability figure as for HCVA, but it is divided by the human capital cost:

$$\frac{\text{Revenue} - (\text{Operating Expense} - (\text{Compensation} + \text{Benefit Costs}))}{(\text{Compensation} + \text{Benefit Costs})}$$

**Human economic value added (HEVA)** shows the wealth created per employee. It shows how much more valuable the organization has become because of the investment in human capital. Wealth is the net operating profit of a firm after the cost of capital is deducted. Cost of capital is the minimum rate of return demanded by shareholders. An HEVA approach requires that all policies, procedures, measures, and methods use cost of capital as a benchmark against which their return is judged. Human resource decisions can be subjected to the same analysis. The formula for HEVA is:

$$\frac{\text{Net Profit after Taxes} - \text{Cost of Capital}}{\text{Full-Time Head Count}}$$

Many financial measures can be tracked and reported to show the contribution human capital make to organizational results. Without such measures, it would be difficult to know what is going on in the organization, identify performance gaps, and provide feedback.

Regardless of the time and effort placed on HR measurement and HR metrics, the most important consideration is that HR effectiveness and efficiency must be measured regularly for managers to know how HR is contributing to organizational success.

### **E. Human Resources Audit**

An **HR audit** is a formal research effort to assess the current state of HR practices in an organization. This audit is used to evaluate how well activities in each of the HR areas (staffing, compensation, health and safety, etc.) have been performed, so that management can identify areas for improvement. An HR audit often helps smaller organizations without a formal HR professional to identify issues associated with legal compliance, administrative processes and recordkeeping, employee retention, and other areas. There are many levels of HR audit. Common levels are as follows:

- *Compliance Audit*—Checks record keeping on state and federal paperwork requirements
- *Benefit Programs Audit*—Reviews regulatory compliance, benefits administration and reporting
- *I-9 Audit*—Reviews compliance with immigration regulations and the I-9 form requirement
- *Specific Program Audit*—Review of specific HR subareas such as compensation
- *Full HR Audit*—Reviews all of the above plus any and all other HR functions

Audits frequently use a questionnaire and interviews performed to collect information and are done by outside entities for more objective data. They can provide assessment on how well HR is doing its job.

### **Critical Thinking Challenges**

1. Discuss how globalization has changed jobs in an organization where you have worked. What are some HR responses to those changes?

Students responses will vary based on their individual experiences. Most jobs have certainly been affected by the increased pressures from foreign competitors, foreign business practices that influence operations in the domestic country, and the technological advances that have eliminated many barriers to operating on a global scale. To effectively compete on an

international scale, the organization needs expertise to administer all HR activities in a wide range of nations. HR responses to globalization could include offshoring the company's operations in order to lower costs or following a global staffing strategy which best fits the company's culture and strategic goals.

2. What steps can HR professionals take to ensure that mergers and acquisitions are successful? How can HR help during the integration process?

Students can refer to Figure 2-10 that lists the HR activities during mergers and acquisitions to help identify what steps HR professionals can take to ensure that M&As are successful. After the deal has been closed, the focus of HR activity switches to the orderly transition of basic HR processes such as payroll and benefits migration. Early in the transition, HR focuses on identifying key talent and establishing initiatives to retain these critical employees.

3. How can an organization maintain its image while dealing with a talent surplus? If layoffs are necessary, what would you recommend managers do to ensure that survivors remain committed and productive?

Best practices for companies carrying out layoffs include:

- Identify the work that is core to sustaining a profitable business.
- Identify the knowledge, skills, and competencies needed to execute the business strategy.
- Protect the bottom line and the corporate brand.
- Constantly communicate with employees.
- Pay attention to the survivors.

Also, it is recommended that companies try to use reduction in hours or compensation, attrition or hiring freezes, and voluntary separations before layoffs. Providing severance benefits and outplacement services can also help an organization to maintain its image while dealing with a talent surplus.

4. As the HR manager for a multinational corporation, you want to identify HR competencies that are critical for global companies. Visit the website for the World Federation of People Management Association ([www.wfpma.com](http://www.wfpma.com)) to research the topic and to identify differences in the body of knowledge in different parts of the world.

At this website students can get information about the competency project that was done by this organization. The following is from the Executive Summary of the project report: "The aim of this World Federation of Personnel Management Associations' project was to

develop a worldwide definition of what an HR professional is and does in terms of a ‘global set of core competencies’. The approach taken was to consider the range of practices in different countries’ professional standards and certification programs by means of a literature review and worldwide surveys.” “The development of an HR competency model is advocated, and a summary is provided of the common core competencies. Variations in these core competencies are discussed against national, organizational and time contexts. Competency is also identified as one of the key enabling factors for an organization to create its own sustainable competitive advantage in the marketplace.” “The HR body of knowledge, and the way this is being taught and assessed around the world, is the focus for the detailed analysis of the documentation provided by associations in addition to completing the survey. The body of knowledge is presented as a Global Framework of Skills and Knowledge. This is broken down into a detailed description of what practitioners are expected to know and to be able to do in order to operate at a support, professional or strategic level in the management and development of people.”

5. As the HR Director of a U.S.-based company that is looking at global opportunities in China, you have been asked by the company president to prepare an outline for an HR strategic plan as part of the company’s expansion process. You need to develop an HR strategic plan that will integrate the goals, objectives, and strategies of the HR Department with those of the company. The plan also needs to support the objectives of other departments within the company. To get ideas on how to develop an HR strategic plan, go to [www.workinfo.com](http://www.workinfo.com).
- A. What is the process to use for identifying the components of the HR strategic planning process?

Most students will probably refer to the Strategic Planning Process shown in Figure 2-1—organizational mission, SWOT analysis, establish goals and objectives, formulate organization strategy, formulate supporting functional strategies, implement, and evaluate and reassess. This process can be used to look at the HR function in the organization and how it is tied to the organizational mission and what are the strengths, weaknesses, opportunities, and threats. Also, Figure 2-4 shows the steps in HR planning process that ties HR to the organization’s mission statement.

- B. What other company strategic objectives must the HR strategic plan integrate and support?

Organizational productivity, customer service and quality, and financial contributions are three strategies that are identified in the text. However, there might be other ones related to globalization, mergers/acquisitions, technology changes, etc.

## Case

### **Analytics at PricewaterhouseCoopers**

1. Why do more companies not use analytics to solve such problems? How would you argue to make the case for analytics in an old-line HR department?

Students could identify different reasons, but some possible answers might be that:

- The HR staff is not knowledgeable about using HR analytics
- Senior management doesn't realize the value of HR analytics and doesn't ask or expect that type of analysis from HR

To make the case for adopting HR analytics, the HR staff could calculate some metrics and do some analysis to show senior management how the power of HR metrics and analytics is an untapped resource.

2. What resources could an HR professional consult to begin building expertise in this area of analytics?

There are HR metrics classes through professional associations such as Society for Human Resource Management (SHRM) and there are many articles, books, and software that the HR staff could use to educate themselves. Also, the HR staff could work through their local SHRM professional association to find other companies that are using HR metrics.

## Supplemental Cases

### **Where Do You Find the Bodies?**

This case identifies problems associated with HR planning and recruiting in a tight labor market. (For the case, go to [www.cengage.com/management/mathis](http://www.cengage.com/management/mathis).)

## **Questions**

1. How does this case illustrate the lack of HR planning?

Student answers may vary. The corporate headquarters did not consider the gap in the wage offered and the acceptable wage rate in the city. Analyzing the jobs that need to be done and the capabilities of people who are currently available in the organization to do them is an important part of HR planning, which the headquarters of the automobile service center

failed to do. When the employees started quitting their jobs the company should have taken a cue from it and corrected the salary offered to the employees in order to retain the rest of the employees from quitting.

2. What approaches could be used to recruit mechanics?

Student answers may vary. Because the objective of strategic planning is to anticipate future events and conditions, managers should evaluate and revise the strategic plan on a periodic basis. Attracting and retaining the right talent is an ongoing challenge as the needs of the business change over time. Organizations need to plan for both the quantity and quality of the workforce over the planning horizon. Having sufficient workers with the right qualifications is essential to achieve the strategic plan. Also the potential employees should be offered competitive wages so that they do not quit their jobs in lieu of other well-paying jobs.

### **Comments**

The situation described in Boomtown is very typical in several parts of the western United States. Unfortunately there are no easy solutions that Milt can adopt. He might try recruiting mechanics from economically depressed areas elsewhere and Milt might design an incentive system for use with shop personnel. Another alternative is to start renting space in the center for individuals to work on their own vehicles. Also, Milt and his boss must convince headquarters that there must be greater flexibility available to the managers in Boomtown. In summary, the case emphasizes the need for planning, flexibility, and creativity in dealing with personnel problems, and the fact that organizations are truly affected by environmental forces.

### **Xerox**

This case highlights the challenges of employee retention during stressful and unpredictable times when Xerox was undergoing a significant shift in its strategic focus. (For the case, go to [www.cengage.com/management/mathis](http://www.cengage.com/management/mathis)).

1. Discuss the challenges faced by HR management when significant staff cutbacks occur and how they should be addressed.

When companies cannibalize the human resources needed to grow and innovate, disruption follows for some time. Downsizing can hurt productivity by leaving “surviving” employees overburdened and demoralized. Survivors need information about why the actions had to be taken and what the future holds for them personally. The more employees are involved in the

restructuring, the more likely the transition is to be smoother. HR professionals and managers, too, find downsizing stressful and may react negatively to having to be the bearers of bad news. The most common methods used when downsizing must occur include attrition and hiring freezes, early retirement buyouts, and layoffs. Voluntary separation programs appeal to employers because they can reduce payroll costs significantly over time. Using such programs is also viewed as a more humane way to reduce staff than terminating long-service, loyal employees. One drawback is that some employees the company wishes would stay, as well as those it wishes would leave, can take advantage of a buyout. Employers must also comply with WARN and other laws. It is often recommended that employers should provide outplacement services to give displaced employees support and assistance.

2. Use of technology, employee retention, and HR development have been at the core of HR becoming more strategic at Xerox. Why have those areas been so key?

These areas have been key because they illustrate to employees that Xerox is committed to professional development and continuous learning for its employees. These efforts should also help Xerox employees perform at a higher level to continue its rebound. Focusing on employee retention and HR development helps Xerox reduce its turnover which is an expensive cost. Using the results of the employee surveys will also assure that Xerox is actually providing the types of programs that lead to employee retention. It is very important when downsizing has occurred that the organization emphasize keeping its high-potential employees and managers.

### **Pioneers in HR Analytics**

HR analytics at four different organizations helped solve several problems and shows how analytics can be used. (For the case, go to [www.cengage.com/management/mathis](http://www.cengage.com/management/mathis).)

1. What are some reasons that more organizations do not implement HR analytics? How would you make the case for adopting HR analytics?

Students could identify different reasons, but some possible answers might be:

- The HR staff is not knowledgeable about using HR analytics
- Senior management doesn't realize the value of HR analytics and doesn't ask or expect that type of analysis from HR

To make the case for adopting HR analytics, the HR staff could calculate some metrics and do some analysis to show senior management how the power of HR metrics and analytics is an untapped resource.

2. How can HR professionals develop the needed skills to analyze and interpret metrics? What resources could an HR professional consult to begin building expertise in this area?

There are HR metrics classes through professional associations such as SHRM and there are many articles, books, and software that the HR staff could use to education themselves. Also, the HR staff could work through their local SHRM professional association to find other companies that are using HR metrics.