Strategy and Human Resources Planning

After studying this chapter, you should be able to

1. Identify the advantages of integrating human resources planning and strategic planning.
2. Understand how an organization’s competitive environment influences strategic planning.
3. Recognize the importance of internal resource analysis.
4. Describe the basic tools for human resources forecasting.
5. Explain the linkages between competitive strategies and HR.
6. Understand the requirements of strategy implementation.
7. Recognize the methods for assessing and measuring the effectiveness of strategy.
One of the clichés about company annual reports is that they often claim that “people are our most important asset.” Although we might believe this to be true, the fact is that historically managers often have not acted as though they themselves really believed it. In the past, executives often tried to remove human resources from the strategy equation, by substituting capital for labor where possible, or by creating hierarchical structures that separated those who think from those who actually do the work. But much is changing today.

In a recent survey by USA Today and Deloitte & Touche, nearly 80 percent of corporate executives said the importance of HRM in their firms has grown substantially over the past ten years, and two-thirds said that HR expenditures are now viewed as a strategic investment rather than simply a cost to be minimized.

Strategic Planning and Human Resources

As we explained in Chapter 1, “competing through people” is the theme for this book. But the idea remains only a premise for action until we put it into practice. To deliver on this promise, we need to understand some of the systems and processes in organizations that link human resources management and strategic management. A few definitions may be helpful up front.

First of all, **strategic planning** involves a set of procedures for making decisions about the organization’s long-term goals and strategies. In this chapter, we discuss strategic plans as having a strong external orientation that covers major portions of the organization. They especially focus on how the organization will position itself relative to competitors in order to achieve long-term survival, value, and growth. **Human resources planning (HRP),** by comparison, is the process of anticipating and making provision for the movement of people into, within, and out of an organization. Overall, its purpose is to help managers deploy human resources as effectively as possible, where and when they are needed, in order to accomplish the organization’s goals. **Strategic human resources management (SHRM),** then, combines strategic planning and HR planning. It can be thought of as the pattern of human resources deployments and activities that enable an organization to achieve its strategic goals.

Although planning has always been an essential process of management, increased emphasis on HR issues becomes especially critical when organizations consider global strategies, mergers, relocation of plants, innovation, downsizing, outsourcing, offshoring, or the closing of operating facilities. Dramatic shifts in the composition of the labor force require that managers become more involved in planning, since such changes affect the full range of HR practices (such as employee recruitment, selection, training, compensation, and motivation).

**Strategic Planning and HR Planning: Linking the Processes**

As organizations plan for their future, HR managers must be concerned with meshing HRP and strategic planning for the organization as a whole. Through strategic planning, organizations set major objectives and develop comprehensive plans to achieve those objectives. Human resources planning relates to strategic planning in
several ways, but at a fundamental level we can focus on two issues: strategy formulation and strategy implementation. Human resources planning provides a set of inputs into the strategic formulation process in terms of what is possible; that is, whether the types and numbers of people are available to pursue a given strategy. For example, when Barnes & Noble executives contemplated the move into web-based commerce to compete with Amazon.com, one of the issues they had to address was whether they had the talent needed to succeed in that arena.

In addition to strategy formulation, HRP is important in terms of strategy implementation as well. Once the strategy is devised, executives must make primary resource allocation decisions, including those pertaining to structure, processes, and human resources. Companies such as GE, IBM, and CIGNA have taken strides to combine these two aspects of strategic management.

All the available evidence suggests that the integration of HRP and strategic planning tends to be most effective when there is a reciprocal relationship between the two processes. In this relationship, the top management team recognizes that strategic-planning decisions affect—and are affected by—HR concerns. Figure 2.1 illustrates the basic outline of how companies have begun aligning HRP and strategic planning in this way. While this figure begins to address this issue of strategic alignment, we will raise the issue at several points throughout the chapter.

As we look at trends in the best of companies, there is virtually no distinction between strategic planning and HRP; the planning cycles are the same and HR issues

### Figure 2.1

<table>
<thead>
<tr>
<th>BUSINESS/CORPORATE</th>
<th>HUMAN RESOURCES</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mission, Vision and Values</td>
<td>• Capture underlying philosophy</td>
</tr>
<tr>
<td>External Analysis</td>
<td>• Establish foundation of culture</td>
</tr>
<tr>
<td>Internal Analysis</td>
<td>• Guide ethical codes of conduct</td>
</tr>
<tr>
<td>Strategy Formulation</td>
<td>• Demographic trends</td>
</tr>
<tr>
<td>Strategy Implementation</td>
<td>• External supply of labor</td>
</tr>
<tr>
<td>Evaluation</td>
<td>• Competitor benchmarking</td>
</tr>
<tr>
<td>SWOT Analysis</td>
<td>• Strengths and weaknesses (SW)</td>
</tr>
<tr>
<td></td>
<td>• Core competencies</td>
</tr>
<tr>
<td></td>
<td>• Resources: People, process, systems</td>
</tr>
<tr>
<td></td>
<td>• Corporate strategy</td>
</tr>
<tr>
<td></td>
<td>• Business strategy</td>
</tr>
<tr>
<td></td>
<td>• Functional strategy: Alignment</td>
</tr>
<tr>
<td></td>
<td>• Design structure, systems, etc.</td>
</tr>
<tr>
<td></td>
<td>• Allocate resources</td>
</tr>
<tr>
<td></td>
<td>• Leadership, communication, and change</td>
</tr>
<tr>
<td></td>
<td>• Assessment and benchmarking</td>
</tr>
<tr>
<td></td>
<td>• Ensuring alignment</td>
</tr>
<tr>
<td></td>
<td>• Agility and flexibility</td>
</tr>
<tr>
<td></td>
<td>• Reconcile supply and demand</td>
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<tr>
<td></td>
<td>• Quality, service, speed, innovation</td>
</tr>
<tr>
<td></td>
<td>• External fit/alignment and internal fit</td>
</tr>
<tr>
<td></td>
<td>• Human capital metrics</td>
</tr>
<tr>
<td></td>
<td>• Balanced Scorecard</td>
</tr>
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As we look at trends in the best of companies, there is virtually no distinction between strategic planning and HRP; the planning cycles are the same and HR issues
are seen as inherent in the management of the business. As James Walker, noted HRP expert, put it, “Today, virtually all business issues have people implications; all human resource issues have business implications.” HR managers are important facilitators of the planning process and are viewed as credible and important contributors to creating the organization’s future. This positive linkage occurs when the HR manager becomes a member of the organization’s management steering committee or strategic-planning group. Once this interactive and dynamic structure exists, HR managers are recognized as contributing strategic planners alongside other top managers. This is an important element for the rest of our discussion in this chapter. Traditionally, authors—and too many HR managers—have treated HR planning and strategic planning as separate activities. Instead, we provide a step-by-step process to show how the two aspects of planning can be integrated.

### Step One: Mission, Vision, and Values

The first step in strategic planning is establishing a mission, vision, and values for the organization. The **mission** is the basic purpose of the organization, as well as its scope of operations. It is a statement of the organization’s reason for existing. The mission often is written in terms of general clients it services. Depending on the scope of the organization, the mission may be broad or narrow. For example, the mission of Merck and Company is as follows:

> The mission of Merck is to provide society with superior products and services by developing innovations and solutions that improve the quality of life and satisfy customer needs, and to provide employees with meaningful work and advancement opportunities, and investors with a superior rate of return.

The **strategic vision** of the organization moves beyond the mission statement to provide a perspective on where the company is headed and what the company can become in the future. Although the terms mission and vision often are used interchangeably, the vision statement ideally clarifies the long-term direction of the company and its strategic intent.

Organizational **core values** are the strong enduring beliefs and principles that the company uses as a foundation for its decisions. Starbucks, for example, lists the following core values:

- Provide a great work environment and treat each other with respect and dignity.
- Embrace diversity as an essential component in the way we do business.
- Apply the highest standards of excellence to the purchasing, roasting, and fresh delivery of our coffee.
- Develop enthusiastically satisfied customers all of the time.
- Contribute positively to our communities and our environment.
- Recognize that profitability is essential to our future success.

These are the underlying parameters for how the company will act toward customers, employees, and the public in general. In many cases, the values capture the underlying philosophy of the company culture and give direction to its employees. The values also place limits on what behavior is seen as ethical and acceptable. Highlights in HRM I shows the results of IBM’s recent effort to reexamine and reinforce its values.
Our Values at Work on Being an IBMer

Business Value and a Company’s Values

We’ve been spending a great deal of time thinking, debating and determining the fundamentals of this company. It has been important to do so. When IBMers have been crystal clear and united about our strategies and purpose, it’s amazing what we’ve been able to create and accomplish. When we’ve been uncertain, conflicted or hesitant, we’ve squandered opportunities and even made blunders that would have sunk smaller companies.

It may not surprise you, then, that last year we examined IBM’s core values for the first time since the company’s founding. In this time of great change, we needed to affirm IBM’s reason for being, what sets the company apart and what should drive our actions as individual IBMers.

Importantly, we needed to find a way to engage everyone in the company and get them to speak up on these important issues. Given the realities of a smart, global, independent-minded, 21st-century workforce like ours, I don’t believe something as vital and personal as values could be dictated from the top.

So, for 72 hours last summer, we invited all 319,000 IBMers around the world to engage in an open “values jam” on our global intranet. IBMers by the tens of thousands weighed in. They were thoughtful and passionate about the company they want to be a part of. They were also brutally honest. Some of what they wrote was painful to read, because they pointed out all the bureaucratic and dysfunctional things that get in the way of serving clients, working as a team or implementing new ideas. But we were resolute in keeping the dialog free-flowing and candid. And I don’t think what resulted—broad, enthusiastic, grassroots consensus—could have been obtained in any other way.

In the end, IBMers determined that our actions will be driven by these values:

- Dedication to every client’s success
- Innovation that matters, for our company and for the world
- Trust and personal responsibility in all relationships

I must tell you, this process has been very meaningful to me. We are getting back in touch with what IBM has always been about—and always will be about—in a very concrete way. And I feel that I’ve been handed something every CEO craves: a mandate, for exactly the right kinds of transformation, from an entire workforce.

Where will this lead? It is a work in progress, and many of the implications remain to be discovered. What I can tell you is that we are rolling up our sleeves to bring IBM’s values to life in our policies, procedures and daily operations.

I’ve already touched on a number of things relating to clients and innovation, but our values of trust and personal responsibility are being managed just as seriously—from changes in how we measure and reward performance, to how we equip and support IBMers’ community volunteerism.

Our values underpin our relationships with investors, as well. In late February, the board of directors approved sweeping changes in executive compensation. They include innovative programs that ensure investors first receive meaningful returns—a 10 percent increase in the

(continued on next page)
Step Two: Environmental Analysis

The mission, vision, and values drive the second component of the strategic management process: analysis of external opportunities and threats. Changes in the external environment have a direct impact on the way organizations are run and people are managed. Some of these changes represent opportunities, and some of them represent real threats to the organization. Because of this, successful strategic management depends on an accurate and thorough evaluation of the environment. Environmental scanning is the systematic monitoring of the major external forces influencing the organization. Managers attend to a variety of external issues; however, the following six are monitored most frequently:

1. Economic factors, including general, regional, and global conditions
2. Industry and competitive trends, including new processes, services, and innovations
3. Technological changes, including information technology, innovations, and automation
4. Government and legislative issues, including laws and administrative rulings
5. Social concerns, including child care, elder care, the environment, and educational priorities
6. Demographic and labor market trends, including age, composition, and literacy

By scanning the environment for changes that will likely affect an organization, managers can anticipate their impact and make adjustments early.

Samuel J. Palmisano
Chairman, President and Chief Executive Officer


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stock price—before IBM’s top 300 executives can realize a penny of profit from their stock option grants. Putting that into perspective, IBM’s market value would have to increase by $17 billion before executives saw any benefit from this year’s option awards. In addition, these executives will be able to acquire market-priced stock options only if they first invest their own money in IBM stock. We believe these programs are unprecedented, certainly in our industry and perhaps in business.

Clearly, leading by values is very different from some kinds of leadership demonstrated in the past by business. It is empowering, and I think that’s much healthier. Rather than burden our people with excessive controls, we are trusting them to make decisions and to act based on values—values they themselves shaped.

To me, it’s also just common sense. In today’s world, where everyone is so interconnected and interdependent, it is simply essential that we work for each other’s success. If we’re going to solve the biggest, thorniest and most widespread problems in business and society, we have to innovate in ways that truly matter. And we have to do all this by taking personal responsibility for all of our relationships—with clients, colleagues, partners, investors and the public at large. This is IBM’s mission as an enterprise, and a goal toward which we hope to work with many others, in our industry and beyond.
Competitive Environment

While many factors in the general environment may influence strategic decisions, analysis of the firm’s competitive environment is central to strategic planning. The competitive environment includes the specific organizations with which the firm interacts. As shown in Figure 2.2, the competitive environment includes customers, rival firms, new entrants, substitutes, and suppliers. In strategic planning, firms analyze the competitive environment in order to adapt to or influence the nature of competition. A general rule of thumb about this analysis is: The more power each of these forces has, the less profitable (and therefore attractive) the industry will be. Let’s look at each of the five forces.

Customers

One of the most important assessments a firm can make is identifying the needs of its customers. At a fundamental level, strategy focuses on creating customer value—and different customers often want different things. For example, in the hotel industry, business travelers may want convenient locations with meeting facilities. Vacationers may want resort locations with swimming pools, golf courses, and luxury spas. Other travelers may just want an inexpensive room next to the highway. The point is that increasingly, “one size does not fit all,” and organizations need to know how they are going to provide value to customers. That is the foundation for strategy, and it influences the kind of skills and behavior that will be needed from employees. For example, actions and attitudes that lead to excellent customer service can include the following:

- Speed of delivering normal orders
- Willingness to meet extraordinary needs
- Merchandise delivered in good condition
- Readiness to take back defective goods and resupply new goods quickly
- Availability of installation and repair services and parts

Figure 2.2 Five Forces Framework
Rival Firms
In addition to customer analysis, perhaps the most obvious element of industry analysis is examining the nature of competition. The first question to consider is: Who is the competition? Often the answer is clear to everyone, but sometimes it is not. For example, for many years, Toys “R” Us viewed its main competitors to be other toy stores such as FAO Schwarz or KB Toys. However, other retailers such as Target and Wal-Mart soon moved into this space very successfully. This had a direct effect on human resources planning for Toys “R” Us. While in the past, Toys “R” Us had been successful with a volume-based approach (that is, “stack it high, and let it fly”), bigger retailers soon gained an advantage—who can beat Wal-Mart’s volume and cost advantage? As a consequence, Toys “R” Us had to modify its strategy to compete more on customer service and the expertise of its employees. But did Toys “R” Us have the number and kind of employees required to compete in this way? Were its staffing, training, performance management, and compensation practices aligned with this strategy?

New Entrants
As suggested previously, new companies can sometimes enter an industry to compete with established firms. And sometimes they can’t. To protect their position, companies often try to establish entry barriers to keep new firms out of the industry. However, when new firms do enter an industry it is often because they have a different—and perhaps better—way to provide value to customers. For example, when JetBlue entered the airline business, it distinguished itself by providing excellent service and low prices in regions where customers did not have many options. The HR implications of this are clear. When we look at the challenges faced by traditional airlines because of the threat of low-cost carriers such as JetBlue, Alaska Air, and Southwest Airlines, we can clearly see that new entrants can change the “rules of the game” in an industry. The impact on labor costs, productivity, skills required, and work design are important considerations in both strategic planning and human resources planning.

Substitutes
At times, the biggest opportunity or threat in an industry is not with direct competition, but from substitution. In the telephone industry, for example, cellular technology is rapidly substituting for land-line phone systems. Similarly, some firms are using new technology to offer telephone service over the Internet (VOIP). These substitutes offer the same service or function as traditional firms, but through a different method. That implies that firms may need to adjust their skill base in order to support different technologies. Or they may need to think about how they will compete in different ways. As an example, think about how the travel business has changed over the years. Travel agents used to be the key resource for flights, hotels, rental cars, and the like. The focus was almost exclusively on transactions. However, with the advent of online reservation systems, travel agents have had to adapt their approach. Today, they are as likely to compete based on the service they provide and the expertise they have about particular locations.

Suppliers
Organizations rarely create everything on their own, but instead have suppliers that provide them with key inputs. These inputs can include raw materials for production, money (from banks and stockholders), information, and people. This last factor—
people, or labor as it is historically called—has direct implications for strategic planning and human resources planning. Because of its central role in both strategic planning and HRP, we explore it next in much more detail.

**External Supply of Labor**

Many factors influence the labor supply, including demographic changes in the population, national and regional economics, education level of the workforce, demand for specific employee skills, population mobility, and governmental policies. National and regional unemployment rates are often considered a general barometer of labor supply. Consider these U.S. Census Bureau facts about American workers:

- By 2012, employment will rise to more than 163 million workers. And while the labor force is expected to grow at a rate of 12 percent, the growth rate for college graduate–level jobs is expected to grow by more than double that.
- By 2012, the average ages of the workforce will be 41, up from 34.7 in 1979. Yet while the group of workers ages 45 to 54 will have increased by 52 percent, the group between ages 35 and 44 will have shrunk by more than 10 percent.
- The fastest-growing segments of the workforce in terms of race will be Asian Americans and Hispanics (an increase primarily effected through immigration).
- By 2012, nearly one in five American workers will be age 55 or older.
- On average nationwide, high school graduates can expect to earn about $27,280 annually. Those with a bachelor degrees can expect to earn, on average, nearly double that amount.
- Women will make up approximately 48 percent of the workforce in 2012. Today, three of every five college graduates are women.
- Nearly 25 percent of the workforce is composed of part-timers, and the number has been steadily rising. But only one in five of these workers has access to medical coverage.
- Over the next ten years another 1 million-plus computer, Internet, and software technology job openings will be created. However, the fastest-growing sector will be in service industries.
- Between 45 and 50 percent of adults in the United States have only limited reading and writing abilities needed to handle the minimal demands of daily living or job performance.

These labor force trends illustrate the importance of monitoring demographic changes as a part of environmental scanning. Fortunately, labor market analysis is aided by various published documents. Unemployment rates, labor force projection figures, and population characteristics are reported by the U.S. Department of Labor. The *Monthly Labor Review* and *Occupational Outlook Handbook*, both published by the Bureau of Labor Statistics (BLS) of the U.S. Department of Labor, contain information on jobholder characteristics and predicted changes in the workforce. In addition, local chambers of commerce and individual state development and planning agencies also may assist both large organizations and new business ventures with labor market analysis.

These sources of information are invaluable. In a rapidly changing environment, it is extremely risky to be caught off guard. Such changes are important for many reasons, some related to operational issues and some to strategic issues. HRP has to
focus on both. At an operational level, the change in labor supply directly influences hiring plans that must take into account the demographic composition of the population in the area where the organization is located. Similarly, with a “maturing” workforce, HRP must consider the implications for recruitment and replacement policies.

From a strategic standpoint, changes in the labor supply can limit the strategies available to firms. High-growth companies in particular may find it difficult to find the talent they need to expand their businesses. While unemployment rates vary by sector, the shortage of talent in high-skill jobs continues to create real challenges for firms.

Step Three: Internal Analysis

As organizations conduct external analyses of environmental opportunities and threats, they also analyze their internal strengths and weaknesses. Internal analysis provides strategic decision makers with an inventory of organizational skills and resources as well as their performance levels.

To be sure, many resources combine to give organizations a competitive advantage. But in contrast to the past, the advantages due to physical assets are being supplanted by intangible assets, including people. As James Brian Quinn noted, “With rare exceptions, the economic and producing power of firms lies more in its intellectual and service capabilities than in its hard assets—land, plant, and equipment.”

The Three Cs: Culture, Competencies, and Composition

In the context of human resource planning, internal analysis focuses especially on “the three Cs”: culture, competencies, and composition.

Culture: Auditing Values, Beliefs, and Attitudes

Think about our initial discussion (in Step One) of mission, vision, and values. Because managers increasingly understand that employee-oriented cultures are critical to success, they often conduct cultural audits to examine the attitudes and beliefs of the workforce as well as the activities they engage in. At one level, this analysis focuses on whether critical values are embraced and demonstrated by employees throughout the organization. Employee surveys, for example, can measure how employees feel on a number of critical issues, and can be very useful for upward assessment and feedback of (and for) management.

However, these audits can go much deeper. Sears, for example, found that positive employee attitudes on ten essential factors—including workload and treatment by bosses—are directly linked to customer satisfaction and revenue increases.

Cultural audits essentially involve discussions among top-level managers of how the organization’s culture reveals itself to employees and how it can be influenced or improved. The cultural audit may include such questions as the following:

- How do employees spend their time?
- How do they interact with each other?
- Are employees empowered?
What is the predominant leadership style of managers?

How do employees advance within the organization?

By conducting in-depth interviews and making observations over a period of time, managers are able to learn about the culture of their organization and the attitudes of its employees. With the increased diversity of the U.S. workplace, cultural audits can be used to determine whether there are different groups, or subcultures, within the organization that have distinctly different views about the nature of work, the quality of managers, and so on. Before any HR planning can take place, managers have to gain a clear idea of how employees view their organization.

Competencies: People as a Strategic Resource

A growing number of experts now argue that the key to a firm's success is based on establishing a set of core competencies—integrated skills and knowledge sets within an organization that distinguish it from its competitors and deliver value to customers. McDonald's, for example, has developed core competencies in management efficiency and training. Federal Express has core competencies in package routing, delivery, and employee relations. Royal Dutch Shell has core competencies in oil exploration and production. Core competencies tend to be limited in number, but they provide a long-term basis for technology innovation, product development, and service delivery.

In many cases, people are a key resource that underlies a firm's core competencies. Particularly in knowledge-based industries such as software and information services, success increasingly depends on “people-embodied know-how.” This includes the knowledge, skills, and abilities of employees. Organizations can achieve a sustained competitive advantage through people if they are able to meet the following criteria:

1. The resources must be valuable. People are a source of competitive advantage when they improve the efficiency or effectiveness of the company. Value is increased when employees find ways to decrease costs, provide something unique to customers, or some combination of the two. Empowerment programs, total-quality initiatives, and continuous improvement efforts at companies such as Nordstrom and UPS are intentionally designed to increase the value that employees represent on the bottom line.

2. The resources must be rare. People are a source of competitive advantage when their knowledge, skills, and abilities are not equally available to competitors. Companies such as Microsoft, McKinsey, and Four Seasons Hotels invest a great deal to hire and train the best and the brightest employees in order to gain an advantage over their competitors.

3. The resources must be difficult to imitate. People are a source of competitive advantage when employee capabilities and contributions cannot be copied by others. Disney, Southwest Airlines, and Starbucks are each known for creating unique cultures that get the most from employees (through teamwork) and are difficult to imitate.

4. The resources must be organized. People are a source of competitive advantage when their talents can be combined and deployed to work on new assignments at a moment’s notice. Companies such as IBM and GE have invested in information technology to help allocate and track employee assignments to temporary projects. Teamwork and cooperation are two other pervasive methods for ensuring an organized workforce.

These four criteria highlight the importance of people and show the closeness of HRM to strategic management.
Composition: The Human Capital Architecture

A related element of internal analysis for organizations that compete on competencies is determining the composition of the workforce. That is, managers need to determine whether people are available, internally or externally, to execute an organization’s strategy. In some respects, this has traditionally been the focal point of human resources planning. Managers have to make tough decisions about whom to employ internally, whom to contract externally, and how to manage different types of employees with different skills who contribute in different ways to the organization.

Figure 2.3 shows that different skill groups in any given organization can be classified according to the degree to which they create strategic value and are unique to the organization. As a general rule, managers often consider contracting externally (or outsourcing) skill areas that are not central to the firm’s core competence. HRP
plays an important role in helping managers weigh the costs and benefits of using one approach to employment versus another.

Evidence from research suggests that employment relationships and HR practices for different employees vary according to which segment they occupy in this matrix. Here are some general trends:

**Core Knowledge Workers.** This group of employees tends to have firm-specific skills that are directly linked to the company’s strategy (such as R&D scientists in a pharmaceuticals company or computer scientists in a software development company). These employees typically are engaged in knowledge work that involves considerable autonomy and discretion. Companies tend to make long-term commitments to these employees, investing in their continuous training and development and perhaps giving them an equity stake in the organization.

**Traditional Job-Based Workers.** This group of employees has skills that are quite valuable to a company, but not particularly unique (such as salespeople in a department store or truck drivers for a courier service). These employees tend to be employed to perform a predefined job. As it is quite possible that they could leave to go to another firm, managers frequently make less investment in training and development and tend to focus more on paying for short-term performance achievements.

**Contract Labor.** This group of employees typically has skills that are of less strategic value and generally available to all firms (such as clerical workers, maintenance workers, and staff workers in accounting and human resources). Individuals in these jobs are increasingly hired from external agencies on a contract basis, and the scope of their duties tends to be limited. Employment relationships tend to be transactional, focused on rules and procedures, with less investment in development.

**Alliance Partners.** This group of individuals has skills that are unique, but frequently not directly related to a company’s core strategy (such as attorneys, consultants, and research lab scientists). Although companies perhaps cannot justify their internal employment, given their tangential link to strategy, these individuals have skills that are specialized and not readily available to all firms. As a consequence, companies tend to establish longer-term alliances and partnerships with them and nurture an ongoing relationship focused on mutual learning. Considerable investment is made in the exchange of information and knowledge.

**Forecasting: A Critical Element of Planning**

While internal analysis of the three Cs (culture, competencies, and composition) may reveal a great deal about where the organization is today, things change. And in an important sense strategic planning is about managing that change. Managers must continually forecast both the needs and the capabilities of the firm for the future in order to do an effective job at strategic planning. As shown in Figure 2.4, managers focus on (at least) three key elements: (a) forecasting the demand for labor, (b) forecasting the supply of labor, and (c) balancing supply and demand considerations. Careful attention to each factor helps top managers meet their human resources requirements.
Consider for a moment the high costs of not forecasting—or forecasting poorly. If job vacancies are left unfilled, the resulting loss in efficiency can be very costly, particularly when lead time is required to train replacements. As ridiculous as it may sound, we have seen situations in which employees are laid off in one department while applicants are hired for similar jobs in another department. This kind of mistake can be frustrating, to say the least, and can be confounded when overhiring results in having to lay off employees who were just recently hired. Poor forecasting also makes it difficult for employees to effectively assess their own careers and development. As a result, some of the more competent and ambitious workers may seek other employment where they feel they will have better career opportunities.

On the plus side, accurate forecasting provides the kind of information managers need to make sound decisions. It can help them ensure that they have the right number and right kind of people in the right places at the right times, doing things that provide value to both the organization and the employees.

**Forecasting Demand for Employees**

If a key component of forecasting is predicting the number and type of people needed to meet organizational objectives, the question remains: “How can this be done?” A variety of factors, including competitive strategy, technology, structure, and productivity, can influence the demand for labor. For example, as noted in Chapter 1, use of advanced technology is generally accompanied by less demand for low-skilled labor.
workers and more demand for knowledge workers. External factors such as business cycles—economic and seasonal trends—can also play a role. For example, retailers such as The Gap, Bath & Body Works, and Marks & Spencer rely heavily on temporary employees between November and January, during the holiday season.

There are two approaches to HR forecasting: quantitative and qualitative. When concentrating on human resources needs, forecasting is primarily quantitative in nature and, in large organizations, is accomplished by highly trained specialists. Quantitative approaches to forecasting can employ sophisticated analytical models, although forecasting may be as informal as having one person who knows the organization anticipate future HR requirements. Organizational demands will ultimately determine which technique is used. Regardless of the method, however, forecasting should not be neglected, even in relatively small organizations.

**Quantitative Approaches.** Quantitative approaches to forecasting involve the use of statistical or mathematical techniques; they are the approaches used by theoreticians and professional planners. One example is trend analysis, which forecasts employment requirements on the basis of some organizational index and is one of the most commonly used approaches for projecting HR demand. Trend analysis is typically done in the following several stages:

First, select an appropriate business factor. This should be the best available predictor of human resources needs. Frequently, sales or value added (selling price minus costs of materials and supplies) is used as a predictor in trend analysis. Second, plot a historical trend of the business factor in relation to the number of employees. The ratio of employees to the business factor will provide a labor productivity ratio (for example, sales per employee). Third, compute the productivity ratio for at least the past five years. Fourth, calculate human resources demand by multiplying the business factor by the productivity ratio. Finally, project human resources demand out to the target year. This procedure is illustrated in Figure 2.5 for a hypothetical building contractor.

![Figure 2.5 Example of Trend Analysis of HR Demand](image-url)

*Projected figures*
Other, more-sophisticated statistical planning methods include modeling or multiple predictive techniques. Whereas trend analysis relies on a single factor (such as sales) to predict employment needs, the more-advanced methods combine several factors, such as interest rates, gross national product, disposable income, and sales, to predict employment levels. While the costs of developing these forecasting methods used to be quite high, advances in technology and computer software have made rather sophisticated forecasting tools affordable to even small businesses.

**Qualitative Approaches.** Admittedly, forecasting is frequently more an art than a science, providing inexact approximations rather than absolute results. The ever-changing environment in which an organization operates contributes to this situation. For example, estimating changes in product or service demand is a basic forecasting concern, as is anticipating changes in national or regional economics. A community hospital anticipating internal changes in technology, organization, or administration must consider these environmental factors in its forecasts of staffing needs. Also, the forecasted staffing needs must be in line with the organization's financial resources.

In contrast to quantitative approaches, qualitative approaches to forecasting are less statistical, attempting to reconcile the interests, abilities, and aspirations of individual employees with the current and future staffing needs of an organization. In both large and small organizations, HR planners may rely on experts who help prepare forecasts to anticipate staffing requirements. Management forecasts are the opinions (judgments) of supervisors, department managers, experts, or others knowledgeable about the organization's future employment needs. For example, at the Ripe Tomato, a growing family dining chain, each restaurant manager is responsible for employment forecasts.

Another qualitative forecasting method, the Delphi technique, attempts to decrease the subjectivity of forecasts by soliciting and summarizing the judgments of a preselected group of individuals. The final forecast thus represents a composite group judgment. The Delphi technique requires a great deal of coordination and cooperation in order to ensure satisfactory forecasts. This method works best in organizations in which dynamic technological changes affect staffing levels.

Ideally, forecasting should include the use of both quantitative and qualitative approaches. In combination, the two approaches complement each other, providing a more complete forecast by bringing together the contributions of both theorists and practitioners.

**Forecasting Supply of Employees**

Just as an organization must forecast its future requirements for employees, it must also determine whether sufficient numbers and types of employees are available to staff anticipated openings. As with demand forecasts, the process involves both tracking current levels and making future projections.

**Staffing Tables and Markov Analysis.** An internal supply analysis may begin with the preparation of staffing tables. **Staffing tables** are graphic representations of all organizational jobs, along with the numbers of employees currently occupying those jobs (and perhaps also future employment requirements derived from demand forecasts). Another technique, called **Markov analysis**, shows the percentage (and actual number) of employees who remain in each job from one year to the next, as well as the proportions of those who are promoted, demoted, or transferred, or exit the
In addition to qualitative, or statistical, approaches, HR managers also rely on the opinions of managers in their organizations to help forecast the demand for future employees.

Organization. As shown in Figure 2.6, Markov analysis can be used to track the pattern of employee movements through various jobs and to develop a transition matrix for forecasting labor supply.

Forecasting the supply of human resources requires that managers have a good understanding of employee turnover and absenteeism. We have included formulas for

<table>
<thead>
<tr>
<th>Figure 2.6</th>
<th>Hypothetical Markov Analysis for a Retail Company</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>2005</strong></td>
<td><strong>2006</strong></td>
</tr>
<tr>
<td><strong>Store Managers</strong> (n = 12)</td>
<td><strong>Asst. Store Managers</strong></td>
</tr>
<tr>
<td>90%</td>
<td>11</td>
</tr>
<tr>
<td>11%</td>
<td>4</td>
</tr>
<tr>
<td><strong>Assistant Store Managers</strong> (n = 36)</td>
<td><strong>Section Managers</strong> (n = 96)</td>
</tr>
<tr>
<td>11%</td>
<td>11</td>
</tr>
<tr>
<td>66%</td>
<td>63</td>
</tr>
<tr>
<td>8%</td>
<td>8</td>
</tr>
<tr>
<td>15%</td>
<td>14</td>
</tr>
<tr>
<td>10%</td>
<td>41</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Transition percentage</strong></td>
<td><strong>Actual number of employees</strong></td>
</tr>
</tbody>
</table>
computing turnover and absenteeism rates in an appendix to this chapter. The calculations are easily made and used by managers of both large and small organizations.

**Skill Inventories and Management Inventories.** While staffing tables, Markov analysis, turnover rates, and the like tend to focus on the number of employees in particular jobs, other techniques are more oriented toward the types of employees and their skills, knowledge, and experiences. **Skill inventories** can also be prepared that list each employee’s education, past work experience, vocational interests, specific abilities and skills, compensation history, and job tenure. Of course, confidentiality is a vital concern in setting up any such inventory. Nevertheless, well-prepared and up-to-date skill inventories allow an organization to quickly match forthcoming job openings with employee backgrounds. When data are gathered on managers,
these inventories are called management inventories. And all of this analysis is made simpler these days through the use of HR information systems and enterprise systems provided by companies such as Oracle-PeopleSoft and SAP.

**Replacement Charts and Succession Planning.** Both skill and management inventories—broadly referred to as talent inventories—can be used to develop employee replacement charts, which list current jobholders and identify possible replacements should openings occur. Figure 2.7 shows an example of how an organization might develop a replacement chart for the managers in one of its divisions. Note that this chart provides information on the current job performance and promotability of possible replacements. As such, it can be used side by side with other pieces of information for succession planning—the process of identifying, developing, and tracking key individuals so that they may eventually assume top-level positions.

In today’s fast-moving environment, succession planning may be more important—and more difficult to conduct—than ever before. Executives frequently lament that their firms are chronically short of talent. Yet in a recent survey of 150 executives with the nation’s 1,000 largest companies, while all agreed on the value of identifying successors, only 72 percent said they are currently preparing someone to take their place. According to William Byham, CEO of Development Dimensions International (DDI), the typical company expects 33 percent turnover in the executive ranks in the next five years and, among these companies, roughly one-third are worried that they will not be able to find suitable replacements. And the cost of replacing these managers is extremely high, says Byham. “The average one-year estimated replacement cost is $750,000. That includes finding the new [person], training and development costs and opportunity costs of getting the new hire up to speed.” Highlights in HRM 2 shows a checklist for evaluating the “success” of succession planning.

**Step Four: Formulating Strategy**

The forecasting techniques discussed previously provide critical information for strategic planning. Recall that we noted at the beginning of the chapter that HR analysis is an input to strategy formulation. However, a word of caution is needed here. Because HR forecasting techniques take us deep into the specifics of labor supply and demand, we need to be careful not to lose sight of the larger strategic picture. One of the biggest concerns among executives is that (at times) HR managers cannot “see the forest for the trees” because they become mired in the administrative details of their planning models. SWOT analysis, discussed shortly, helps managers combine various sources of information into a broader framework for analysis.

After managers have analyzed the internal strengths and weaknesses of the firm, as well as external opportunities and threats, they have the information they need to formulate corporate, business, and HR strategies for the organization. A comparison of strengths, weaknesses, opportunities, and threats normally is referred to as a **SWOT analysis**. SWOT analysis helps executives summarize the major facts and forecasts derived from external and internal analyses. Strategy formulation builds on SWOT analysis to use the strengths of the organization to capitalize on opportunities, counteract threats, and alleviate internal weaknesses. In short, strategy formulation moves from simple analysis to devising a coherent course of action.
Succession-Planning Checklist

RATe THE SUCCESS OF YOUR SUCCESSION PLANNING

For each characteristic of a best-practice succession-planning and management program appearing in the left column below, enter a number to the right to indicate how well you believe your organization manages that characteristic. Ask other decision makers in your organization to complete this form individually. Then compile the scores and compare notes.

<table>
<thead>
<tr>
<th>Characteristics of a Best-Practice Succession-Planning and Management Program</th>
<th>How Would You Rate Your Organization’s Succession Planning and Management Program on the Characteristic?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Your organization has successfully...</td>
<td>Very Poor (1)</td>
</tr>
<tr>
<td>1 Clarified the purpose and desired results of the succession-planning and management program.</td>
<td></td>
</tr>
<tr>
<td>2 Determined what performance is required now for all job categories in the organization by establishing competency models.</td>
<td></td>
</tr>
<tr>
<td>3 Established a means to measure individual performance that is aligned with the competencies currently demonstrated by successful performers.</td>
<td></td>
</tr>
<tr>
<td>4 Determined what performance is needed in the future by establishing future competency models for all job categories.</td>
<td></td>
</tr>
<tr>
<td>5 Created an ongoing means by which to assess individual potential against future competency models.</td>
<td></td>
</tr>
<tr>
<td>6 Established a means by which to narrow gaps through the use of individual development plans (IDPs).</td>
<td></td>
</tr>
<tr>
<td>7 Created a means to follow up and hold people accountable.</td>
<td></td>
</tr>
<tr>
<td>8 Created a means by which to document competence and find organizational talent quickly when needed.</td>
<td></td>
</tr>
<tr>
<td>9 Created and sustained rewards for developing people.</td>
<td></td>
</tr>
<tr>
<td>10 Established a means by which to evaluate the results of the succession planning and management program.</td>
<td></td>
</tr>
</tbody>
</table>

Total (add up the scores for items 1–10 and place in the box on the right)

SCORES

- **50–40**: Congratulations. The succession-planning and management program in your organization conforms with best practices.
- **29–20**: Okay. While your organization could make improvements, you appear to have some of the major pieces in place for a succession-planning and management program.
- **39–30**: Pretty good. Your organization is on the way toward establishing a first-rate succession-planning and management program.
- **19–10**: Not good at all. Your organization is probably filling positions on an as-needed basis.
- **9–0**: Give yourself a failing grade. You need to take steps immediately to improve the succession-planning and management practices of your organization.

Corporate Strategy

In any industry, firms decide where and how they will compete. Corporate strategy focuses on domain selection; that is, where they will compete. Some firms choose a concentration strategy that focuses on only a limited portion of the industry. For example, Visteon Corporation specializes in electronics, climate, and power train technologies for the automotive industry. In contrast, Henry Ford at one time had fully integrated his company from the ore mines needed to make steel all the way to the showrooms where his cars were sold.

Growth and Diversification

As companies grow, their strategic choices tend to focus on geographic, volume, and product expansion. HR planning is a vital input to these decisions. Growth hinges on three related elements: (a) increased productivity, (b) a greater number of employees, and (c) developing or acquiring new skills. Concerns about staffing, training, motivation, performance, and the like can either enable growth or limit its potential. As companies diversify into new businesses, managers inevitably are faced with a “make or buy” decision. That is, should they develop the capabilities in-house or contract externally? For example, when IBM entered the personal computer market in the early 1980s, it contracted with (startup companies) Intel and Microsoft to make the hardware and operating systems for its PC. The decision did not rest solely on human resources issues, but they were an important part of the equation.

Some companies diversify far beyond their core businesses. GE, for example, has diversified from its original base in electrical and home appliance products to such wide-ranging industries as health, finance, insurance, truck and air transportation, and even media, with its ownership of NBC. In order to manage such a diverse portfolio, GE has invested heavily in the development of general management skills and leadership ability. CEO Jeffrey Immelt has stated that GE’s future depends on pursuing businesses that leverage human capital (in contrast to its traditional focus on manufacturing). This new strategy is strongly linked to human resources. In fact, the strategy is viable only because the company has done such an enviable job developing talent over the years.

Mergers and Acquisitions

In addition to strategies of growth and diversification, corporate America has seen a host of mergers and acquisitions in recent years. These include such firms as Hewlett-Packard and Compaq, Daimler-Benz and Chrysler, Walt Disney and ABC, Kmart and Sears, and Procter & Gamble and Gillette. And while there are some important competitive reasons for mergers such as these, it is unfortunate to note that many of them have not gone well. Not surprisingly, perhaps, the failure rate among firms is very high. Some estimates suggest that only about 15 percent of all mergers achieve their objectives (measured by return on investment, shareholder value, and the like). Often the failure is due to cultural inconsistencies, as well as conflicts among the managers of each firm. Clearly, these concerns point directly to the importance of effective HR planning prior to—and during—the merger process. Highlights in HRM 3 shows key HR activities associated with different phases of a merger or acquisition.
Strategic Alliances and Joint Ventures

Sometimes firms do not acquire or merge with another firm, but instead pursue cooperative strategies such as a strategic alliance or joint venture. Especially when firms enter into international joint ventures, the issues of culture (both company culture and national culture) become paramount. On the front end, HR plays a vital role in assessing the compatibility of cultures and potential problems. As the alliance is formed, HR helps select key executives and develop teamwork across the respective workforces. In addition, HR is typically involved in the design of performance assessment and mutual incentives for the alliance. And, of course, one of the controversial issues related to such alliances is the inevitable issue of outsourcing or offshoring work to other locations.

Business Strategy

While we think about corporate strategy as domain selection, business strategy is viewed in terms of domain navigation. It is more focused on how the company will compete against rival firms in order to create value for customers. We can think of value creation in a cost/benefit scenario (that is, value = benefits − costs). Companies can increase customer value either by decreasing costs to customers or by increasing their benefits (or some combination of the two). And their business strategies reflect these choices.

Low-Cost Strategy: Compete on Productivity and Efficiency

A low-cost strategy means keeping your costs low enough so that you can offer an attractive price to customers (relative to competitors). Organizations such as Dell, Wal-Mart, and Southwest Airlines have been very successful at using a low-cost strategy. Critical success factors for this strategy focus on efficiency, productivity, and minimizing waste. These types of companies often are large and try to take advantage of economies of scale in production and distribution. In many cases, the large
size allows them to sell their products and services at a lower price, which leads to higher market share, volume, and (hopefully) profits. However, even a low-cost leader must offer a product or service that customers find valuable. As Gordon Bethune, CEO of Continental Airlines, put it, "You can make a pizza so cheap that no one will buy it." Ultimately organizations need to use a cost strategy to increase value to customers, rather than take it away.

### Key HR Activities Associated with Merger or Acquisition Phases

<table>
<thead>
<tr>
<th>HR Issues</th>
<th>Key HR Activities</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Stage 1—Precombination</strong></td>
<td></td>
</tr>
<tr>
<td>Identifying reasons for the M&amp;A</td>
<td>Participate in preselection assessment of target firm</td>
</tr>
<tr>
<td>Forming M&amp;A team/leader</td>
<td>Assist in conducting thorough due diligence assessment</td>
</tr>
<tr>
<td>Searching for potential partners</td>
<td>Participate in planning for combination</td>
</tr>
<tr>
<td>Selecting a partner</td>
<td>Assist in developing HR practices that support rapid learning and knowledge transfer</td>
</tr>
<tr>
<td>Planning for managing the process</td>
<td></td>
</tr>
<tr>
<td>Planning to learn from the process</td>
<td></td>
</tr>
<tr>
<td><strong>Stage 2—Combination</strong></td>
<td></td>
</tr>
<tr>
<td>Selecting the integration manager(s)</td>
<td>Assist in recruiting and selecting integration manager(s)</td>
</tr>
<tr>
<td>Designing/implementing transition teams</td>
<td>Assist with transition team design and staffing</td>
</tr>
<tr>
<td>Creating the new structure/strategies/leadership</td>
<td>Develop retention strategies and communicate to top talent</td>
</tr>
<tr>
<td>Retaining key employees</td>
<td>Assist in deciding who goes</td>
</tr>
<tr>
<td>Managing the change process</td>
<td>Facilitate establishment of a new culture</td>
</tr>
<tr>
<td>Communicating to and involving stakeholders</td>
<td>Provide assistance to ensure implementation of HR policies and practices</td>
</tr>
<tr>
<td>Developing new policies and practices</td>
<td></td>
</tr>
<tr>
<td><strong>Stage 3—Solidification and Assessment</strong></td>
<td></td>
</tr>
<tr>
<td>Solidifying leadership and staffing</td>
<td>Participate in establishing criteria and procedures for assessing staff effectiveness</td>
</tr>
<tr>
<td>Assessing the new strategies and structures</td>
<td>Monitor the new culture and recommend approaches to strengthen it</td>
</tr>
<tr>
<td>Assessing the new culture</td>
<td>Participate in stakeholder satisfaction</td>
</tr>
<tr>
<td>Assessing the concerns of stakeholders</td>
<td>Assist in developing and implementing plans for continuous adjustment and learning</td>
</tr>
<tr>
<td>Revising as needed</td>
<td></td>
</tr>
<tr>
<td>Learning from the process</td>
<td></td>
</tr>
</tbody>
</table>

A low-cost strategy has several links to HR planning. The first has to do with productivity. A common misconception about low-cost strategies is that they inevitably require cutting labor costs. On the contrary, there are several good examples of companies that pay their employees “top dollar,” but gain back cost advantages because of excellent productivity. That is, they get a terrific “bang for the buck.” Either they produce more from the workforce they have, or they can produce the same amount with a smaller workforce. Starbucks is an often-recognized example of a company that pays its employees among the highest wages in its industry, yet still has the lowest overall costs among all competitors. This is because highly motivated employees can often work more efficiently, ensure better quality, eliminate waste, and provide better service.

The second way that low-cost strategies are linked to HR pertains to outsourcing. In some cases, companies seeking low cost may consider contracting with an external partner that can perform particular activities or services as well (or better) at a lower cost. This decision directly links strategic planning to human resources planning. Decisions such as these often result in layoffs, transfers, and the like. As noted before, organizations need to have a clear understanding of their core processes and skills in order to make these decisions. Too often, firms approach outsourcing decisions based on costs alone, but this can lead to detrimental effects in the long run if core skills and capabilities are eroded.

**Differentiation Strategy: Compete on Value Added**

While decreasing costs is one important way to enhance customer value, another involves providing something unique and distinctive to customers. A differentiation strategy is often based on high product quality, innovative features, speed to market, or superior service. Ritz-Carlton’s commitment to quality and luxury, FedEx’s focus on speed and flexible delivery, Neiman Marcus’s commitment to fashion and customer service, and Sony’s emphasis on innovation and product development are all easily identifiable examples of differentiation strategies.

Each of these strategies is rooted in the management of human resources. Companies that focus on service, for example, need to identify and support ways to empower employees to serve customers better. In contrast to the company that emphasizes low cost and efficiencies, you may find that differentiating companies will bend the rules a bit more, allow more flexibility to let you “have it your way,” and customize products and services around the customer’s particular needs. In place of rigid rules, service-oriented companies often try to embed their values in the cultural values of the company. David Pace, executive vice president of partner resources at Starbucks, noted that the key feature he looks for in new employees is “discernment,” the ability to make good decisions on their own.

**Functional Strategy: Ensuring Alignment**

In addition to formulating corporate and business-level strategies, managers also need to “translate” strategic priorities into functional areas of the organization (such as marketing, manufacturing, human resources, and the like). This involves all aspects of the business, but in particular there needs to be a clear alignment between HR and the requirements of an organization’s strategy. In this regard, HR policies and practices need to achieve two types of fit: external and internal.”18
External Fit/Alignment

External fit (or external alignment) focuses on the connection between the business objectives and the major initiatives in HR. For example, as noted earlier, if a company’s strategy focuses on achieving low cost, HR policies and practices need to reinforce this idea by reinforcing efficient and reliable behavior, enhanced productivity, and the like. On the other hand, if the organization competes through innovation and new product development, then HR policies and practices would be more aligned with the notion of enabling creating creativity and flexibility. Highlights in HRM 4 shows the external fit between major business objectives and HR imperatives at Continental Airlines.

Internal Fit/Alignment

In addition to external alignment or fit, managers need to ensure that HR practices are all aligned with one another internally to establish a configuration that is mutually reinforcing. Job design, staffing, training, performance appraisal, and compensation—the entire range of HR practices—need to focus on the same workforce objectives (such as efficiency, creativity, and loyalty). Unfortunately, often one HR practice, such as training, might be focused on teamwork and sharing, while another HR practice, such as appraisal and compensation programs, reinforces the ideas of individual achievement. Charles Schwab and Company, for example, faced this very situation. The company has a reputation in the financial services industry for developing a culture of teamwork that has been important to its strategy. However, when it changed its compensation strategy to provide more rewards to high-performing brokers, it ran into a potential problem of sending mixed signals to employees: Which is more important, teamwork or individual high flyers?29

While we raise the issue of alignment and fit here as an element of strategy formulation, it clearly links directly to strategy implementation as well. At the end of this chapter, we raise the issue again in the context of evaluating and assessing the success of strategic planning.

Step Five: Strategy Implementation

As the old saying goes, “Well begun is half done.” But only half. Like any plan, formulating the appropriate strategy is not enough. Managers must also ensure that the new plans are implemented effectively. Recently organizations have been paying more attention to implementation and execution. As Larry Bossidy, the former CEO of Honeywell, noted, “My job these days is to restore the discipline of execution to a company that had lost it. Many people regard execution as detail work that’s beneath the dignity of a business leader. That’s wrong. To the contrary, it’s the leader’s most important job.”20

Figure 2.8 shows the now classic 7-S framework and reveals that human resources management is instrumental to almost every aspect of strategy implementation, whether it pertains to structure, systems, style, skills, staff, or shared values. While strategy lays out the route that the organization will take in the future, organizational structure is the framework in which activities of the organization members are coordinated.
Achieving Strategic Fit at Continental Airlines

**Continental Airlines**

**The “Go Forward” Plan**

**WORKING TOGETHER**
- Focus on safer work environment
- Make payroll and benefit programs easy to use
- Establish frontline supervisors as leaders and credible source of information
- Open, honest, direct communication of information with all employees
- Compensation that is fair to the employees and fair to the company
- All employees treat each other with dignity and respect

**MAKE RELIABILITY A REALITY**
- Perform in top 3 (out of 10) airlines on key customer/DOT metrics
- On-time arrivals/departures
- Baggage
- Complaints
- Continue to improve our image
- Clean airplanes
- Refurbish planes
- Upgrade Pres. Clubs
- Upgrade advertising/sponsorships
- Improve Trans-Atlantic product
- Complete new image upgrade
- Enhance product with low-cost improvements

**FLY TO WIN**
- Allocate flying to maximize profit
- Grow hubs in IAH, EWR, CLE
- Grow Europe and Air Mic
- Improve customer mix
- Backpacks and flipflops to coats and ties
- Align travel agents and sales force
- Develop an alliance network across the Atlantic
- Aggressively eliminate non-value-added costs

**FUND THE FUTURE**
- Eliminate excess lease/interest expense
- Develop and implement five-year fleet plan
- Acquire sufficient real estate in our hubs to support growth
- Build cash balances to achieve long-term stability
- Eliminate GECC covenants
- Reduce interest expense, own our markets, and lay foundation for growth

Source: Company document.
If the strategy requires redeployment or reorganization of employees, HR will be intimately involved. Closely related to structure are systems and processes. These include formal and informal procedures that govern everyday activity. As organizations consider reengineering and process redesign to implement strategies, HR helps ensure that the best workflow models are in place and—importantly—that employees are involved in sharing their advice.

Shared values were discussed earlier in the chapter as a guiding parameter for strategic planning. They arise again as an important issue in implementation as well. Strategic change often requires employees and managers to modify, or abandon, their old ways of doing things. HR managers play a central role as guardians of the corporate culture, the principles on which the company is founded, the fundamental ideas around which the business is built. This is tightly connected to the issue of style, which refers not only to the leadership approach of top managers, but also the way in which employees present themselves to the outside world (to suppliers, customers, and so on.).

Skills and staff relate directly to the concerns of human resources management and point to the critical role that HR plays in strategy implementation. At a fundamental level, HR’s role in strategy implementation focuses on reconciling (1) human resources demanded and (2) human resources available.
Taking Action: Reconciling Supply and Demand

Through HRP, organizations strive for a proper balance between demand considerations and supply considerations. Demand considerations are based on forecasted trends in business activity. Supply considerations involve determining where and how candidates with the required qualifications can be found to fill vacancies. Because of the difficulty in locating applicants for the increasing number of jobs that require advanced training, this aspect of planning has been receiving a great deal more attention. Greater planning effort is also needed in recruiting members of protected classes for managerial jobs and technical jobs that require advanced levels of education.

In an effort to meet the demand for human resources, organizations have several staffing possibilities, including hiring full-time employees, having current employees work overtime, recalling laid-off workers, and using temporary employees. However, when forecasts show a surplus of employees, organizations may restrict hiring; reduce work hours; institute work sharing; or consider layoffs, demotions, and/or terminations. Additionally, over time organizations may try to reduce their workforce by relying on attrition (a gradual reduction of employees through resignations, retirements, and deaths). Over the past two decades, early retirements have become a more and more common means for organizations to reduce excess labor supply. Organizations as diverse as state colleges, healthcare facilities, and travel companies encourage employees to accept early retirement by offering “sweetened” retirement benefits. The various types of benefits are discussed in Chapter 11.

Organizational Downsizing, Outsourcing, and Offshoring

As discussed in Chapter 1, organizations have undertaken the extremely painful task of downsizing and restructuring over the past decade to reduce “head count.” Because of either economic or competitive pressures, organizations have found themselves with too many employees or with employees who have the wrong kinds of skills. In an effort to reconcile labor supply and demand considerations, companies such as Motorola, Corning, and Hewlett-Packard have eliminated thousands of jobs. These job cuts are not simply restricted to hourly workers. Technical, professional, and managerial positions have been (and are still being) eliminated at an unprecedented rate. In many cases, the move is part of a longer-term process of restructuring to take advantage of new technology, corporate partnerships, and cost minimization.

Making Layoff Decisions

Decisions about employee layoffs are usually based on seniority and/or performance. In some organizations, especially those with labor agreements, seniority may be the primary consideration. In other organizations, such factors as ability and fitness may take precedence over seniority in determining layoffs.

In the case of unionized organizations, the criteria for determining an employee’s eligibility for layoff are typically set forth in the union agreement. As a rule, seniority on the job receives significant weight in determining which employees are laid off first. Similar provisions in the union agreement provide for the right of employees to be recalled for jobs that they are still qualified to perform. Organizational policy, as
well as provisions in the labor agreement, should therefore establish and define clearly the employment rights of each individual and the basis on which layoff selections will be made and reemployment effected. The rights of employees during lay-offs, the conditions concerning their eligibility for recall, and their obligations in accepting recall should also be clarified. It is common for labor agreements to preserve the reemployment rights of employees laid off for periods of up to two years, providing that they do not refuse to return to work if recalled sooner.

It has become customary, however, for employers to give some degree of recognition to seniority even among employees who are not unionized. Unions generally advocate recognition of seniority because they feel that their members should be entitled to certain rights proportionate to the years they have invested in their jobs. Nevertheless, whenever seniority provides a basis for determining or even influencing HR decisions, the discretion of management is reduced accordingly. One of the major disadvantages of overemphasizing seniority is that the less-competent employees receive the same rewards and security as the more-competent ones. Also, the practice of using seniority as the basis for deciding which workers to lay off may well have a disparate impact on women and minority workers, who often have less seniority than other groups.

In cases where economic conditions have brought about layoffs, employees who were let go while in good standing may be recalled to their jobs when the economic outlook brightens and job openings occur. However, in many cases these new jobs require a different set of skills than the jobs they replace. Identifying individuals for these jobs can be accomplished by searching among previous employees or among current employees who can be transferred, but frequently it requires searching externally in the broader labor market.

**Step Six: Evaluation and Assessment**

At one level, it might seem that assessing effectiveness is the final step in the planning process. That is true. But it is also the first step. Planning is cyclical, of course, and while we’ve somewhat conveniently placed evaluation at the end, it actually provides the inputs to the next cycle in the planning process. Issues of measurement, benchmarking, alignment, fit, and flexibility are central to the evaluation process.

**Evaluation and Assessment Issues**

In order to evaluate their performance, firms need to establish a set of parameters that focus on the “desired outcomes” of strategic planning, as well as the metrics they will use to monitor how well the firm delivers against those outcomes. Because strategic management is ultimately aimed at creating a competitive advantage, many firms evaluate their performance against other firms. **Benchmarking** is the process of identifying “best practices” in a given area—say, productivity, logistics, brand management, training, and so on—and then comparing your practices and performance to those of other companies. To accomplish this, a benchmarking team...
would collect information on its own company’s operations and those of the other firm in order to determine gaps. The gaps help determine the causes of performance differences, and ultimately the team would map out a set of best practices that lead to world-class performance.

Interestingly, the target company for benchmarking does not need to be a competitor. For example, when Xerox wanted to learn about excellent customer service, it benchmarked L. L. Bean. By working with noncompeting companies, Xerox was able to get access to information a competitor would not divulge.

In the context of HR strategy, metrics fall into two basic categories: human capital metrics and HR metrics. Human capital metrics assess aspects of the workforce, while HR metrics assess the performance of the HR function itself. The Saratoga Institute publishes the annual *Human Capital Benchmarking Report*, which includes benchmarking information from almost 900 companies (see Highlights in HRM 5). Clients can use the information from studies of such areas as pay structure, return on investment per employee, turnover rates, and cost-per-hire and time-to-fill for key employees. This kind of detailed information clarifies potential bases of competitive advantage and reveals a path for developing future HR strategies.

### Measuring Strategic Alignment

Earlier in the chapter, we discussed the importance of strategic alignment and fit as an element of strategy formulation and implementation. As an element of evaluation, some very useful techniques help managers assess the extent to which they have achieved these objectives.

### Strategy Mapping and the Balanced Scorecard

One of the most enthusiastically adopted tools for mapping a firm’s strategy in order to ensure strategic alignment is the **Balanced Scorecard (BSC)**. Developed by Harvard professors Robert Kaplan and David Norton, the BSC is a framework that helps managers translate strategic goals into operational objectives. The model has four related cells: (1) financial, (2) customer, (3) processes, and (4) learning. The logic of the BSC is firmly rooted in human resources management. People management and learning help organizations improve their internal processes and provide excellent customer service. Internal processes—product development, service, and the like—are critical for creating customer satisfaction and loyalty, and they are also important for ensuring productivity to contain costs for better financial performance. Customer value creation, in turn, drives up revenues, which enhances profitability.

Figure 2.9 shows how this might work at Starbucks. In each cell, Starbucks would identify the key metrics that help translate strategic goals to operational imperatives. For example, under customer metrics, Starbucks might look at percentage of repeat customers, number of new customers, growth rate, and the like. Under people metrics, managers might measure the numbers of suggestions provided by employees, participation in Starbucks’ stock sharing program, employee turnover, training hours spent, and the like. Each of these cells links vertically. People management issues such as rewards, training, and suggestions can be linked to efficient processes (brewing the perfect cup, delivering top-notch customer service, and so forth). These processes then lead to better customer loyalty and growth. Growth and customer loyalty in turn lead to higher profitability and market value.
The Top Ten Measures of Human Capital

The top ten areas to measure, as recommended by Jac Fitz-enz, chair of the Saratoga Institute (now part of Spherion’s Human Capital Consulting Group), in an issue of Workforce magazine (http://www.workforce.com), won’t all apply to your company, but some will:

1. **Your most important issues.** These are the targets of all lower-level measures. Focus on them and ensure that your metrics lead in a direct line to them.

2. **Human capital value added.** How do your workers optimize themselves for the good of the company and for themselves? This is the primary measure of an individual’s contribution to profitability.

3. **Human capital ROI.** This is the ratio of dollars spent on pay and benefits to an adjusted profit figure.

4. **Separation cost.** How many people are leaving? From which departments? What does it cost the company? The average cost of separation for an employee is at least six months’ equivalent of revenue per employee.

5. **Voluntary separation rate.** Lost personnel equal potential lost opportunity, lost revenue, and the cost of workers having to fill the gaps under greater stress. Cutting the separation rate saves the cost of hiring and keeps customer service quality high.

6. **Total labor-cost/revenue percentage.** This is total benefits and compensation cost as a percentage of organizational revenue and shows how much of what you are taking in through revenue goes to support the company’s total labor cost, including temporary, seasonal, and contract or contingent workers. This metric can help you track changes in your workforce. Best approach: Compare it to your revenue factor and compensation, benefits, and contingent off-payroll costs. If the metric is rising, determine whether compensation or benefits costs are up or revenue is down. This will help you decide what actions to take.

7. **Total compensation/revenue percentage.** This is the percentage of the company’s revenues allocated to the direct costs of employees. It excludes costs for off-payroll employees who receive a 1099 form (as does the metric in item 6). Before creating strategies to address concerns, compare this metric to your revenue factor, compensation costs, and benefits costs to analyze what is happening with workers.

8. **Training investment factor.** Basic skills are crucial: Workers who cannot read, write, do simple calculations, or talk intelligently with customers need to have these skill deficiencies addressed.

9. **Time to start.** Recruitment will continue to be a challenge. The amount of the time it takes from approval of a job requisition until the person is on the job is a strategic indicator of revenue production.

10. **Revenue factor.** This is the basic measure understood by managers.

Measuring Internal Fit

Recall that internal fit means that HR practices are all aligned with one another to establish a configuration that is mutually reinforcing. Figure 2.10 shows an example of how organizations can assess the internal fit of their HR practices. There are essentially three steps. First, managers need to identify the key workforce objectives they hope to achieve. Often this information can come from the people/learning cell of the Balanced Scorecard, and might include loyalty, customer service, productivity, and creativity. Second, managers would identify each of the HR practices used to elicit or reinforce those workforce objectives (job design, staffing, training, appraisal, compensation, and so on). Third, managers would evaluate each HR practice on a scale of −5 (not supportive) to 5 (supportive). By tallying up the ratings across managers, organizations can get a very clear idea of which HR practices are working together to achieve the workforce objectives, and which are not.

An important caveat to this analysis is that internal fit is a necessary, but insufficient, cause of strategic alignment. A company could have nearly perfect alignment among its HR practices, and they still might not be aligned with the competitive strategy. For that reason, it is important for managers to assess both internal fit and external alignment.
Ensuring Strategic Flexibility for the Future

Apart from the need to establish and measure fit between HR and strategy, HR is also focused on ensuring flexibility and agility when the environment changes. Ultimately, successful HRP helps increase organizational capability—the capacity of the organization to continuously act and change in pursuit of sustainable competitive advantage.24

Flexibility can be achieved in two primary ways: coordination flexibility and resource flexibility. Coordination flexibility occurs through rapid reallocation of resources to new or changing needs. Through HRP, managers can anticipate upcoming events, keep abreast of changes in legal regulations, forecast economic trends, recognize competitor moves, and the like. With advance notice, managers can move people into and out of jobs, retrain them for new skill requirements, and modify the kinds of incentives they use. Use of a contingency workforce composed of part-timers, temporary employees, and external partners also helps achieve coordination.
flexibility. Resource flexibility, on the other hand, results from having people who can do many different things in different ways. Cross-training, job rotations, team-based work modes, and the like are all focused on establishing a flexible workforce.

We will draw on these ideas throughout the text. But at this point we want to close the chapter by emphasizing that strategic planning is a process designed to ensure superior performance today, as well as establishing the capability and agility to respond tomorrow. As the great hockey player Wayne Gretsky used to say, “I don’t skate to where the puck is. I skate to where the puck is going to be.”

**SUMMARY**

Strategic human resources management (SHRM) integrates strategic planning and HR planning. It can be thought of as the pattern of human resources deployments and activities that enable an organization to achieve its strategic goals. HR planning and strategies becomes especially critical when organizations consider global strategies, mergers, relocation of plants, innovation, and downsizing, or when dramatic shifts in the composition of the labor force are occurring.

Analyzing the firm’s competitive environment is central to strategic planning. The competitive environment includes the specific organizations with which the firm interacts. Firms analyze the competitive environment in order to adapt to or influence the nature of competition.

Conducting an internal analysis to gauge the firm’s strengths and weaknesses involves looking a firm’s “three Cs”—its culture, competencies, and composition. An internal analysis enables strategic decision makers to inventory the organization’s skills and resources as well as their performance levels.

An organization’s success increasingly depends on the knowledge, skills, and abilities of employees, particularly as they help establish a set of core competencies that distinguish an organization from its competitors. When employees’ talents are valuable, rare, difficult to imitate, and organized, an organization can achieve a sustained competitive advantage through people.

HRP is a systematic process that involves forecasting demand for labor, performing supply analysis, and balancing supply and demand considerations. Forecasting demand requires using either quantitative or qualitative methods to identify the number and type of people needed to meet organizational objectives. Supply analysis involves determining whether sufficient employees are available within the organization to meet demand and also whether potential employees are available on the job market. Reconciling supply and demand requires a host of activities, including internal and external recruitment.

As organizations plan for their future, top management and strategic planners must recognize that strategic-planning decisions affect—and are affected by—HR functions. On one hand, HRP plays a reactive role in ensuring that the right number and type of employees are available to implement a chosen business plan. On the other hand, HRP can proactively identify and initiate programs needed to develop organizational capabilities on which future strategies can be built. HRP and strategic planning tend to be most effective when there is a reciprocal relationship between the two processes.
Formulating an HR strategy is only half of the HR battle: The strategy must also be implemented. Employment forecasts must be reconciled against the internal and the external supplies of labor the firm faces. This can include hiring, downsizing, outsourcing, and off-shoring. If there is a labor shortage, the firm might have to reformulate its long- and short-term strategic plans.

Firms need to establish a set of parameters that focus on the “desired outcomes” of strategic planning, as well as the metrics they will use to monitor how well the firm delivers against those outcomes. Issues of measurement, benchmarking, alignment, fit, and flexibility are central to the evaluation process. Firms use benchmarking, strategy mapping, and the Balanced Scorecard (BSC) as tools to gauge their outcomes.

**KEY TERMS**

- Balanced Scorecard (BSC)
- benchmarking
- core competencies
- core values
- cultural audits
- environmental scanning
- human resources planning (HRP)
- management forecasts
- Markov analysis
- mission
- organizational capability
- replacement charts
- skill inventories
- staffing tables
- strategic human resources
- management (SHRM)
- strategic planning
- strategic vision
- succession planning
- SWOT analysis
- trend analysis
- value creation

**DISCUSSION QUESTIONS**

1. Identify the three key elements of the human resources planning model and discuss the relationships among them.
2. What competitive environmental forces influence the firm’s strategy?
3. What criteria must be met if firms are to achieve a competitive advantage through their employees?
4. Which approach do you think should be relied on more heavily for strategy formulation—the quantitative or qualitative approach?
5. Explain the difference between a firm’s corporate strategy and business strategy. Why do firms need to look at both aspects?
6. What steps does the firm need to take to reconcile labor supply and labor demand?
7. Why is organizational capability important to firm and how can HR managers enhance it?
Customizing HR for Different Types of Human Capital

Part of strategic planning in HR is mapping an organization’s human capital. When we look at the strategic value of a person’s skills as well as their uniqueness, we soon discover that organizations comprise different kinds of workers who have very different kinds of skills. Some are core knowledge workers; some are more traditional job-based employees; some are contract workers; and some are external partners. In this context, it is unlikely that we would manage all of these employees the same way (as much as we might want to for fairness). There are differences in HR practices for different groups. That’s not bad, but it makes the job of HR managers more difficult.

Assignment

The following are descriptions of three different employees. How would you characterize each worker? What role does each play when it comes to the organization’s strategy?

Andrea Bascomb is a highly talented computer programmer for MiniFluff, Inc. She is among the elite set of engineers in the computer industry that is doing leading-edge work on advanced computer modeling. In truth, CEO Bill Ding believes that the future of the company rests on the innovative work that Andrea and her team are doing. He worries that someone might lure Andrea away to work for them. So he wants to give her all the room she needs to grow and stay committed to MiniFluff.

Calvin Duff is a salesperson on the retail side of MiniFluff. He has daily contact with customers and is responsible for making sales and communicating with service personnel. Make no mistake: To many customers, Calvin and his co-workers are the “face” of MiniFluff. Always on the lookout for a better situation, Calvin has thought about working for PeachTree Computing, MiniFluff’s main competitor. In truth, other salespeople have found that they can leave MiniFluff and get “up to speed” easily at other firms. Their skills are very transferable and the transition is not difficult. Bill Ding and other managers at MiniFluff recognize this fact, so they try to keep salespeople loyal and productive, recognizing that many of them do eventually leave.

Evelyn Frank is a part-time secretary for MicroFluff. She handles routine typing and filing work for the company, particularly in peak periods in the summer and around the holidays. She usually works for a few weeks at a time and then takes time off. The executives at MicroFluff have considered either outsourcing the job to an agency or automating it through a new computer system. But for now things are steady.

BIZFLIX EXERCISES

U-571: Setting Strategy

Watch the scene from U-571. It shows several aspects of strategic planning described earlier in this chapter. This action-packed World War II thriller shows a U.S. submarine crew’s efforts to retrieve an Enigma encryption device from a disabled German submarine. After the crew gets the device, a German vessel torpedoes and sinks the U.S. submarine. The survivors must now use the disabled German submarine to escape
Mazda Motors UK (United Kingdom) is only too aware of the importance of staying up to date with competitor developments and so its HR department conducts a benchmarking analysis every two years. This involves comparing its pay and benefits packages against twenty-two blue-chip companies, including other automotive firms, and against a more general service industry database. The fact that Mazda Motors UK gives every employee a car was found to be a major differentiating factor from some competitors, which provide a car only for employees at certain levels. Its benefits package, which is the same for all of its ninety employees, was also found to be much flatter than usual.

Jemma Galbraith-Marten, HR officer at Mazda Motors UK, says: “You must benchmark regularly because current information may not be valid in a few years’ time. We’ve found the exercise very useful in terms of recognizing our general position in the marketplace and it has fuelled a lot of internal debate about how we recognize and reward our employees. It has helped us to set grades within the company and to pitch effectively for recruitment. It has also stimulated conversations about whether to provide a flex scheme because, in view of our benefits package, some individuals may find that more flexibility better addresses work-life balance issues.”

What to Watch for and Ask Yourself

• Does Lt. Tyler analyze the submarine’s external environment? Does he engage in environmental scanning as described earlier in this chapter?
• What is Lt. Tyler’s assessment of the submarine’s strengths and weaknesses?
• Does Lt. Tyler consider threats and opportunities in forming his strategic plan? Has he done a SWOT analysis as described earlier in this chapter?

QUESTIONS

1. What do you think of Mazda Motors UK’s efforts to benchmark its benefits package on an annual basis?
2. As a prospective employee, would you have more interest in working for a company that conducts such benchmarking?
3. What are the benefits and costs associated with giving employees a free car to drive? In what way does it give Mazda a competitive edge in terms of recruiting and retaining employees?
4. Should Mazda offer different benefits for employees who, say, use public transportation or would prefer other benefits such as flextime? How do you think such an alternate package could be crafted?

With 61,000 workers in more than ninety countries, Dole Food Company has talent all over the world. Only a few hundred of those employees are in top management at the 151-year-old company headquartered in Westlake Village, California. Trouble is, Dole doesn’t have comprehensive knowledge of who these managers are or what they can do. If a key job opens up in North America, the business unit leader wouldn’t know if the perfect candidate worked in another Dole unit in South America. Dole has no way to match its top managerial talent with its executive needs.

But that is changing. The highly decentralized company is launching a succession-planning process, supported by web-based software, through which Dole executives hope to rectify their inability to promote the best and the brightest across the corporation. The process itself requires a change of culture and could become an agent for further culture change. “The idea of succession planning is contrary to being highly decentralized,” says Sue Hagen, vice president of HR for North American operations, who led the effort.

Hagen talked informally to all corporate executives and the leaders and staffs of each business unit to generate consensus for succession planning for corporate positions—corporate officers, business unit presidents, and their direct reports. The initial group would be about 100, she says. Next year, another few hundred will be included.

The reaction was mostly positive, Hagen says. Hagen’s next step was to hold a series of in-depth interviews with the executives to determine which succession-planning processes were needed and how often they should be conducted. The goal was to reflect as much of their thinking as possible. “One division wanted to review succession plans on their people six times a year. Another didn’t want to do it at all,” she says. Hagen compromised: Succession planning will be conducted twice a year. She also identified four competencies on which everyone would be evaluated: accountability, business acumen, multifunctionality (cross-training), and vision/originality.

Many HRMS software suites have an optional succession-planning module, but neither Dole nor its business units have an HRMS. Since most employees are farm or factory workers, there is not much need for the detailed information an HRMS provides, says Hagen. “It would be overkill.” In a way, the succession-planning software Dole adopted will become a mini-HRMS for top personnel, she adds.

Hagen also wanted an application service provider (ASP) model. Outsourcing, including payroll, is common at Dole. Hagen didn’t want to own and support technology, and she didn’t want the small corporate information technology staff to have to work on it.

The users of the system—top managers—access the program from the Web with a password. They fill out a resume, including career interests, and note any mobility restrictions. They assess themselves on the four competencies. When they are done, the system automatically notifies their manager, who does an assessment and indicates whether he or she thinks the individual could be promoted. The manager also assesses overall potential and the risk of losing the user. This assessment then goes automatically to the division head, then the divisional HR director, and then Hagen. Hagen will use the information to create a career development plan for each individ-
ual, including seminars she’ll organize. She’ll also direct business unit leaders to potential candidates in other units when they have appropriate openings. “The beauty is, for the first time we’ll have a database that ties together these talent metrics and can serve as a clearinghouse for people available for opportunities,” Hagen says.

Dole’s corporate management hopes all business units will eventually adopt similar succession-planning processes and software, Hagen says. “I view this as a pilot, a very visible pilot,” she says. “To get the buy-in of individual business units, we’ll show them that this was adopted by their senior management and that it works.”

QUESTIONS

1. Why do you think companies like Dole need succession planning?
2. Do you see any disadvantage of “automating” succession planning?


NOTES AND REFERENCES


Throughout this chapter we have emphasized that HRP depends on having an accurate picture of both the supply of and the demand for employees. Two factors, employee turnover and absenteeism, have a direct impact on HR planning strategy and recruitment processes. In this appendix, we provide a detailed discussion of turnover and absenteeism, methods for measuring them, and suggestions for managing their impact.

### Employee Turnover Rates

*Employee turnover* refers simply to the movement of employees out of an organization. It is often cited as one of the factors behind the failure of U.S. employee productivity rates to keep pace with those of foreign competitors. It is also one of the chief determinants of labor supply. Even if everything else about an organization stays the same, as employees turn over, its supply of labor goes down. This involves both direct and indirect costs to the organization.

### Computing the Turnover Rate

The U.S. Department of Labor suggests the following formula for computing turnover rates:

\[
\frac{\text{Number of separations during the month}}{\text{Total number of employees at midmonth}} \times 100
\]

Thus, if there were 25 separations during a month and the total number of employees at midmonth was 500, the turnover rate would be:

\[
\frac{25}{500} \times 100 = 5 \text{ percent}
\]

Turnover rates are computed on a regular basis to compare specific units such as departments, divisions, and work groups. In many cases, comparisons are made with
data provided by other organizations. The *Bureau of National Affairs Quarterly Report on Job Absence and Turnover* is a very good source of comparative turnover data.1

Another method of computing the turnover rate is one that reflects only the avoidable separations \((S)\). This rate is computed by subtracting unavoidable separations \((US)\)—for example, due to pregnancy, return to school, death, or marriage—from all separations. The formula for this method is as follows:

\[
\frac{S - US}{M} \times 100 = T \text{ (turnover rate)}
\]

where \(M\) represents the total number of employees at midmonth. For example, if there were 25 separations during a month, 5 of which were \(US\), and the total number of employees at midmonth \((M)\) was 500, the turnover rate would be:

\[
\frac{25 - 5}{500} \times 100 = 4 \text{ percent}
\]

In looking at the impact of turnover on HR planning and recruitment, it is vitally important to recognize that quantitative rates of turnover are not the only factor to be considered. The *quality* of employees who leave an organization is equally important. If poor employees leave, what experts refer to as “functional turnover,” this can prove to be beneficial to the organization. The costs of keeping unproductive workers may be far more than the costs to recruit and train a new, more effective performer.

**Determining the Costs of Turnover**

Replacing an employee is time-consuming and expensive. Costs can generally be broken down into three categories: separation costs for the departing employee, replacement costs, and training costs for the new employee. These costs are conservatively estimated at two to three times the monthly salary of the departing employee, and they do not include indirect costs such as low productivity prior to quitting and lower morale and overtime for other employees because of the vacated job. Consequently, reducing turnover could result in significant savings to an organization. *Highlights in HRM 6* details one organization’s costs associated with the turnover of a single computer programmer. Note that the major expense is the cost involved in training a replacement.

**Employee Absenteeism Rates**

How frequently employees are absent from their work—the absenteeism rate—is also directly related to HR planning and recruitment. When employees miss work, the organization incurs direct costs of lost wages and decreased productivity. It is not uncommon for organizations to hire extra workers just to make up for the number of absences totaled across all employees. In addition to these direct costs, indirect costs may underlie excessive absenteeism. A certain amount of absenteeism is, of course, unavoidable. There will always be some who must be absent from work because of sickness, accidents, serious family problems, or other legitimate reasons. However, chronic absenteeism may signal deeper problems in the work environment.
CHAPTER 2  Strategy and Human Resources Planning

**Costs Associated with the Turnover of One Computer Programmer**

Turnover costs = Separation costs + Replacement costs + Training costs

**Separation costs**
1. Exit interview = cost for salary and benefits of both interviewer and departing employee during the exit interview = $30 + $30 = $60
2. Administrative and record-keeping action = $30
   Separation costs = $60 + $30 = $90

**Replacement costs**
1. Advertising for job opening = $2,500
2. Preemployment administrative functions and record-keeping action = $100
3. Selection interview = $250
4. Employment tests = $40
5. Meetings to discuss candidates (salary and benefits of managers while participating in meetings) = $250
   Replacement costs = $2,500 + $100 + $250 + $40 + $250 = $3,140

**Training costs**
1. Booklets, manuals, and reports = $50
2. Education = $240/day for new employee’s salary and benefits × 10 days of workshops, seminars, or courses = $2,400
3. One-to-one coaching = ($240/day per new employee + $240/day per staff coach or job expert) × 20 days of one-to-one coaching = $9,600
4. Salary and benefits of new employee until he or she gets “up to par” = $240/day for salary and benefits × 20 days = $4,800
   Training costs = $50 + $2,400 + $9,600 + $4,800 = $16,850

**Total turnover costs** = $90 + $3,140 + $16,850 = $20,080


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**Computing Absenteeism Rates**

Managers should determine the extent of the absenteeism problem, if any, by maintaining individual and departmental attendance records and by computing absenteeism rates. Although there is no universally accepted definition of “absence” or a standard formula for computing absenteeism rates, the method most frequently used is that recommended by the U.S. Department of Labor:
Number of worker-days lost through job absence during period \( \times \frac{100}{\text{Average number of employees} \times \text{number of workdays}} \)

If 300 worker-days are lost through job absence during a month having 25 scheduled working days at an organization that employs 500 workers, the absenteeism rate for that month is:

\[
\frac{300}{500 \times 25} \times 100 = 2.4 \text{ percent}
\]

The Department of Labor defines job absence as the failure of employees to report to work when their schedules require it, whether or not such failure to report is excused. Scheduled vacations, holidays, and prearranged leaves of absence are not counted as job absence.

**Comparing Absenteeism Data**

The Bureau of Labor Statistics of the U.S. Department of Labor receives data on job absences from the Current Population Survey of Households conducted by the Bureau of the Census, and analyses of these data are published periodically. These analyses permit the identification of problem areas—industries, occupations, or groups of workers with the highest incidence of absence or with rapidly increasing rates of absence. Comparison with other organizations may be made by referring to Bureau of Labor Statistics data reported in the *Monthly Labor Review* or by consulting such reporting services as the Bureau of National Affairs and Commerce Clearing House.

**Costs of Absenteeism**

Traditional accounting and information systems often do not generate data that reflect the costs of absenteeism. Consequently, their usefulness in HR planning is often limited. To accentuate the impact of absenteeism on organizational performance, managers should translate the data into dollar costs. A system for computing absenteeism costs for an individual organization is available. Organizations with computerized absence-reporting systems should find this additional information easy and inexpensive to generate. The cost of each person-hour lost to absenteeism is based on the hourly weighted-average salary, costs of employee benefits, supervisory costs, and incidental costs.

For example, XYZ Company, with 1,200 employees, has 78,000 person-hours lost to absenteeism; the total absence cost is $560,886. When this figure is divided by 1,200 employees, the cost per employee is $467.41. (In this example, we are assuming the absent workers are paid. If absent workers are not paid, their salary figures are omitted from the computation.)

**Absenteeism and HR Planning**

While an employer may find that the overall absenteeism rate and costs are within an acceptable range, it is still advisable to study the statistics to determine whether there are patterns in the data. Rarely does absenteeism spread itself evenly across an organization. It is very likely that employees in one area (or occupational group) may have
nearly perfect attendance records, while others in a different area may be absent frequently. By monitoring these differential attendance records, managers can assess where problems might exist and, more important, begin planning ways to resolve or improve the underlying causes. For example, incentives could be provided for perfect attendance. Alternatively, progressive discipline procedures might be used with employees having a record of recurring absenteeism.

By establishing a comprehensive absenteeism policy, Allen-Bradley cut absenteeism 83.5 percent in a twenty-five-month period. This reduced the strain on labor costs and increased productivity. Part of the company’s attendance policy reads:

It is important to the successful operation of the Motion Control Division that employees be at work each scheduled workday. Each employee is performing an important set of tasks or activities. Excessive and/or avoidable absenteeism places unfair burdens on co-workers and increases the company’s cost of doing business by disruption of work schedules, [creating] inefficiency and waste, delays, costly overtime, job pressures and customer complaints.³

NOTES AND REFERENCES


2. The looseleaf publications of these organizations are sources of invaluable information for managers and HR professionals. These publications may be found in most libraries containing business reference books.