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HUMAN RESOURCE STRATEGY
Chapter 2
of

HUMAN RESOURCE MANAGEMENT: AN ECONOMIC APPROACH
by

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HUMAN RESOURCE MANAGEMENT; AN ECONOMIC APPROACH

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CHAPTER TWO: HUMAN RESOURCE STRATEGY

Concepts of the firm as an organization, capital hiring labor, employees as stakeholders, the employment contract, and the efficiency of human resource policies, which were presented in the opening chapter of this volume, imply that firms consciously formulate and execute human resource strategies. In fact, it is only recently that concepts of human resource strategy have made their way into the academic literature and that the development of formal human resource strategy has come to be practiced by the firm[1]. An appropriate starting point for a discussion of this topic is the link between human resource strategy and business strategy.

Concepts of Business Strategy

The fundamental idea underlying business strategy is that the firm can chart its future[2]. It does so by developing a strategy for the business--strategy formulation--and by developing a strategy for achieving business objectives--strategy implementation. Stated differently, the firm attempts to determine where it wants to be at some point in the future and how it will get to that point. The firm's strategy typically is formalized in a written business plan. The very word "planning" implies a long-term focus, and written business plans typically identify a five-year strategy and set of objectives. A written business plan also typically includes an operating plan, which indicates what the firm's objectives are in the short-run--usually one year.

The business strategy literature identifies a well-established framework for strategy formulation, which begins with an environmental analysis[3]. Key dimensions of the environment, or environmental forces, are the subject of this analysis; these include economic, social, political, legal, and technological forces. Changes in one or more of these forces may provide certain opportunities for the firm, but may also pose threats to it. For example, an analysis of the macroeconomic environment conducted by a real estate firm, such as Broad Inc., which leads to a forecast of economic expansion, may result in the identification of new opportunities for land acquisition, real estate development and commercial construction, such as of shopping centers or office complexes. In contrast, a forecast of economic contraction (that is, recession) reached by Broad, Inc. may result in the identification of threats to this real estate firm's completion of current development projects, and may also cause it to scale back its plans for future land acquisition.

At the industry level, competitor analysis is especially important to the firm's identification of future business opportunities and threats[4]. To illustrate, a computer software firm, such as Microsoft, which saw few threats posed to its domination of the market for computer software in the 1980s, may identify several new entrants to the industry in the 1990s, with consequent threats to its dominant market position. Major manufacturers of mainframe computers, such as International Business Machines Corporation (IBM) and Digital Equipment Corporation (DEC), have increasingly experienced threats to their businesses from manufacturers of personal computers (such as Compaq) and computer workstations (such as Sun Workstations), which serve as substitutes for some of the functions traditionally provided by mainframe computers. Determining the future rate-threat of such substitution is an important part of the business planning process at IBM and DEC in the 1990s.

With respect to legal forces, pharmaceutical firms such as Merck, Inc. and Pfizer, Inc. conduct environmental analyses aimed at forecasting whether or not the "abortion pill," known as UR-486, will be legalized for entry into and production in the U.S. If so, certain opportunities for production, distribution, and joint venturing with the French manufacturer of UR-486 may present themselves to Merck and Pfizer. At the same time, these two pharmaceutical firms are analyzing the legal environment for the purpose of forecasting whether or not price controls or other restrictions on the production and sale of prescription drugs will be enacted by the U.S. government. If so, certain threats to the pricing of and revenue received from the sales of prescription drugs produced by these firms will manifest themselves, and these firms' business plans will indicate how they plan to respond to such threats.

The process of formulating business strategy also includes an analysis of the particular firm's internal or organizational strengths and weaknesses[5]. This type of analysis addresses such questions as, "Is the firm properly organized to respond to its market environment?," "Are the jobs required to get the firm's work performed properly organized?," "Does the firm have the right people with the right skills to perform the jobs?," "Do the firm's decision-making processes fit the requirements of its business?," and "Is the firm's leadership style appropriately suited to the requirements of the business?" The firm engages in this process of organizational strength-weakness analysis in order to determine what changes in its organization, jobs, people, decision-making processes, and leadership style should be made in order to more properly align the firm with its market-competitive environment, as identified in the written business plan. Clearly, the process of organizational strength-weakness analysis involves the consideration of several human resource management aspects and characteristics of the business.

<u>Changing Influences on Business Strategy</u>

The fundamental idea underlying human resource strategy for the firm is that firm should be able to identify a human resource strategy which is closely linked to its business strategy, helps the firm to take advantage of the market opportunities available to it, and enhances the firms' internal organizational strengths[6]. In other words, human resource strategy should be fundamentally aimed at and be a tool for implementing the business strategy formulated by the firm.

The notion that human resource strategy can contribute to achievement of the firm's strategic objectives is of relatively recent origin. Until recently, "human resources" was conceived of largely as a functional unit or department of the business which was responsible for devising policies, programs, and practices to recruit, hire, train, appraise, reward, counsel, discipline, and separate employees[7]. In other words, this traditional "personnel" function was heavily, if not exclusively, process-oriented and the firm's expenditures on the function were treated exclusively as a cost. The modern human resource function in business enterprises is increasingly being treated as an integral part of the business or line management, rather than as a separate unit or department, and is increasingly being viewed as having an investment or asset component, not just a cost component. In this regard, senior human resource executives are increasingly being called upon to serve as business partners and decreasingly as the provider of employee services and protector of employee rights[8].

Why has this occurred? What factors help to explain why the traditional, relatively narrow, process-oriented personnel function has evolved into a broader, more fundamentally business-oriented human resource function that focuses on the development of the core competencies of the firm and the execution of the firm's business strategy? One explanation of this evolution stems from an examination of fundamental ideas and disciplines that have contributed to strategic business planning. As shown in Figure 1, certain disciplines and functions have had important influences on the process of strategic business planning during selected eras.

The first of these disciplines/functions is economics, which strongly influenced strategic business planning during the 1960s[9]. This influence stemmed from the role of economics and economists during the late 1940s and early 1950s in the development of national income and product accounting through which a nation could determine its current and forecast its future economic output and performance. The now popular index of Gross National Product (GNP) is grounded in macroeconomics and serves as a way of measuring the rate at which a nation's economy is growing or declining. Business firms, which began seriously to be interested in strategic planning during the late 1950s and early 1960s, adopted the tools of macroeconomic accounting and forecasting, primarily econometric modeling, to develop forecasts of sales revenue and production in the specific industries in which they operated[10]. The typical written business plan which resulted from applications of macroeconomics to business strategy went on to identify the forecasted position of the firm in its industry in terms of its share of industry production and sales. Additional indicators of the growing role of economics and economists in strategic business planning during the 1960s included the founding of the National Association of Business Economists in 1962, the emergence and rapid growth of economics newsletters containing macroeconomic forecasts which became heavily subscribed to by business organizations, and the creation by business organizations of internal economic analysis and planning groups and the hiring of economists to staff them. In short, economics was the dominant disciplinary influence on strategic business planning during the

1960s.

The second discipline/function which came to have a major impact on strategic business planning was marketing. In the late 1960s, the Boston Consulting Group and certain marketing scholars developed a matrix approach to business strategy which combined two main elements, namely, market share and operating margin[11]. Market share refers to the proportion of an industry, product group, or individual product's sales volume (or revenue) obtained by a particular firm. For example, in the late 1960s, the Xerox Corporation had about an 85% share of the sales volume of photoelectric copiers. At about the same time, the General Motors Corporation had about a 51% share of the sales volume of automobiles in the United States. More recently, Merck & Co. has had approximately an 11% share of the sales volume of pharmaceutical products worldwide. Operating margin refers to the profit earned by a company from the sale of all of its products, a group of products or an individual product. To illustrate, during the 1980s Merck & Co. achieved a 23% profit rate on sales of its pharmaceutical products worldwide, and Hewlett-Packard achieved a 26% profit rate on sales of its line of printers.

The two-by-two matrix established by the combination of market share and operating margin led to well-known descriptions of companies that occupy particular cells in the matrix--for example, "star" to characterize a company with high market share and high operating margin, "dog" to characterize a company with low market share and low operating margin, "cash cow" to characterize a company with low market share and high operating margin, and "problem child" to characterize a company with high market share and low operating margin[12]. More to the point, the development of this matrix approach led marketing executives and specialists to take a major step forward in terms of their influence on strategic business planning, and marketing strategy became and important specialization in the academic study of marketing during the 1970s.

The third discipline/function which came to have a strong impact on business strategic planning was finance. Theoretical and empirical work done by finance scholars on such topics as capital asset pricing models and tests of efficient market hypotheses had major influences on business strategies (and thus firm behavior) during the 1980s. Of particular importance in this regard was portfolio theory, which placed key emphasis on the risk and the reward associated with the investment of assets in a particular business[13]. Following portfolio theory, the role of senior executives is to forecast the risks that the business will face in a future period, for example, five years, and to forecast the rewards that the business will obtain during the same future period; this may be thought of as the risk-to-reward ratio.

To illustrate, if senior executives of, say, an electronics manufacturing company forecast a rapidly rising risk-to-reward ratio five years into the future, the key action implied by this forecast is to reduce the company's investment in this business and consider investing its resources in another business or businesses. Indeed, if this company's forecast is for the risk-to-reward ratio to rise very rapidly during the next five years, then the attendant action implication is for the company to get out of or divest itself of its electronics manufacturing business. Relatedly, according to portfolio theory, this company should examine and forecast the risk-to-reward ratios in other businesses which it does not presently own, but which it may subsequently decide to invest in or acquire. The overall result of this application of portfolio theory may well be that our hypothetical company will, during the next five years, cease to manufacture electronic equipment and begin to manufacture other products or perhaps even own and operate service type businesses[14]. A real-world company which closely matches this hypothetical example is General Electric which, by the end of the 1980s, was no longer manufacturing electronic products but which owned and operated a major telecommunications business, the Radio Corporation of America (RCA)--which in turn owns and operates the National Broadcasting Company (NBC).

Many other examples of companies that have in effect used portfolio theory to guide their strategic planning processes can be cited. One of these is the Singer Company, which produced the first sewing machines in the United States and has long been thought of as a (or even "the") sewing machine company. But between the mid-1970s and the early 1980s, the Singer Company ceased to produce sewing machines for sale in markets in developed countries (though it continued to do so for sale in markets in developing countries), and became a producer of electronic guidance systems, satellite platforms, and weapons systems for the U.S. Department of Defense. In another case, Mobil Corporation, which has long been know as a major energy company, expanded its investment in its chemical business during the 1970s, acquired a can manufacturing business and a large retail department store chain during the 1970s, and made major investments in a real estate business during the 1980s. Later, Mobil divested itself of the can manufacturing business and the retail department store chain, following repeated and unsuccessful attempts to turn these businesses into profitable ventures.

Also during the 1980s, the pace at which portfolio theory was applied to strategic business decisions, especially acquisition and divestiture decisions, seemed to quicken as new forms of leveraged buyouts emerged. Those buyouts which were financed by so-called junk bonds became especially well-known (and, in some cases, notorious), and a whole new set of terms--for example, white knight, poison pill, greenmail--emerged to characterize the efforts of companies to ward off leveraged buyouts, especially the hostile takeover. Apart from the undeniably important question concerning the net benefit to an economy and a society of leveraged buyouts and related forms of financial intermediation, there can be little doubt that the discipline/function of finance had a major impact on strategic business planning during the 1980s, and that finance specialists and executives took a major step forward in terms of their influence on strategic business planning.

Human Resources and Business Strategy

If economics, marketing, and finance have all had major periods or eras of influence on strategic business planning, what factors help us understand why traditional (nonstrategic) personnel administration is apparently evolving into strategic human resource management, and why the discipline/function of human resources may have a major impact on strategic business planning during the 1990s? One such factor has been the growing international competition facing U.S. firms, the pace of which quickened markedly during the early 1980s.

The leading international competitor nation is this regard has been Japan, but what is especially important about the Japanese example for the advance of strategic human resource management is the "discovery," often reported by Chief Executive Officers and presidents of U.S. companies who have visited Japanese firms, that the Japanese firm has gained competitive advantage over the U.S. firm through its use of "people," that is, human resources, and not, it should be noted, through its particular brand of economic forecasting, marketing strategy or finance strategy. In case after case, the Japanese firm is said to have achieved competitive advantage by making more efficient use of its labor force, meaning that the Japanese firm attains higher quality products, a higher quantity of production, lower labor costs, and/or various combinations thereof, than competing firms in the U.S. and elsewhere[15]. Additionally, the Japanese firm is often reported to have a more highly committed labor force than is the case with firms located in the U.S. and elsewhere, meaning that Japanese workers are more loyal, more likely to internalize company values, and less like to complain or grieve than workers in other nations[16]. Thus, Japanese firms are claimed to have managed their work forces in ways which have enabled them to achieve economic and behavioral advantages over other firms, and this aspect of international competition has sparked a new interest in strategic human resource management among firms in the U.S. and other nations[17].

A second factor influencing the recent thrust toward strategic human resource management has been the spate of best selling books about business, which typically claim that certain leading or "best practice" companies have achieved superior performance through their management of people. Works in this genre include In Search of Excellence, The Change Masters, and Theory Z[18]. Until the 1980s, it was unusual, indeed, unheard of for books about business or management to be widely read by mass audiences, but that is exactly what occurred in the case of the aforementioned volumes and some others that followed them. Consequently, millions of people around the world have been exposed to the idea that high-performing firms achieve their results through the effective management of people--human resources--and this idea permeated business and management thinking as well. That scientific evidence supporting the claim that firms can obtain competitive advantage through the (strategic) management of human resources was sparse or even absent from these written works matters far less than that this thesis came to be accepted by the general public and by many in business and management circles.

A third factor contributing to the growing emphasis on strategic human resource management in the firm is the academic literature on this subject, particularly that portion of the literature that deals with the decline of unionism in the U.S. (and elsewhere) and the growth of nonunion workplaces and firms. For example, the authors of the influential book, The Transformation of American Industrial Relations, contend that by the mid-1980s management had become the dominant "actor" in the United States' system of industrial relations, supplanting the labor union and government which were the dominant actors in prior eras[19]. This new management domination was reflected in management's strengthened opposition to the unionization of its nonunion work forces, it's investment in nonunion facilities and operations and disinvestment in unionized facilities and operations, and it's hardened stance at the bargaining table when dealing with unionized employees. These and related developments are claimed not only to have shifted the balance of power in the employment relationship, but also to signify the newly proactive or strategic focus that firms have adopted with respect to the management of human resources[20].

To be sure, this line of reasoning has not gone uncriticized. Consider, for example, that in shifting from unionized to nonunion operations, United States' firms may simply be reacting to the availability of lower cost labor and production opportunities elsewhere, including outside of the United States. Some firms may be substituting new and relatively less expensive forms of capital for relatively more expensive unionized labor, which is a well known and long-standing option/practice, and other firms may simply be following the lead of larger competitor firms in shifting resources from unionized to nonunion operations. Further, the argument that management actions and behavior have importantly contributed to the decline of unionism in the United States (and in much of the developed world more broadly) downplays, perhaps even overlooks, the declining "demand" for unionism by employees in the United States (and elsewhere)[21].

As will be elaborated later in this book, the customer that labor unions seek to enroll as members and supply with certain services is the employee; the union must somehow convince the employee that the costs of membership are at least offset by the benefits to be derived from membership. Consider that if large portions of a company's customer base decide not to continue purchasing the company's product, or if potential new customers do not choose to purchase the company's product, we regard this as and label it a decline in demand at the level of the firm. Similar reasoning can be applied to existing and potential customers of labor unions. Indeed, a decline in customer demand for union membership and services should lead the union (as it presumably would a firm) to define a new strategy to counter this declining demand. Whether and to what extent labor unions actually respond to declining customer demand by defining new organizing and membership strategies is an empirical question, but the main analytical point is that the characterization of firms-employers as engaging in strategic human resource management by exerting major influence on the incidence of work force unionization may overstate both the importance of the firm in the direct customer-union relationship and the extent to which firms are actually engaged in the strategic management of human resources[22].

Nevertheless, the fact of declining union membership, the shift of resources from unionized to nonunion plants, offices, and businesses, and the extraction by employers of bargaining concessions from unionized employees during the 1980s and 1990s have added to the impression that management has adopted a more proactive, strategic approach to the management of human resources. Moreover, there is no denying that some firm are explicit about their desire to remain nonunion and about their adoption and use of certain human resource policies and practices to achieve this objective. For example, Federal Express, whose human resource policies and practices are discussed in greater detail in Chapter 18 of this book, maintains a Guaranteed Fair Treatment (GFT) procedure through which employees may formally register their complaints and have hearings to resolve them[23]. Federal Express openly describes this grievance-like procedure as one of its several substitutes for unionism, touts the benefits of the GFT when recruiting new employees, and openly states its desire to remain a nonunion business. Other companies, such as IBM, Northrop, and Toyota, also openly express their desire to remain union-free (in the United States), and still other companies which are less explicit in this respect nevertheless set union avoidance as a business objective and sometimes penalize managers whose operations or facilities become unionized. Thus, the idea that the union status of a firm tells us something about the extent to which human resources are taken into account in the firm's strategic planning process and about the extent to which human resources are managed strategically is not without merit.

But perhaps more telling in this respect are recent company initiatives at and academic literature about employee financial and nonfinancial participation in the firm, both in nonunion and unionized settings. Concerning financial participation, the 1980s bore witness to widespread efforts on the part of firms to tie a portion of employee compensation more closely to unit or organizational performance. The most popular of these initiatives took the form of profit-sharing, bonus, and stock ownership plans (which are discussed in detail in Chapter Eight of this book), which relate a portion of an employee's compensation to the overall performance of the business[24]. Other plans, such as gainsharing and productivity sharing plans, link a portion of an employee's compensation to the performance of an organizational unit, such as a plant or facility. What these plans have in common is that they put more risk into compensation arrangements, which is why they are sometimes referred to as "variable pay" or "pay at risk" plans. Recently, evidence has been produced showing that "pay at risk" plans apparently pay off in the sense of being statistically associated with improvements in firm performance[25]. Such evidence, in turn, reinforces the notion that financial participation of employees in the business is an important component of strategic human resource management.

Attracting even more practitioner and scholarly attention, perhaps, are the numerous recent initiatives at employee nonfinancial participation, or participation in decision-making, in the firm. These include quality circles, quality-of-work life improvement programs, autonomous and semi-autonomous work teams, joint labor-management committees, and even employee attitude/ morale/climate surveys[26]. As with financial participation or pay-at-risk plans, these nonfinancial participation initiatives have been undertaken largely in the belief that they will contribute to improvements in firm performance. And, recent statistical evidence seems to support this belief, especially when nonfinancial participation initiatives are combined with financial participation initiatives[27]. Such evidence reinforces the notion that nonfinancial participation of employees in the business is an important component of strategic human resource management.

In sum, several factors have contributed to the claim that human resource strategy can be closely linked to business strategy, to the belief that human resources can be managed strategically, and to the movement away from process-oriented personnel administration toward results or outcomes-oriented strategic human resource management in business organizations. However, the question remains as to whether or not the discipline/function of human resource management will develop a central analytical framework or technique, such as that of econometric forecasting, the market share-operating margin matrix, or portfolio theory, to guide the choice of human resource strategy in the firm as well as human resource management strategy research. In the absence of such a core framework or technique, it is doubtful that human resource strategy and management will become truly central to strategic business planning or that human resource executives will take a major step up to the strategy table, as did their economics, marketing, and finance counterparts before them. In our judgment, no dominant theory, framework, or technique of human resource management strategy has yet emerged, certainly not one that has "driven out" competing theories, frameworks, or techniques. Consequently, we turn out attention to some of the leading frameworks and concepts which are presently competing for dominance in the area of human resource strategy.

Concepts of Human Resource Strategy

One conceptual approach to human resource strategy is grounded in an organizational life cycle framework of analysis, as shown in Figure 2. As with industry life cycle, product life cycle, and individual life cycle concepts, the organizational life cycle framework begins with a start-up or birth phase[28]. By dint of its being founded, a business necessarily experiences the birth phase of the organizational life cycle. Joint ventures between two or more companies and so-called entrepreneurial businesses are commonly referred to as business start-ups, but more generally it is most accurate to think of any new business as a start-up. During the 1980s, annual rates of new business start-ups in the U.S. and abroad repeatedly reached record high levels, but so too did failure rates of new business start-ups. This fact underscores that while all new businesses experience the start-up phase of the organizational life cycle, they do not necessarily experience or transition to the growth phase of the cycle. This is because start-up businesses often are not able to identify a market niche for their products or services, attract new customers, or earn sufficient revenues to cover expenses, including the cost of capital. Indeed, the typical start-up business must be prepared to undergo an initial period of operating loss, and this initial period may be several years in length. Unless the start-up business is able to attract sustained financing from one or another source over an initial multi-year period, its chances of surviving are slim indeed. As an example, U.S.A. Today, which was founded in 1979, did not turn a profit until its eighth year of operation. Had U.S.A. Today not been sustained financially by its parent organization, the Gannett Company, it is highly doubtful that this newspaper would have survived the start-up phase of the organizational life cycle.

If a business does survive the start-up phase, it then moves to the growth phase of the organizational life cycle, which is characterized by relatively rapid growth of its customer base, revenues, market share and return on investment[29]. Apple Computer, Avon Products, Merck & Co., Amgen and SONY were leading examples of growth companies during the 1980s, while Microsoft, Compaq

Computer, and Nintendo are leading examples of growth companies during the 1990s. Businesses in the growth phase of the organizational life cycle are also notable for the rapid expansion of their work forces, which is consistent with microeconomic theory in that the demand for labor is derived from the demand for the product.

Virtually all businesses would prefer to remain in the growth phase of their respective organizational life cycles, but especially when product markets are competitive it is difficult to maintain rapid and sustained high growth rates. When a business' rates of growth of customers, revenue, market share and return on investment begin to decline, the business is entering the maturity phase of the organizational life cycle. Continued declines in these relevant growth rates indicate that the business is becoming highly mature and is perhaps in danger of entering the decline phase of the organizational life cycle. Recent examples of highly mature businesses include IBM Corporation, General Motors Corporation, Digital Equipment Corporation, American Express, and Grumman Aircraft.

When a business recognizes that it is in the maturity phase of the organizational life cycle, it typically will attempt to renew or transform itself so as to avoid moving into the decline phase of the cycle. Renewal initiatives can take many forms, including structural reorganization, consolidation and elimination of certain product lines, relocation of selected operations and facilities, and especially work force restructuring. For U.S.

businesses in particular, the last of these initiatives has been the one most widely adopted by mature businesses and has resulted, in turn, in work force reductions (which will be more fully discussed below)[30]. Mature businesses usually seek to reduce the ratio of labor or payroll cost to total operating cost, and this requires either or both a reduction in the number of jobs and a reduction of per capita compensation.

Failure to renew or transform the mature business will likely mean that the business will enter the decline phase of the organizational life cycle. This phase is characterized by absolute declines in the number of customers, revenues, market share, and rate of return on investment. Failure to stem these declines may well mean that the business will experience the ultimate in decline, that is, it will die. While, in the U.S., a business that files for bankruptcy may not really die in that it can emerge from bankruptcy as a restructured and refinanced entity, a bankrupt business nevertheless faces especially formidable challenges in attempting to renew itself so as to move "backward" in, that is, to return to an earlier phase of, the organizational life cycle. Recent examples of businesses in the decline phase of the cycle include Castle & Cook, Columbia Savings & Loan, Macy's, Crazy Eddie's, and Trans World Airlines (TWA), all of which filed for bankruptcy in the late 1980s and early 1990s.

As also shown in Figure 2, the concept of an organizational life cycle is joined to the concept of a "human resource management portfolio" in providing an analytical perspective on human resource strategy. The human resource management portfolio refers to that collection of human resource areas, activities or components which are of central importance to the business. These typically include job design, selection, performance appraisal, compensation and rewards, training and development, employee relations/voice, health and safety, and affirmative action/equal employment opportunity. We say "typically" because, from a global perspective, centrally important human resource management components may differ from region to region or country to country[31]. To illustrate, affirmative action/equal employment opportunity is more closely regulated and thus of greater operating relevance to a business in the U.S., Canada, and Great Britain than in other nations. In another example, workplace safety and health is more highly valued by businesses in developed than in developing nations. Hence while the concept of a human resource management portfolio at the level of the firm can be thought of as having wide, indeed, global applicability, the particular components of the portfolio will vary by a nation's stage of economic development, laws and customs as well as by location, industry and company.

The fundamental idea that emerges from the organizational life cycle-human resource management portfolio matrix depicted in Figure 2 is that a business' human resource strategy, policies, and practices should be mapped to the business' stage of its organizational life cycle. Further, this matrix provides guidance to a business about the relative importance of the components of its human resource management portfolio, and about specific policies and practices that should be followed within specific component areas.

For example, a start-up business needs to attract human resources--employees--from the external labor market. That is, it must select or "buy" human resources externally since, by definition, it has no current employees and therefore cannot fill particular vacancies by "making" employees through programs of training and development. When buying human resources from the marketplace, compensation and reward systems are particularly important because potential new employees of the start-up business will compare the compensation and rewards offered by this business with what they presently receive from their current employers or are offered by other businesses. Therefore, the human resource strategy of a start-up business will focus most strongly on two components of the human resource management portfolio, namely, selection/sourcing and compensation and reward systems[32]. If the start-up business has a written strategic plan and if that plan explicitly addresses human resource strategy, selection/sourcing and compensation and reward system plans and objectives should be spelled out in it.

In addition, the start-up business can use the organizational life cycle framework to guide its choices of particular selection and compensation policies and practices. For example, a start-up business' employee selection policy is likely to emphasize relevant experience more than formal schooling or training. Consequently, the start-up business is most likely to recruit new employees from other businesses rather than from schools and colleges, and is more likely to place job advertisements in trade journals or specialized industry publications than in newspapers or on radio and television. In the area of compensation and reward systems, the start-up business is most likely to emphasize equity participation of employees in the business. This means that a stock ownership, bonus, profit-sharing, stock option plan or combinations thereof are likely to be part of the compensation package for new employees, and that base wages or salaries as well as fringe benefits will not be the sole components--and perhaps will be relatively minor components--of the compensation package.

For a business in the growth stage of the organizational life cycle, such human resource management components as performance appraisal and training and development are likely to be most heavily emphasized. This is due in part to the needs of a growing business to structure career paths, identify promotable employees, and plan for management succession. Put differently, a business in the growth stage of the organizational life cycle must invest in firm-specific human capital in order to supply the human resources necessary to meet the demands of an expanding market and a more complex organizational structure. While some of these human resource needs will be met by recruiting and hiring from the external labor market, others will be met by structuring internal labor markets so as to enable the business to "make" human resources internally in order to fill the jobs which are created as a result of the business' expanding sales, revenue and (perhaps) market share. Performance appraisal and training and development programs thus come to occupy an especially prominent place in the human resource management portfolios of businesses in the growth stage of the organizational life cycle.

For businesses which enter the maturity phase of the organizational life cycle, pressures emerge for productivity improvement and the containment of labor costs. To enhance productivity, businesses will often adopt new human resource programs featuring one or another form of incentive pay. The Scanlon Plan, Rucker Plan, and Improshare Plan constitute leading forms of such incentive arrangements, and the common element of these plans is the "payoff" to labor and management for achieving costs that are below established standards for given levels of production[33]. To reduce labor costs or, more specifically, the ratio of labor (personnel) costs to total operating costs, businesses are faced with the aforementioned alternatives of reducing employment or reducing per capita compensation. Faced with this imperative, most U.S. businesses have chosen to reduce employment or, more specifically, to reduce the employment of full-time, "regular" personnel and expand the employment of peripheral employees, namely, those employed on a part-time, temporary, contracted or vendored basis. The latter group of employees constitute a lower cost form of labor input to the production process than do the former group of employees because most peripheral employees are employed under time-limited (contracted) wages and salaries and receive far lower levels of fringe benefits than regular or core employees. The question of whether peripheral employment in the U.S. economy is merely a function of the business cycle, and is thus a short-term phenomenon, or instead represents a long-term structural shift in the nature of the employment relationship, is key to both the macro and micro levels of human resource management. Also characteristics of mature businesses is their tendency to adopt new employee involvement/participation programs which are based on principles of self-management. Often claimed to "empower" employees to have more responsibility for decision-making, these programs also feature the reduction of labor costs via the elimination of lower-level supervisory and management personnel and thus have an important labor cost containment objective and underlying rationale.

For businesses that enter the decline phase of the organizational life cycle, human resource strategy, policies, and practices are aimed at major labor cost reduction. Employee layoffs are common among declining businesses, but so too are "incentivized" early retirement programs, the sale or divestiture of low performing business units, and initiatives to have employees bear (or share) a certain portion of the costs of fringe benefit programs, especially (in the U.S.) health care programs. Managements of declining business are also more likely than managers of businesses in other stages of the organizational life cycle to consider selling the business to employees--thereby creating so-called employee-owned businesses which may be regarded as the ultimate form of employee involvement in decision-making (or empowerment). For businesses in the decline phase (and, to a lesser extent, in the maturity phase) of the organizational life cycle, jobs are typically redesigned to become larger in scope, and the "selection" problem becomes one of deciding whom to select out of rather than into the business. In sum, the organizational life cycle perspective on human resource management strategy, policy and practice emphasizes the responsibility of management to match or fit such strategy, policy and practice to the business' stage of the organizational life cycle. This may be termed the "analytical value" of the organizational life cycle-human resource management portfolio framework depicted in Figure 2.

However, Figure 2 also suggests the "normative value" of this particular framework, principally in the column labeled "renewal." The underlying idea here is that a business becomes more mature, it can recognize this and take steps to renew or transform the organization in order to avoid moving into the decline phase of the organization life cycle. With respect to human resource management policy and practice, renewal may involve the introduction of work teams to replace narrow individual jobs and work, labor cost containment and incentive compensation programs, team based and/or peer type performance appraisals, targeted training programs to enhance newly required skills, and other measures. More broadly and for the business as a whole, renewal may involve fundamental reengineering of work processes, redesign of the organization's structure and control systems, and perhaps even a recasting of the business' basic mission and strategy. The concept of renewal in the context of the organization life cycle underscores the idea that a business can move back or up the cyle to reposition itself as a growth business and thus survive, rather than inevitably be drawn into the decline stage of the cycle or, ultimately, go out of existence.

A different perspective on human resource strategy is offered by the flow model of human resource management depicted in Figure 3. The key components of this model are business strategy, human resource strategy, human resource policy and practice, human resource outcomes, and business outcomes. The connection between human resource outcomes and business outcomes constitutes the key analytical insight offered by this model. Consider that human resource policies and practices (in each of the components of the human resource management portfolio represented in Figure 2) lead to particular human resource management outcomes, for example, hiring rates, staffing ratios, employee turnover, absenteeism and work attendance rates, performance appraisal ratings, grievance rates and employee morale.

While these and other outcome measures have traditionally been used to assess the effectiveness of the human resource (or personnel) function in business organizations, recently increased competitive pressures on business organization have brought about a stronger emphasis on and a questioning of the relationship between human resource outcomes (measures) and business outcomes (measures). Increasingly business organizations want to know how employee turnover, morale, work attendance, grievance rates and other human resource outcomes are related to such business outcomes as return on investment, return on assets or capital employed, and market share[34]. Establishing and measuring the relationships between human resource management outcomes and business outcomes is a difficult and tricky task because one must control for the many other factors, for example, industry, capital/labor ratio, company size and age, etc., which can influence business performance. Yet this task must be attempted if we are to know more about how human resource management policies and practices and the outcomes associated with them affect business performance outcomes.

In this regard, some guidance is provided by long-standing and newer research into the effects of employee unionism and collective bargaining on business organizations[35]. Using a standard microeconomic framework of analysis, researchers have statistically measured the effects of unionism on wages and fringe benefits, productivity, capital investment, research and development expenditures, firm profitability, and even market value (usually measured by stock prices). Because the (traditional) role of the labor union, especially in the U.S., has been to raise wages and benefits above prevailing market levels and, more generally, to shift economic returns from owners of capital to workers, researchers typically hypothesize that the economic effects of unionism on business will be negative. And, researchers have generally found such effects to be in this direction and to be statistically significant--findings which help to explain the secular decline of unionism in the U.S.

While this topic will be more fully addressed in Chapter 12 of this volume, the modelling of unionism's effects on the business organization provides a useful starting point for analysis of the effects of human resource management policies and practices on the business organization. To illustrate, businesses that have adopted programs of employee financial and nonfinancial participation in the business do so in the belief that such initiatives will enhance business performance. For researchers, this belief can be translated into a set of hypotheses positing expected positive relationships between employee financial and/or nonfinancial participation in the business and the performance of the business. Recent empirical work which tests these hypotheses finds that measures of employee financial participation in business organizations and measures of employee nonfinancial participation in business organizations are indeed separately and interactively positively related to such business performance measures as return on investment, return on assets, and productivity (revenue per employee)[36]. Similarly, significant positive relationships between the labor cost containment initiatives of business organizations and measures of business performance have been reported by researchers[37]. In contrast, nonsignificant to negative relationships between individual performance appraisal rating systems and business performance, and between various employee recruitment and selection methods and business performance,have also been reported in the literature[38].

For present purposes, the validity and generalizability of these studies are perhaps less important than the fact that researchers have made considerable progress in linking and sorting out the linkages between human resource management policies and practices, on the one hand, and measures of business performance, on the other hand. Such business performance-oriented human resource management research, in turn, reflects the growing recognition of the potential importance of human resources to businesses' "bottom line"--which is the key linkage in the analytical framework presented in Figure 3.

The final conceptual framework for the analysis of human resource management presented here may be dubbed the "human resource stakeholder-human resource success factor" framework, as depicted in Figure 4[39]. Underlying this framework are two questions, which must fundamentally be addressed by management: "How valued or important are human resources (employees) relative to other stakeholders in the business?", and "How valued or important are human resources (employees) relative to other success factors in the business?"

As shown in Figure 4, where employees are weakly valued both as a stakeholder group and as a success factor in the business, the dominant orientation toward employees and, therefore, of human resource strategy is "transactional." This means that a business' work force is likely to be transient, have high turnover, be provided with little in the way of training and development opportunities, and more generally be treated as a commodity. Empirically, transient or transactional type human resource management strategies, policies and practices are found in the agricultural, apparel, and retail trade industries, and in accounting firms, small firms, and developing economies.

Where employees are weakly valued as a stakeholder group but strongly valued as a success factor in the business, the dominant orientation toward employees and, therefore, of human resource strategy is "structured." This means that a business' work force is likely to be centrally directed and controlled, assigned to narrow jobs (tasks), have well specified terms and conditions of employment, be subject to one way (top-down) communication, and be closely supervised and monitored. Empirically, structured or centrally directed type human resource management strategies, policies and practices are found in manufacturing industries, especially durable goods manufacturing industries such as automobiles, steel, rubber and aerospace; in large firms; and in service businesses with large paper processing or "back room" operations, such as insurance and banking. Historically, highly structured and centrally directed work forces represented the dominant orientation toward the human resources of business organizations in the U.S. and abroad during much of the 20th century[40].

Where employees are strongly valued as a stakeholder group but weakly valued as a success factor in the business, the dominant orientation toward employees and, therefore, of human resource strategy is "paternalistic." This means that a business' work force is likely to be and feel entitled to continuous employment, regular pay increases, expanding fringe benefits, well specified career paths, promotional opportunities and, more generally, a high morale-inducing work environment. Empirically, paternalistic or entitlement type human resource management strategies, policies and practices seem to have developed primarily during the third quarter of the 20th century, and were perhaps most evident in the computing, telecommunications, utilities and office products industries; in large multinational firms and family-owned businesses; in businesses that dominated their respective product markets; and in publicly-held firms with widespread, diffused stock ownership. Thrusts toward deregulation during the 1980s and the spread of global competition during the 1980s and 1990s seem to have been the strongest forces eroding the paternalistic-entitlement orientation toward human resource management in business enterprises, and work force downsizings (reductions in force) probably constitute the leading manifestation of this erosion.

Where employees are highly valued as a stakeholder group and as a success factor in the business, the dominant orientation toward employees and, therefore, of human resource strategy, is "participative." This means that a business' work force is likely to be (or be made to feel) empowered, highly involved in work place decision-making, employed in broad flexible jobs, trained to perform multiple skills, and organized into work teams. Participative or empowerment type human resource management strategies, policies and practices have only recently come to the fore in the U.S., and are widely judged to constitute a "corrective" to the earlier paternalistic-entitlement orientation toward human resources[41]. Empirically, initiatives at employee participation-empowerment have taken place primarily in large manufacturing businesses and very often have been mounted as part of a program of total quality management (TQM), continuous measurable improvement (CMI,) or statistical process control (SPC). Such initiatives also have often been instituted in new businesses or business units of large conglomerate firms, in entrepreneurial businesses, and in joint ventures. The joint venture between General Motors Corporation and Toyota Motor Corporation which began in 1984, known as New United Motor Manufacturing Incorporated (NUMMI), and the automobile manufacturing subsidiary company owned by General Motors which produced its first product in 1990, known as Saturn, are perhaps the best know extant examples of team-based organizations based on principles of employee participation and empowerment[42]. The Minnesota Mining and Manufacturing Company, Motorola, Ford Motor Company, and Xerox are leading examples of business organizations which have recently instituted TQM-type programs with a dominant orientation toward employee participation-empowerment.

Challenges to Human Resource Management

The analytical frameworks for the study and practice of human resource management presented in this chapter have some obvious differences, but they commonly appear to pose a challenge to business organizations in general and human resource executives and professionals in particular. The challenge is to make human resources a more central component of business strategy and, relatedly, to have senior human resource executives occupy a major seat at the business strategy table. Does the "typical" senior human resource executive occupy such a seat?

The data presented in Table 1 are useful for answering this question. The data were obtained as part of a larger study of human resource management policies and practices in 495 U.S. businesses, and reflect the distribution of responses to the question, "To what extent is your senior human resource official involved in business planning?[43]" On a seven point scale with one equalling "never" and seven equalling "always," the mean response was 4.70 but the range was from one to seven. Indeed, about 27 percent of the responses to this question were distributed among the three lowest points on the scale, and another 27 percent or so of the responses were at the high point of the scale. Consequently, there appears to be no "standard practice" when in comes to the involvement of senior human resource executives in the business planning process of (large, publicly-held) U.S. firms. Moreover, other comparable surveys of the involvement of senior marketing, finance, and operations executives in strategic business planning yield equivalent mean scores of between 6.0 and 6.7 on seven point scales[44]. This suggests that senior human resource executives are not as involved in strategic business planning as their counterparts in other key functional units of business organizations. Without some enhancement of the strategic business planning role of senior human resource executives, opportunities to link human resource strategy more closely to business strategy and human resource outcomes to business performance outcomes may go unfulfilled. This, in turn, casts doubt on the ability of business organizations to use human resources for competitive advantage.

Finally, and in light of the large amount of attention given to the way in which Japanese businesses are claimed to manage their human resources for competitive advantage, we may ask whether or not the line executives of U.S. and Japanese firms differ in the extent to which they value employees as a stakeholder group in the business, and the extent to which they desire employee participation in business decisions. The data presented in Tables 2 and 3 are relevant to this issue. The data are drawn from recent surveys of samples of executives of U.S.-owned and Japanese-owned firms operating in the U.S., which in effects permits us to hold constant certain important environmental variables that would come into play if the comparisons were made between executives operating in the U.S. and executives operating in Japan[45].

The data in Table 2 show that executives of Japanese firms operating in the U.S. rank employees as a stakeholder group significantly more highly than do executives of U.S. firms operating in the U.S. For the Japanese executives, employees are ranked second among the six stakeholder groups listed in Table 2, whereas the U.S. executives rank employees fourth among these six stakeholder groups. This same study also found that Japanese executives operating in the U.S. are significantly more likely than U.S. executives operating in the U.S. to favor employee participation in business decision-making as a whole. However, whereas the U.S. executives demonstrated a slight preference, relative to Japanese executives, for employee participation in workplace level decisions, the Japanese executives demonstrated a marked preference, relative to U.S. executives, for employee participation in strategic level decisions.

The regression results presented in Table 3 indicate that thee findings are not random or, put differently, that they are systematically influenced by certain important variables. One of these variables in the aforementioned executive ranking of employees as a stakeholder group in the business. This variable is significantly positively related to executive preferences for employee participation in business decision-making, both at the strategic and workplace levels. Overall, the Japanese executives have a stronger preference than the U.S. executives for employee participation in business decisions, in part because the Japanese executives place a higher value on employees as a stakeholder group than do the U.S. executives. But executives' preferences for employee participation in business decisions is also importantly influenced by the home country of the executive. The regression results in Table 3 show that executives from Japan demonstrate a significantly stronger preference than executives from the U.S. for employee participation in strategic level business decisions, but a significantly weaker preference than executives from the U.S.

from employee participation in workplace level business decisions.

Hence, once all is said and done, value differences among executives do appear to exert strong influence on the valuation of employees, preferences for employee participation in business decisions, and ultimately the role of human resources in business strategy. If executives of U.S. businesses are to achieve a closer integration of human resource strategy with business strategy, and of human resource outcomes with business outcomes, they may well want to reconsider their own views about the importance of employees as a stakeholder group in the business, and about the level of decisions in which employees are "empowered" to participate--especially given the values and preferences in these respects of Japanese executives who are widely claimed to have managed human resources for competitive advantage and to have outperformed U.S. executives in this regard.

FIGURE 1

DISCIPLINES AND FUNCTIONS THAT INFLUENCE
BUSINESS STRATEGY AND PLANNING

Time Period	Discipline/ Function	Concept/ Tool	Application/ Variables
1960s	Economics	Econometrics	Industry Forecasting
1970s	Marketing	Matrix	Share-Margin
1980s	Finance	Portfolio	Risk-Reward
1990s (?)	Human Resources	Organization Life Cycle	Asset-Expenditure

FIGURE 2

THE ORGANIZATIONAL LIFE CYCLE AND
HUMAN RESOURCE MANAGEMENT PORTFOLIO

Human Resource Component	Stage of the Life Cycle				
	Start-Up	Growth	Maturity	Renewal	Decline
Job/Work Design					
Sourcing/ Selection					
Performance Appraisal					
Compensation Rewards					
Training/ Development					
Participation/ Voice					
Safety/ Health					
Equal Employment Opportunity					

FIGURE 3

THE HUMAN RESOURCE MANAGEMENT FLOW MODEL

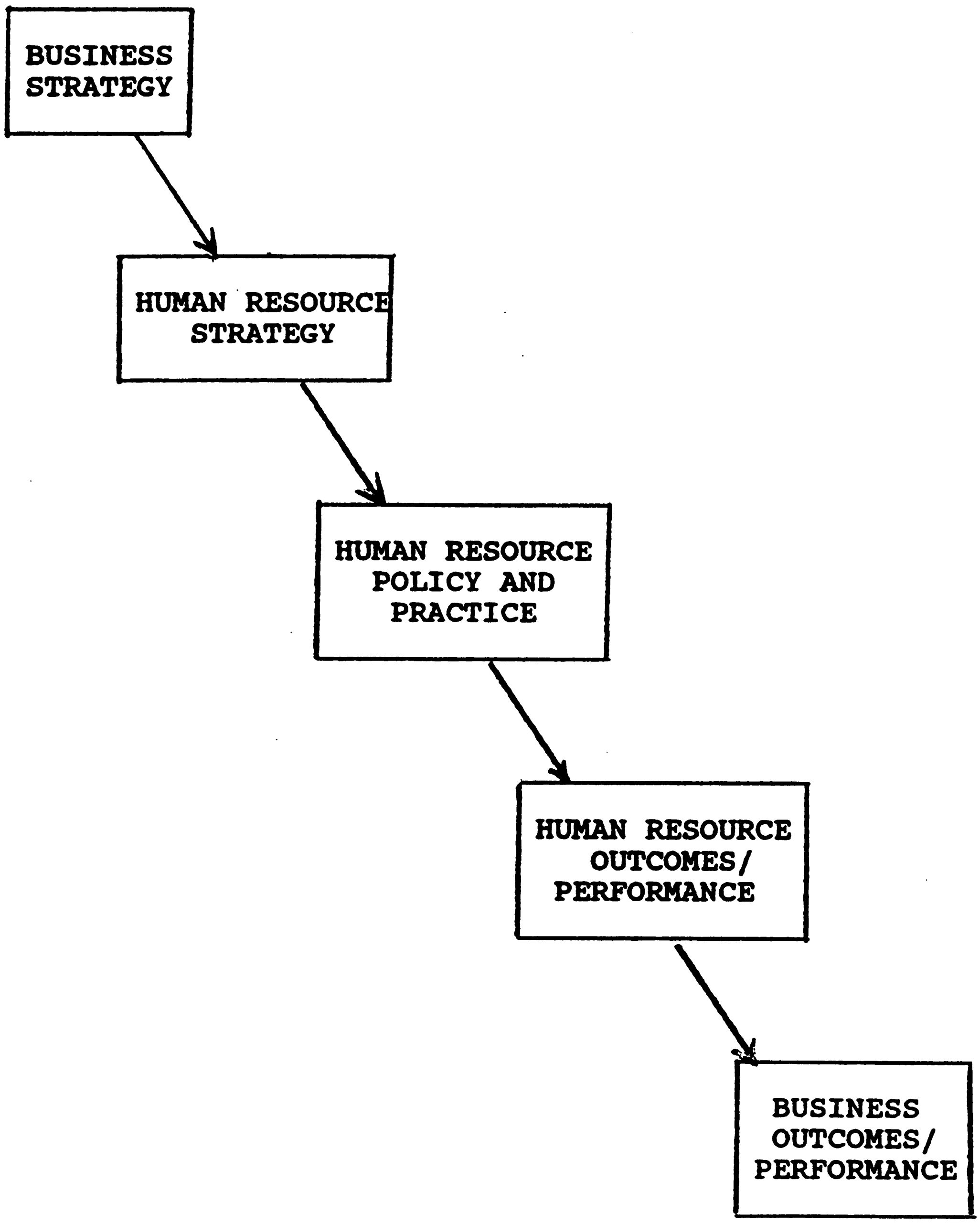

FIGURE 4

THE HUMAN RESOURCE STAKEHOLDER-
HUMAN RESOURCE SUCCESS FACTOR FRAMEWORK

Value of Human Resources Relative to Other Stakeholders		Importance of Human Resources Relative to Other Success Factors: Less Important	Importance of Human Resources Relative to Other Success Factors: More Important
	More Valued	Entitled Workforce (Paternalistic)	Empowered Workforce (Participative)
	Less Valued	Transient Workforce (Transactional)	Directed Workforce (Structured)

TABLE 1

SENIOR EXECUTIVE INVOLVEMENT
IN BUSINESS PLANNING

	Scale						
	Never						Always
	1	2	3	4	5	6	7
Percent of Responses	9.6	8.1	9.6	12.3	18.4	14.6	27.4
Number of Responses	43	36	43	55	82	65	122

Mean = 4.70

Source: John Thomas Delaney, David Lewin and Casey Ichniowski, Human Resource Policies and Practices in American Firms, Bureau of Labor-Management Relations and Cooperative Programs, U.S. Department of Labor, BLMR #137 (Washington, D.C.: G.P.O., 1989), p. 61.

TABLE 2

SENIOR EXECUTIVE RANKINGS OF STAKEHOLDER GROUP IMPORTANCE
(Ranked on a scale with 1=most important to 6=least important)

Rank by Importance	Executives of U.S. Firms	Executives of Japanese Firms Operating in the U.S.
First	Shareholders M = 1.38 SD = 0.21	Customers M = 1.43 SD = 0.31
Second	Customers M = 1.97 SD = 0.37	Employees M = 1.83 SD = 0.29
Third	Suppliers M = 2.73 SD = 0.33	Suppliers M = 2.66 SD = 0.28
Fourth	Employees M = 3.78 SD = 0.37	Government Regulatory Agencies M = 3.59 SD = 0.34
Fifth	Government Regulatory Agencies M = 4.62 SD = 0.56	Shareholders M = 4.54 SD = 0.38
Sixth	Community Groups M = 5.59 SD = 0.40	Community Groups M = 5.67 SD = 0.36
N =	384	107

M = Mean Ranking; SD = Standard Deviation
Source: David Lewin and Peter D. Sherer, "Does Strategic Choice Explain Senior Executives' Preferences on Employee Voice and Representation?," in Bruce E. Kaufman and Morris M. Kleiner, eds., Employee Representation: Alternatives and Future Directions (Madison, WI: Industrial Relations Research Association, 1993), p. 248.

TABLE 3

REGRESSION COEFFICIENTS ON SENIOR EXECUTIVE RATINGS OF THE DESIRABILITY OF EMPLOYEE VOICE AND REPRESENTATION IN STRATEGIC AND WORKPLACE LEVEL ISSUES
(standard errors in parentheses)

Independent Variables	Strategic Issues	Workplace Issues
Executive Rankings of Employees as Stakeholders	1.92* (0.88)	2.02* (0.91)
Home Country of Firm	2.12** (0.82)	-1.72* (-0.77)
N =	491	491
R = squared	0.41	0.39

* = Significant at p = < .05.
** = Significant at p = < .01.

Source: David Lewin and Peter D. Sherer, "Does Strategic Choice Explain Senior Executives' Preferences for Employee Voice and Representation?," in Bruce E. Kaufman and Morris M. Kleiner, eds., <u>Employee Representation: Alternatives and Future Directions</u> (Madison, WI: Industrial Relations Research Association, 1993), p. 258.

FOOTNOTES

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40. Reinhard Bendix, Work and Authority in Industry (New York: Wiley, 1956); Sanford M. Jacoby, Employing Bureaucracy: Managers, Unions and the Transformation of Work in American Industry, 1900-1945 (New York: Columbia University Press, 1985).

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42. Bill Childs, "New United Motor: An American Success Story," Proceedings of the 1989 Spring Meeting, Industrial Relations Research Association (Madison, WI: Industrial Relations Research Association, 1989), pp. 453-460; Saul Rubenstein, Michael Bennett and Thomas A. Kochan, "The Saturn Partnership: Co-Management and the Reinvention of the Local Union," in Bruce E. Kaufman and Morris M. Kleiner, eds., Employee Representation: Alternatives and Future Directions (Madison, WI: Industrial Relations Research Association, 1993), pp. 339-370.

43. Delaney, Lewin and Ichniowski, op. cit., p. 61.

44. Lewin, "Financial Dimensions of Workforce Management," op. cit.

45. David Lewin and Peter D. Sherer, "Does Strategic Choice Explain Senior Executives' Preferences on Employee Voice and Representation," in Bruce E. Kaufman and Morris M. Kleiner, eds., Employee Representation: Alternatives and Future Directions (Madison, WI: Industrial Relations Research Association, 1993), pp. 235-263; David Lewin and John Zuan Yang, "HRM Policies and

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