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Strategic Human Capital Measures

Orientation, Accountability, and Communication

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Strategic Human Capital Measures

Orientation, Accountability, and Communication

by Stephen Gates

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Foreword

Human capital is possibly the most vital, yet overlooked, means of establishing competitive advantage for companies today. In nearly every business periodical we read about the "global war for talent," the need for better ways to encourage innovation, the complexities posed by the maturing workforce, the academic preparedness of the talent pipeline, etc. Rarely have I picked up a company's annual report or listened to a CEO without being reminded that "people are our greatest asset."

Regardless of how well executives may genuinely extol the necessity to attract, grow, motivate, and retain talent, our means of measuring the management of talent and, more importantly, empirically demonstrating its impact continue to lag behind.

This report provides powerful insight into the current use of human capital measures (HCMs), highlights case studies of two of the global leaders in human capital measurement and management, and gives a historical context for understanding the development of HCMs and their use.

I'm very encouraged by some of the results of the survey conducted for this study. More than half of the participants reported that their companies use HCMs for evaluating their managers and calculating their bonuses. Nearly seven out of every 10 companies used HCM benchmarking to ensure that they are remaining competitive in their management practices. Most critically, we are seeing increases in the use of HCMs to determine whether a company has achieved its specific goals. These advances demonstrate that the value of human capital is gaining greater attention and that the management of talent is becoming more aligned with the operation of businesses.

But this research also reveals some continuing challenges. While more than half of the participants used HCMs to evaluate and reward their managers, fewer than 20 percent of them actually provided these measures to managers at all levels of the organization. This raises the question of whether managers can—or should be—held accountable for targets that have little or no visibility.

While a clear majority of companies used some form of human capital benchmarking techniques, more than half reported that benchmarking was, at best, "moderately" effective—and nearly 20 percent of companies using benchmarks indicated that these techniques were only "slightly effective" or "not effective at all."

While it is encouraging to see that HCMs are being used in establishing performance goals for companies, it isn't clear whether these are linked to meaningful financial or operational performance goals of the company or are simply being used to evaluate how efficiently the human resources function is managing itself. Since more than half of the respondents indicated that their human resources department played "no role at all" in developing their company's strategies, it stands to reason that these advances in the use of HCMs are less focused on business strategies and more on department efficiencies.

This study represents a turning point for The Conference Board and its members. Stephen Gates has provided us with a very clear examination of what the human resources function has been able to accomplish in demonstrating the importance of human capital. But in the next phase of this evolution, human resources practitioners need to:

- move beyond the efficient use of human capital and begin to demonstrate how it empirically drives organizational performance;
- prepare both themselves as human resources practitioners and the human resources field in general to move beyond understanding the importance of "being at the table" and begin developing the tools and competencies that will help lead the conversation once human resources "gets its seat"; and
- set the groundwork for moving the management of human capital beyond being "aligned" with a company's strategies and to begin to learn (and then teach) how human capital can be powerfully "integrated" into those strategies.

The Conference Board is dedicated to helping our members address these challenges. Through Evidence-Based Human Resources—our new approach to human capital analytics—we are working to equip human resources executives with conceptual models, empirical techniques, and practical tools to integrate talent into strategy and to measure its impact. We understand that our goals are ambitious. They won't be accomplished without active involvement by our members over a period of time. However, with the help of our Evidence-Based Human Resources Advisory Panel (a collection of world-class thinkers and managers of human capital) and the resources of our Management Excellence Research Team, we are confident that we will reach our goals.

John Gibbons
Senior Research Associate
Management Excellence
The Conference Board

Key Findings

Companies are choosing human capital measures (HCMs) based on specific goals Organizations focused on differentiating themselves through offering unique products or services choose innovation metrics; companies primarily interested in cost concentrate on efficiency measures. But whatever a company's orientation, finding an ideal list of HCMs is less important than ensuring human resources is heavily involved in strategy formulation and implementation.

Human resources departments still play a limited role in strategy development Only 22 percent of human resources professionals who responded to a 2006 survey conducted for this report said their human resources function was a full partner in creating business strategy, while 53 percent claimed they either played "no role" or only "implemented strategy once it has been developed." When the human resources function has limited participation in setting strategy, it is difficult to link HCMs to strategic goals.

While a majority of companies use dashboards, causal models may prove a more effective interface Of the 69 percent of respondents who used HCMs in a dashboard, 53 percent considered such dashboards "moderately" or "less than moderately" effective. Out of the remaining dashboard implementers, 31 percent considered them "significantly" or "totally" successful and 16 percent rated them "slightly" or "not at all" successful. For a more direct correlation between human resources and performance, some companies are turning from dashboards to causal models, which show the impact of human resources on business outcomes.

HCMs are increasingly a factor in setting bonus plans Over half of the survey respondents—57 percent—were using HCMs in managers' bonus plans and 48 percent reported that HCMs received over 15 percent weighting in determining bonus plans. Of the 57 percent who include HCMs in managers' bonus metrics, 43 percent reported that they were "moderately" or "less than moderately" aligned with business targets, while 21 percent considered them "not at all" or "slightly" aligned.

HCM reports restricted to top executives The results from HCMs are most commonly delivered to top management, which was the practice at 85 percent of survey firms. The finding that only 19 percent of respondents distributed such briefings to all their business managers indicates that many companies do not view these reports as decision-making tools for managers. Moreover, the relatively small distribution of results also means that the findings are seldom broken down to the appropriate level for action planning.

Using Human Capital Metrics to Advance Strategy

Increasingly sophisticated software systems offer companies the ability to further develop the nonfinancial aspects of their management control systems. These innovative measurement possibilities have led to the emergence of a new generation of human capital metrics (HCMs). To demonstrate the value added from measuring human capital, companies must begin linking HCMs to their overall organizational strategies. In an effort to understand how to forge such bonds, The Conference Board launched two research working groups. This report offers findings from their investigations.

While human capital measurement has been gaining ground over the past 20 years, it still remains largely disconnected from business strategy. In a 2004 report published by The Conference Board, only 12 percent of respondents reported making significant use of HCMs to meet their strategic targets or key performance indicators (KPIs).[1] Nevertheless, 84 percent of the respondents in the same survey predicted that their use of HCMs to meet these goals would increase over the next three years. This disconnect between practice and potential may stem from how both the definition of human capital and its link to strategy have evolved over time.

A Concept with a Long History

The term "human capital" can be traced back to the writings of Adam Smith and other 18th-century economists. More recently, five different economists have won Nobel prizes for their research in this field.[2] Human capital theory explores how individuals and society derive economic benefits from investments in people, and education consistently emerges as the prime human capital investment for empirical analysis. From an economist's point of view, then, human capital clearly designates investments in improving competencies and skills.

In recent years, however, the management community has significantly broadened how the term is understood. Instead of being a notion strictly limited to investment in education and training, human capital has come to mean all human resources initiatives to recruit, develop, and retain employees. In this report, human capital measurement will be defined practically as the common categories of measures that the 104 respondents to a 2006 survey conducted for The Conference Board Research Working Group on Human Capital Strategy and Measurement frequently encountered in their organizations (Table 1).

Table 1
Frequently Used HCMs

Human Capital Measure	Percent who report measure is "frequently" used
Turnover (voluntary)	94%
Workforce diversity	79
Employee engagement	78
Workforce age	65
Employee satisfaction	64
Training	58
Health and safety	48
Leadership	47
Readiness level	44
Promotion rate	44
Employee commitment	40
Span of control	39
Competence level	37
Executive stability (or churn)	32
Depletion cost	14
Other	9

1 Stephen Gates, *Measuring More than Efficiency: The New Role of Human Capital Metrics*, The Conference Board, Research Report 1356, 2004, p. 7.

2 See, for example, Gary S. Becker, *Human Capital: A Theoretical and Empirical Analysis, with Special Reference to Education,* 2d ed. (New York: National Bureau of Economic Research, 1993).

HCMs Come of Age

Much of the modern effort to measure human capital stemmed from a more widespread frustration with how companies determined their worth. In 1987, H. Thomas Johnson and Robert Kaplan published *Relevance Lost*, a damning critique of how accounting systems were disconnected from the drivers of performance and, thus, failed to assist companies in long-term planning.[3] As a result, a number of attempts were made to reform accounting. One was Activity-Based Costing, which Johnson went on to champion.[4] Another was the Stern Stewart & Co. concept of Economic Value-Added, which found favor with companies seeking to look beyond return on assets (ROAs) to understand where value was created and lost.[5]

Calls for a revolution in accounting also led to a number of initiatives to track the nonfinancial aspects of business. Kaplan and David Norton promoted their Balanced Scorecard model as a way to systematically record information about customers, internal processes, and the learning and growth of skills in an organization.[6] There was also a renaissance of interest in Gary Becker's consideration of how to measure the economic value created by education.[7]

The "competency" movement, too, with its emphasis on seeing internal resources as the source of strategy and value creation, added strength to the focus on identifying the value stored in people.[8] Other research in knowledge management[9] sought to develop methods to capture the value created by what Peter Drucker called "knowledge workers."[10] In 1997, the accountancy practice of PricewaterhouseCoopers developed what it called ValueReporting, now subsumed in its Corporate Reporting Framework, to link methods to monitor human capital and other nonfinancial measures for management purposes with the external reporting requirements of public companies.[11]

Looking at the Human Resources Practices/Company Performance Connection in Reverse

Despite numerous studies that have attempted to move beyond conjecture to establish direct, causal links between human resource practices and improvements in financial performance, there has been frustratingly little success in proving this connection. This may be because the actual link between human resource initiatives and firm performance might be the opposite of what most researchers believe. After an exhaustive review of 68 studies on the subject, Patrick M. Wright, Timothy M. Gardner, Lisa M. Moynihan, and Matthew R. Allen found that few of these inquiries had tested for reverse causality (i.e., the proposition that good firm performance may lead to better human resource policies).* It's not such an implausible idea. Good leadership might, for instance, create strong financial performance and thereby the resources to develop generous training and development, which then add to the functioning of the company. One of the few studies that did control for reverse causality showed that firm performance *preceded* improved human resources practices. This led the researchers to conclude that "high performing organizations by their nature possess slack resources…. Firms that are profitable may share these profits with employees in a number of ways."** This team's own analysis revealed that none of the positive correlations between human resource's actions and future performance remained significant once the propositions were tested for reverse causality. The results, they concluded, suggest that any link was at best tentative and should be treated with great caution.

* Patrick M. Wright, Timothy M. Gardner, Lisa M. Moynihan, and Matthew R. Allen, "The Relationship between HR Practices and Firm Performance: Examining Causal Order," *Personnel Psychology*, Volume 58, Number 2, 2005, pp. 409–446.

** Wright et al., "The Relationship between HR Practices and Firm Performance," p. 419.

3 H. Thomas Johnson and Robert S. Kaplan, *Relevance Lost: The Rise and Fall of Management Accounting* (Boston: Harvard Business School Press, 1987).

4 H. Thomas Johnson, *Relevance Regained: From Top-Down Control to Bottom-Up Empowerment* (New York: Free Press, 1992).

5 Joel Stern, Bennett Stewart, and Don Chew, "The EVA™ Financial Management System," *Journal of Applied Corporate Finance*, Volume 8, Number 2, 1995, pp. 32-46.

6 Robert S. Kaplan and David P. Norton, *The Balanced Scorecard: Translating Strategy into Action* (Boston: Harvard Business School Press, 1996).

7 Gary S. Becker, *Human Capital: A Theoretical and Empirical Analysis with Special Reference to Education*, 3rd ed. (Chicago: University of Chicago Press/National Bureau of Economic Research, 1993).

8 This movement was launched by C. K. Prahalad and Gary Hamel in "The Core Competence of the Corporation," *Harvard Business Review*, Volume 68, Number 3, May/June 1990.

9 See Ikujiro Nonaka and Hirotaka Takeuchi, *The Knowledge Creating Company–How Japanese Companies Create the Dynamics of Innovation* (Oxford: Oxford University Press, 1995).

10 Although he had coined the phrase much earlier, Drucker elaborated on these issues in a book that, typically for him, caught the spirit of much of the technology-driven innovation that was just then emerging. See Peter Drucker, *The Post-Capitalist Society* (New York: Random House, 1993).

11 The PricewaterhouseCoopers Corporate Reporting framework is detailed on www.corporatereporting.com

Finding a correlation remains an elusive goal

Despite this high level of interest among both academics and practitioners, human capital measurement is still a work in progress. There is no denying that labor costs, which include training and development, contribute to financial performance in ways other than as a number to be subtracted from revenue on the way to calculating profits. Recruitment costs, team building, and other expenditures clearly bear resemblances to spending on research and development or marketing in that they build a reservoir of value for the future. They are, in some sense, assets. But what is their value? And if that can't be determined, how can we understand which efforts lead to improvements in productivity and, ultimately, financial performance?

Although many imitators have used the Kaplan and Norton scorecard to create measuring tools for human resources, the results of these metrics were often ambiguous. For example, as human resources consultant Mark Graham Brown notes, staff turnover, depending on who is leaving, can be good or bad.[12] Even the number of staff development objectives achieved can be misleading because this is often more a measure of attendance than of learning. Twenty years after widespread interest in human capital measurement emerged, Peter Howes sees little evidence that its practices have advanced very much. While better than nothing, Howes views the available measures as "simplistic concepts of aggregated metrics."[13]

Even the concept that good human resources practices build an asset value worthy of being called human capital has been difficult to implement. In Sweden, human capital measurement has been widely embraced, most famously by the insurance company Skandia, which hired Leif Edvinsson, a leading researcher in the field, as its director of intellectual capital.[14] But Ulf Johanson has detailed how difficult it can be to implement measurement systems even in a country with a supportive culture and a government that, in the early 1990s, proposed a legal obligation for all but the smallest companies to report on the full cost of human resources. Even with all of these accommodations, companies still had difficulty getting the necessary accounting and cost systems in place.[15]

Using Strategy to Guide Metrics Selection

Whether their companies have fully implemented human capital metrics or not, our survey respondents still had opinions about the types of HCMs they would like to create and put in place. When survey participants were asked about their level of interest in developing different HCMs, only one—employee productivity—of the top five measures could be considered a cost measure.

Table 2

Interest Orientation for HCMs

Human Capital Measure	Percent
Extremely high interest	
Capacity to innovate	36%
Capacity to identify new opportunities	27
Teamwork skills	23
Organization change efforts	21
New specific measures of employee productivity	17
Ability of employees to reduce costs	12
Employees' cost-conscious attitudes	8
Entrepreneurial skills	6
Significant interest	
New specific measures of employee productivity	52%
Teamwork skills	43
Capacity to identify new opportunities	42
Ability of employees to reduce cost	41
Organization change efforts	39
Employees' cost-conscious attitudes	35
Capacity to innovate	34
Entrepreneurial skills	19
Moderate or less than moderate interest	
Entrepreneurial skills	75%
Employees' cost-conscious attitudes	58
Ability of employees to reduce cost	47
Organization change efforts	39
Teamwork skills	34
New specific measures of employee productivity	31
Capacity to innovate	31
Capacity to identify new opportunities	31

Note: Due to rounding, percentages may add up to more or less than 100.

12 Mark Graham Brown, "Human Capital's Measure for Measure," *Journal for Quality and Participation*, Volume 22, Number 5, 1999, pp. 28-31.

13 Peter Howes, "The New Face of HR Metrics," *IHRIM Link Journal*, August-September 2003.

14 Leif Edvinsson, *Corporate Longitude: Discover Your True Position in the Knowledge Economy* (Harlow, Essex: FT Prentice Hall, 2002).

15 Ulf Johanson, "Why the Concept of Human Resource Costing and Accounting Does Not Work: A Lesson from Seven Swedish Cases," *Personnel Review*, Volume 28, Number 1–2, 1999, pp. 91–107.

Building a Metrics Toolbox

Despite these difficulties, the search for *predictive* metrics continues and, as with the earlier quest for improved accounting procedures, a number of new alternatives have emerged to meet this demand. Boston Consulting Group uses a system it calls "workonomics" to assess value creation by employees. "From an employee-oriented perspective, value creation is the number of employees multiplied by the difference between employee productivity and cost per employee," explains Felix Barber, Phil Catchings, and Yves Morieux.[16] They suggest a number of comparisons between HCMs and traditional, capital-driven measures, finding similarities between ROAs and employee productivity, balance sheet changes and new hires and attrition, and capital investments and workforce development plans. The Saratoga Institute, one of the early advocates of HCMs and now part of PricewaterhouseCoopers, has identified 10 key human resource-based metrics that link personnel practices to financial performance, including what it calls "human capital value added."[17]

The software company SAP tried such a model a few years ago when it was struggling with its efforts to track investments in human capital. The company's management knew these investments were growing in importance, but the systems in place to measure them were not adequate. In response, the company developed a model that measured 13 human capital processes that fed into seven human capital capabilities. One year into its turnaround efforts, SAP found that many initiatives seemed to be paying off in relatively high process and capability scores.[18]

Mark Graham Brown suggests companies draw up an initial human capital index with even fewer metrics: number of years in the business or field, level in the company by job grade or organizational chart, performance ratings, and number of positions or assignments held. The index would then assign a percentage to each of these categories. Brown also proposes a more complex index involving a component combining experience and performance measures and another grouping competencies and skills.[19]

Determining leading indicators

But how to establish which indicators are most effective? When the rankings for the most frequently used measures in Table 1 on page 7 are compared with the ratings for the measures survey participants found to be leading metrics (i.e., those that predict forthcoming impacts on the company) in Table 3, "employee engagement" was the only one that remained in the top three, indicating a lack of consensus about which metrics are leading. (See the Royal Bank of Scotland case study on page 13 for an in-depth example of how a company can use employee engagement to identify correlations between human resources practices and business metrics.)

Table 3

Leading HCMs

Human Capital Measure	Percent who consider measure a "leading" metric
Employee engagement	69%
Leadership	39
Employee commitment	37
Readiness level	34
Turnover (voluntary)	29
Employee satisfaction	29
Competence level	28
Workforce diversity	24
Training	21
Promotion rate	17
Executive stability (or churn)	17
Workforce age	16
Health and safety	14
Span of control	9
Depletion cost	6
Other	0

16 Felix Barber, Phil Catchings, and Yves Morieux, "Rules of the Game for People Businesses: Succeeding in the Economy's Highest Growth Segment," Boston Consulting Group report, 2005. The report is available at www.bcg.com

17 See Robert J. Grossman, "Measuring Up: Measuring Human Resources Performance," *HR Magazine*, January 2005, pp. 28–35. "Human capital value added" equals revenue, which is equal to operating expenses minus the combined compensation and benefits costs divided by total employment measured in full-time equivalents.

18 Susan Cantrell, James M. Benton, Terry Laudal, and Robert J. Thomas, "Measuring the Value of Human Capital Investments: The SAP Case," *Strategy & Leadership*, Volume 34, Number 2, 2006, p. 45.

19 Brown, "Human Capital's Measure for Measure."

Although Michael Bokina, former manager at Saratoga/PricewaterhouseCoopers, stresses that every organization is different, making it difficult to offer “typical” leading indicators, generic correlation analysis showed that three HCMs were leading indicators for Saratoga:

Executive stability ratio and voluntary separation rate Corporations with executives having more than three years’ executive experience lower voluntary turnover.

Management ratio and promotion rate The fewer the number of employees that each manager or executive supports impacts the number of promotions. Span of control is important in developing employees professionally.

Training investment factor and promotion rate More dollars allocated to training will increase professional employee development.

Anticipating potential problems

Companies should be aware that even the most carefully selected measures can fail to deliver desired results. For example, many metrics are only reported at the highest levels of aggregation, which may only be sufficient for understanding what is happening in functions with a large number of largely undifferentiated workers. As Mark Huselid, Richard Beatty, and Brian Becker point out, “Companies simply can’t afford to have ‘A players’ in all positions. Rather, businesses need to adopt a portfolio approach to workforce management, systematically identifying their strategically important A positions, supporting B positions, and surplus C positions, then focusing disproportionate resources on making sure A players hold A positions.”[20] The risk associated with having the wrong person in a job is as high as the opportunity cost of keeping an A person in a C job. The implication is that human capital measurement needs to be quite granular. The authors state, “We all know that effective business strategy requires differentiating a firm’s products and services in ways that create value for customers. Accomplishing this requires a differentiated workforce strategy as well.”[21]

Moreover, even when measures are calibrated for a differentiated workforce, HCMs can backfire if not properly integrated with the complex system of the organization. John Boudreau and Peter Ramstad find that attempts to link human resource practices to strategic aims are often crude and not really integrated.[22] An organization might have the strategic goal to increase sales of solutions and then set a human resources measure to increase bonuses for solutions-selling activities. But without business integration to ensure that products themselves integrate into solutions or that the right talent pools are in place, the bonuses won’t work.

The Value of Adding Metrics to Business Plans

“Include HC metrics in the business plan. That will get the business to take a more holistic approach, rather than just focusing on one metric–the financial one. It was instrumental to get three HC metrics into the business plans:

Employee opinion surveys What are response rates, satisfaction levels, and action plans?

War for talent What are we doing to retain people and monitor turnover?

Embedding diversity What have we done to make this a way of doing business?

Showing this in a performance scorecard made sure it was in everyone’s line of sight. HCMs were embedded into processes.”

Kevin Prue
Vice President of Human Resources Planning
Prudential

20 Mark A. Huselid, Richard W. Beatty, and Brian E. Becker, “‘A Players’ or ‘A Positions’? The Strategic Logic of Workforce Management,” *Harvard Business Review*, December, Volume 83, Number 12, 2005, pp. 110-117.

21 Huselid, Beatty, and Becker, “‘A Players’ or ‘A Positions’?”

22 John W. Boudreau and Peter M. Ramstad, “Strategic HRM Measurement in the 21st Century: From Justifying HR to Strategic Talent Leadership,” Cornell University Working Paper, 2002.

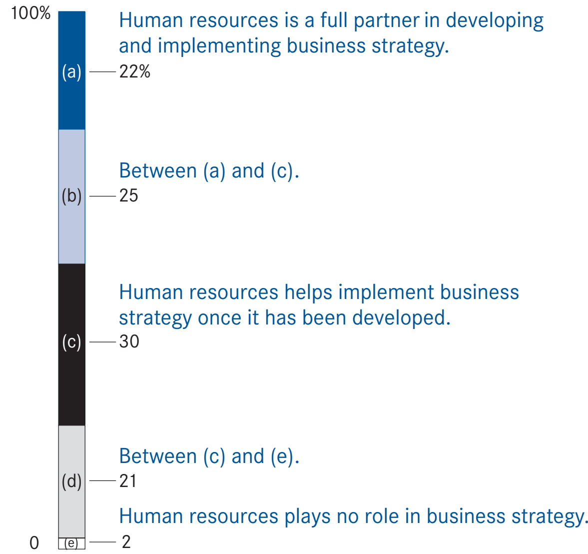
What Is the Impact of HCMs on Strategy?

The hope persists that an "ideal" list of human capital measures, especially prospective human capital measures, could exist and that these measures could prove how investments in people can deliver bottom-line results for business strategy. Rather than continue this possibly quixotic search, companies might find it more practical to investigate the role that the human resources function plays in strategy. In the 2006 survey, only 22 percent of respondents claimed that the human resources function is a full partner in developing and implementing business strategy. More than half of the respondents responded that the function had "no role" in strategy or simply implemented business strategy "once it has been developed." Not only does this lack of involvement in formulating or implementing strategy limit the ability of human resources to understand managers' business KPIs, it could also explain why so few companies create HCMs to gauge the organization's capacity to innovate or to identify new business opportunities.

For executives who wish to manage and measure their workforce in conjunction with human resources, Huselid, Becker, and Beatty advocate a human-resources-specific scorecard as a supplement to their companies' existing scorecards.[23] They also encourage senior executives to take greater responsibility for setting human capital measures and targets. In this way, human resources' lack of involvement in setting strategy would not hinder the execution of the company's people strategy.

Chart 1

Describe the relationship between the human resources function and business strategy in your company



[23] Mark Huselid, Brian Becker, and Richard Beatty, *The Workforce Scorecard: Managing Human Capital to Execute Strategy* (Boston: Harvard Business School Press, 2005).

CASE STUDY

Royal Bank of Scotland Group

Building a Human Capital Model to Create Greater Cohesion and Better Communication

The Royal Bank of Scotland Group (RBS) is one of the world's largest financial institutions, with over 40 brands, 35 million customers, 135,000 employees spread across 30 countries, and 2006 operating profits of £9.4 billion ($17 billion). But the current company is very different from the RBS of the late 1990s, which was a modest-sized bank with 35,000 employees based mainly in the United Kingdom.

As might be expected, the human resources function has changed along with the company. "Pre-1996, the human resources function was predominantly transactional, more of an order-taker than a strategic partner," explains Greig Aitken, head of human capital strategy at RBS. "Following the appointment of Neil Roden as human resources director in 1997, we embarked on a business partner/shared services model that would transform human resources into a more business-focused and value-driven function. This included centers of excellence, business-facing human resources teams, and a shared services infrastructure."

This new model was well in place by the time of RBS's acquisition of National Westminster Bank (NatWest) in 2000. At $30 billion dollars, NatWest was, at that time, the largest purchase in the company's ongoing program of growth by acquisition and organic growth. RBS's pursuit of this multi-brand strategy has allowed it to capture the benefits of the high awareness of acquired brands in their various geographic markets. For example, while the Royal Bank of Scotland isn't limited to Scotland itself, NatWest had a stronger presence in England and Wales. In North America, Citizens Financial Group, a company that RBS acquired in 1988, pursued its own strategy of growth through acquisition. By purchasing a host of small banks and then absorbing Charter One in 2004, Citizens has now become the ninth-largest banking group in the United States by assets. But, Aitken says, it wasn't until after the NatWest acquisition that the company "developed an integrated human capital strategy that would have at its core the ability to help RBS leaders understand the effectiveness of their people strategy and its impact on business performance—a line of sight between intervention and impact."

This project dovetailed nicely with the broad aim of Sir Fred Goodwin, RBS's chief executive, to become the world's "Most Admired Bank," an aspiration that was based on a strategy of differentiation rather than pure cost leadership.[24] Achieving Goodwin's goal in a people-oriented business like banking would require an emphasis on the effectiveness of the workforce in delivering quality service with a high degree of impact on customers.[25] To do so, RBS needed to define its commitment to service delivery and business outcomes; help corporate, divisional, and local management use human capital more effectively; and measure the links between employee behavior and business results to determine the impact of its employee proposition, including compensation and flexible benefits plans on employees. In pursuit of these aims, the company started development of the "RBS Global Human Capital Strategy & Toolkit" in 2003.

Measuring Performance

RBS's growth-through-acquisition and organic growth strategy and the need to maintain strict separation of business types and geographies in a highly-regulated industry like banking make it difficult to produce centralized coordination, let alone common practices. But the performance elements needed for strong service delivery suggest there are many benefits to pooling best practices and disseminating learning widely and quickly throughout the organization. Bearing this in mind, RBS adopted an approach that was both global and local in

24 Differentiation, cost leadership, and niche strategy are the three generic strategies outlined by Michael Porter in *Competitive Strategy: Techniques for Analyzing Industries and Competitors* (New York: The Free Press, 1980).

25 Many of the human resource measures that influence strategy can be sorted into the three categories devised by John Boudreau and Peter Ramstad: efficiency (the level and quality of human resources practices produced from the resources available), effectiveness (the relationship between human resources practices and the quality of people), and impact (the relationship between changes in the quality of employees and competitive success). As we shall see, this project also yielded efficiencies, as well as effectiveness and impact. See John F. Boudreau and Peter M. Ramstad, "Strategic HRM Measurement in the 21st Century: From Justifying HR to Strategic Talent Leadership," in *HRM in the 21st Century*, Marshall Goldsmith, Robert P. Gandossy, and Marc S. Efron, eds. (New York: John Wiley, 2003), p. 7.

scope and contained a loose-tight mix of components based around a toolkit of survey techniques and measurements of behavior that provide comparable data across business units, by job function, and, where appropriate, between geographic business units.

The human capital model that grew out of this approach measures the central "employee proposition" through a variety of different survey types. The effectiveness of this proposition is then set against an array of business metrics. These measures then feed into decision-making processes about leadership, incentive design, recruitment, and the business program. It is the predictive nature of these measurements that has allowed the group to spread best practices throughout the business units.

Taking the pulse of employees

Under the Human Capital Model, RBS conducts an annual survey of all employees. Aitken says, "The survey goes out to 135,000 staff in 30 countries in nine languages online and on paper." In addition to a number of questions that also appear in the company's joiner, leaver, and pulse surveys, this questionnaire includes 16 questions that allow the group to monitor what it considers the eight drivers of employee engagement:

- employee recognition
- performance and development opportunities
- relationships
- total reward
- "the work itself"
- product brands and reputation
- leadership
- work-life balance[26]

Because of the global consistency of the core questions, RBS is able to segment its employee base and then compare business units (e.g., the marketing department) in one business with their counterparts elsewhere in the group, measure the performance and attitudes of people in one division against those in another, and judge the needs and interests of employees by age, gender, country, etc.

In 2006, some 87 percent of the workforce took part in the survey—at least 20 percent higher than is the average in the financial services sector—which suggests a high level of commitment to the company.[27] Furthermore, high scores for the group, the divisions, the business units, and even individual bank branches suggest a strong sense of engagement among the employees, which, in turn, has a high predictive value for business performance. According to Aitken, engaged employees contribute to the business by **saying** (speaking consistently and positively about RBS to colleagues, potential employees, and customers), **staying** (showing an intense desire to be an RBS member), and **striving** (giving the extra effort and behaving in ways that contribute to success). This extra effort manifests itself in financial performance and leading indicators of performance, such as the level of cross-selling.

RBS also conducts other significant measurement initiatives throughout the year:

- All new joiners and all people leaving the company are surveyed.
- Ad-hoc issues are assessed with "pulse" surveys, and the results are then mapped against the global database of personnel records. In one instance, a survey was conducted to discover why some people apply for and go through the recruitment process for certain positions and then turn down the job when it is offered.
- Outside of the company, RBS measures itself against its competitors with the use of "paid for" norms.

The consistency and high response rates of these surveys—all of which are undertaken with the promise of complete anonymity for the employee—allow RBS to formulate a proposition for employees and identify correlations between human resource practices and business metrics like customer service, profitability of bank branches, staff turnover, and financial performance metrics.

26 While this standard "core" questionnaire is used for the whole group, options do exist for business-specific questions as necessary.

27 Source: "Case Study: Capital Performance," *HR Director Magazine*, April 2006, pp. 36-37.

Refining the employee proposition

The Human Capital Model has given the group the ability to monitor its employee attitudes and intentions much more closely and fine-tune its offerings accordingly. One initiative tracked employees' use of RBSelect, the bank's flexible reward program that allows employees to tailor their own reward packages. After examining the results of this inquiry, RBS was able to identify that the "employee engagement" scores of employees selecting three or more items from the menu were 20 percent higher than the norm. Insights such as this enable RBS to develop a more compelling reward strategy and a stronger employee proposition.

The ability to segment employees according to a variety of criteria also helps focus communication about these benefits. "For every pound or dollar spent on segmented communication to these groups, it appears to be twice as effective compared to nonsegmented communication," Aitken says. In effect, it doubles the effectiveness of internal communications.

All of the bank's individual efforts have also helped direct global human resources policy. The following objectives for 2006 from the RBS Corporate Responsibility Report were heavily influenced by the Human Capital Strategy and the Group's employee opinion survey:

- Implement actions to improve customer focus and performance management and development scores.
- Use the Human Capital Toolkit to identify and address specific areas of the business where improved employee performance would most directly result in increased levels of customer satisfaction.
- Introduce the Human Capital Toolkit to RBS businesses in North America.
- Introduce a new executive leadership program to develop the innovation skills of senior management.
- Introduce measures to meet the needs of disabled employees.

The Advantages of an Online Toolkit

Just as RBS has used its Human Capital Model to create a rich warehouse of data, the bank has innovated new ways of disseminating both findings and the information and methodology behind them to individual businesses and their human resources functions. One of the primary vehicles for spreading this information has been the company's online Human Capital Toolkit, which was launched in January 2005 after only six months of development. Aitken and his team, drawing on lessons from the group's customer websites, designed the site so that it would take no more than five clicks to get to anywhere from the front page. (See "Key Elements of the Human Capital Toolkit" for a detailed list of the site's contents.)

Key Elements of the Human Capital Toolkit

1. **Survey toolkit** This element offers a do-it-yourself survey utility that allows business units to conduct ad-hoc and "pulse" surveys, view global survey results, and access more than 1,000 interactive tools.
2. **Reporting toolkit** This knowledge bank allows visitors to read internal management reports and external human capital reports. It also provides access to presentations from throughout the group that staff can use in their own briefings without having to replicate all the drawings or reproduce all the text and explanatory documents.
3. **Benchmarking toolkit** This component contains comparable metrics from a selected range of peer group companies.
4. **Research toolkit** This section offers access to external research that is collected and collated to avoid duplication of data while ensuring breadth.
5. **Measurement toolkit** Human resources managers can use the metrics contained in this section to drill down to human capital measures for every cost center worldwide.

The current secure intranet site contains both analytic and survey tools, benchmarking norms, links to external sources (including the RBS Business School created in conjunction with Harvard Business School), and third-party research data (e.g., reports from The Conference Board). Because of their new access to these resources, human resources teams no longer have to make requests to the head office or seek external support when they want to conduct their own research.[28] Moreover, the Toolkit permits human resources professionals to commission research and analysis on any topic straight from the desktop of human resources staff. Once a request is received, external partner researchers in Washington and London begin work on the subject and report back to the questioner within two weeks. Conversely, the site prevents business unit managers from "making up their own surveys" and allows RBS to benchmark and segment their pulse surveys in a manner similar to their global survey.

Surprisingly, the cost of the Toolkit was relatively modest. Most of the work was done internally, using many components—including security features—from other internal sites and customer banking websites developed elsewhere in the group. Aitken also used internal design, marketing, and technology resources from around the group. Not only was the initial price tag low, but Aitken's introduction of consistent pulse survey design, delivery, and reporting tools (developed internally within RBS) saved the business over £340,000 in the site's first 10 months of operation. The toolkit gives access to analysis and diagnostic tools (e.g., benchmarks and historical analysis). "It's been a real boon for us to be able to share key information globally from one single site," Aitken says.

28 While only authorized human resources professionals have access to the full suite of applications, the usefulness of the information on the site has led RBS to consider releasing select components to business managers.

Stages of Implementation

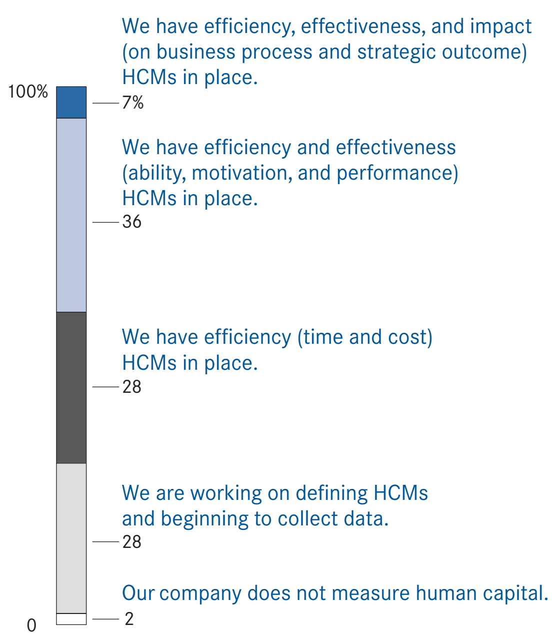
Successful and strategic application of HCMs—from initial conception to execution to distribution of results—is a long and difficult process.

The first step in strategic HCM formation is the determination of an accurate headcount, which can be a formidable task for large global companies. Once this figure is calculated, human resources departments can begin tracking the cost of activities with efficiency measures of time and cost. As their processes mature, companies can move on to monitoring investments in workforce capability with HCMs regarding efficiency and effectiveness (e.g., ability and motivation metrics). In the final step, companies can introduce impact measures to concentrate on business process and strategic outcomes. Only 43 percent of survey respondents described themselves as having reached these last two stages, which are the phases where the greater benefits of linking HCMs to strategy are realized (Chart 2).

Even though they may not have attained their desired level of HCM implementation, respondents to the survey found few of the challenges they were asked about in the survey "extremely" difficult. It is particularly encouraging to note that buy in—whether from senior management, middle management, or human resources business partners—was allocated a "moderate" difficulty rating by over three-quarters of the respondents (Chart 3). This would seem to imply that attitudes have changed since a 2003 survey by The Conference Board in which one of the participants, in response to an open-ended question on the reasons behind resistance to implementing HCMs, wrote, "Management doesn't consider HR a business partner."[29]

Chart 2

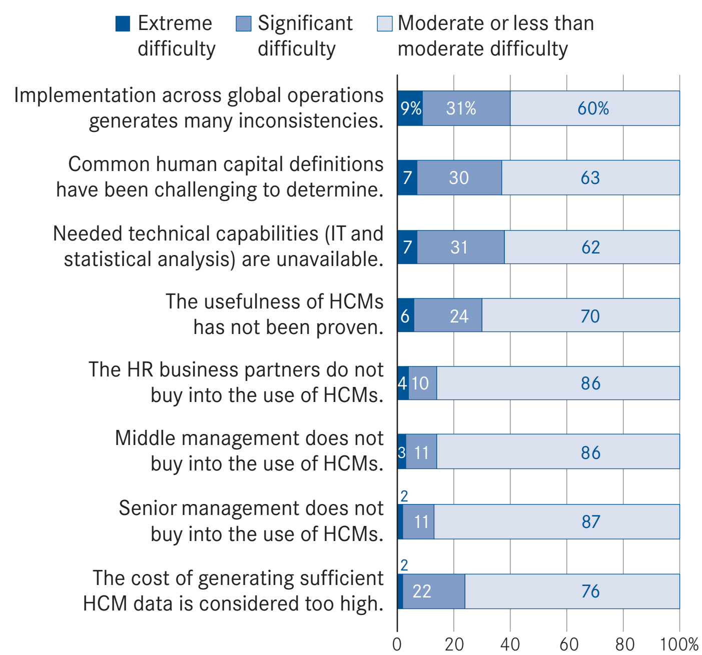
Stages of HCM implementation



Note: Due to rounding, percentages add up to more than 100.

Chart 3

Rating challenges to HCM implementation



29 Stephen Gates, *Linking People Measures to Strategy: From Top Management Support to Line Management Buy-in*, The Conference Board, Research Report 1342, 2003, p. 24.

Ranking the Greatest Challenges

Facing an institutional digital divide

Instead of citing resistance from colleagues as a significant challenge, survey participants pointed to the difficulties involved with the operational aspects of defining, harmonizing, and executing an international HCM program. When the "extreme" and "significant" difficulty scores are combined, lack of necessary technical capabilities is second only to inconsistent global implementation as a difficulty. Technology issues were also frequently mentioned by research working group members. "One challenge which limits the impact of HCMs is that our HR metric updates compete for HR IT resources with many other high priority projects," says Amy Balensiefen, employee research consultant, John Deere & Company. "Moving forward, it is critical for us to educate our organization on the value that HCMs provide the business."

As for diagnosing business problems using the analytical capabilities of HCMs, one research working group member says, "Linking human capital data with measurement from outside human resources (customer, business operational, financial) isn't as easy as you might think. In addition, we want to focus on positions in the company that are strategically important. That requires a lot of process, and it requires a redesign of IT capabilities to allow decision support over only that subset of the position."

Table 4

Top Four Challenges to HCM Application

Implementation across global operations generates many inconsistencies.	40%
Needed technical capabilities (IT and statistical analysis) are unavailable.	38
Common human capital definitions have been challenging to determine.	37
The usefulness of human capital metrics has not yet been proven.	30

Note: Percentages represent a combination of the "extreme" and "significant" difficulty scores for these challenges. Multiple answers allowed.

Matters of definition

The problems associated with the third place "extreme"/ "significant" challenge—"Common human capital definitions have been hard to determine"—are widespread. In an SHRM survey of American companies in 2002, two-thirds of the respondents did not have a consistent way of describing human capital.[30] As the experience of one research working group member indicates, even harmonizing the definition of "promotion" worldwide can create quandaries. In some countries where the company operated, a promotion was defined by upward movement in the company. In others, promotions were primarily associated with an increase in salary and benefits. Since nearly 80 percent of employees are working under one definition, the company's HCM team is hoping that the remaining 20 percent will slowly adopt and accept the majority definition.

Organizing the HCM Group

Another issue of special interest to research working group members that was not included in the survey is the formation of the HCM group. While some organizations have a clear organizational unit devoted to HCMs, many research working group members say that such work in their organization is spread across various corporate human resources services. While much can be gained from having such a group, there are also potential liabilities.

Gaining Accountability for HCMs

When asked in an informal survey about accountability for HCMs, a majority of research working group members indicated that the lines of responsibility are not clear. The written comments of those who said their companies have transparent accountability for such projects offer a range of possibilities for the use of HCMs:

"Human resources is responsible for collecting data; senior executives for use."

"If the HCMs are key corporate measures, human resources measures them and business managers report them to the chairman."

"HCMs are included in the business plan."

"HCMs are inserted into business processes, workforce planning, and annual incentives."

"HCMs are tied to business results and individual executive compensation."

"HCMs are included in the scorecard and performance evaluation process."

30 *Aligning HR with Organization Strategy Survey*, SHRM Research, November 2002.

Getting the Word Out

Partners in the application of HCMs, therefore, must understand the metrics and know how to apply them. Responses from the survey about the use of HCMs in linking people activities to business managers' KPIs, which was considered the most effective application of such metrics, reveal there is a divide between the two tasks. Although 75 percent of respondents said they recommended measures to managers as a way to meet these KPIs, only 15 percent reported that business managers used the metrics for this purpose to a "significant" or "total" extent. This low use rate may be due to inadequate communication of the benefits of HCMs to human resources business partners, who, in turn, are unable to advise their managers about using such metrics.

Chart 4

Rate of recommendation of HCMs to meet KPIs

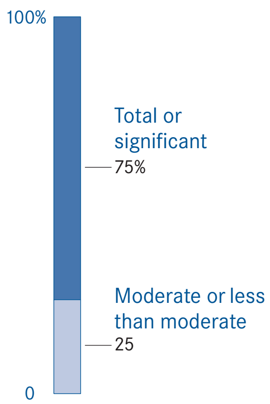
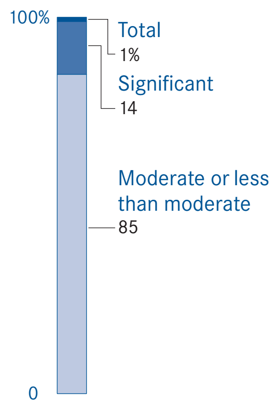


Chart 5

Rate of use of HCMs to meet KPIs



Different Avenues for Display

HCMs work best when they are considered in relation to each other. This is why many companies choose to put them in one of two types of frameworks:

Scorecards provide a means by which HCMs are viewed in alignment with execution of the company's overall strategy.

Dashboards are graphic interpretations (gauges, dials, etc.) of trends based on selected benchmarks or metrics.[31]

A comparison of the HCMs found in working group members' scorecards uncovers clear metrics preferences for the manufacturing (efficiency measures), high technology (effectiveness or innovation measures), and financial services (efficiency and effectiveness measures) sectors. No matter what metrics are incorporated into a scorecard or dashboard, they can serve as useful tools for focusing management attention.

31 Definitions are taken from John Gibbons and Christopher Woock, *Evidence-Based Human Resources: A Primer and Summary of Current Literature*, The Conference Board, Electronic Report 15, 2007, p. 8 (scorecards); and Marc S. Miller, *Establishing Value for HR Technology*, The Conference Board, Research Report 1350, 2004, p. 17 (dashboards).

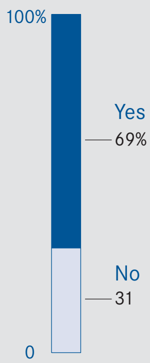
Causal Models: The Framework of the Future?

Of the 69 percent of our survey respondents who used either a dashboard or a scorecard, a majority (53 percent) said they were “moderately” or “less than moderately” effective.

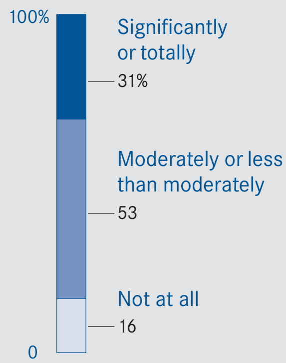
One of the reasons for this tepid response may be the limitations of the format itself. “A scorecard keeps the score, which is fine, but that is all that it does,” says one research working group member. “On the other hand, creating and testing a causal model shows impact on business outcomes so you can become more of a strategic consulting partner.”

For example, when this member was working at a large transportation company, injuries in the workplace were on the rise.

Does your company use HCMs in a dashboard or scorecard?



If so, how effective do you consider your dashboard or scorecard?



When the human resources department was tasked with reducing accident costs, team members investigated the problem using a causal model. Since safety managers could not agree on the source of the problem, many different hypotheses were used. Some suggested poor safety training; others, traffic conditions or weather. After reviewing a safety survey, the HR team created a causal model including multiple factors related to safety training, promotion, and climate.

Two of the factors that caught the attention of the investigators were equipment availability and training. The causal model provided evidence that these two factors were the source for a significant percentage of injuries. In essence, employees were getting hurt because they were carrying multiple heavy boxes on their shoulders when they should have used the proper equipment. Unfortunately, the lack of such equipment, which could be obtained at minimal cost, was the cause of workplace injuries. A major investment in equipment led to significant savings in accident costs, not to mention the avoidance of employees’ physical pain. One year later, the company reported the lowest amount of accidents ever, even though the number of drivers was at its highest.

In order to reinforce this equipment-based safety practice, targets in managers’ scorecards were changed. Managers are now evaluated on whether equipment is fully available and working at all times. In addition, as part of the employee survey, managers are rated on their efforts to promote safety.

Communicating Results: To Whom? How Often?

Once HCMs have been carefully assembled and used to gather data, who should receive the final results and the related analysis? In terms of releasing results to top management, 78 percent of respondents said they released their findings on a quarterly basis and 52 percent distributed them on a monthly basis. The latter reporting schedule is preferable because it allows the measures to be of greater help in identifying where corrective action is needed at an earlier stage.

Not only does the timing of the reporting vary from company to company, there were wide differences in the number of measures presented to top management as well, ranging from 24 percent of companies that reported one to three HCM measures to 26 percent that delivered the results from more than 10 HCMs. Half of respondent companies offered between four and 10 HCMs, reflecting the belief of performance management experts that managers may have difficulty focusing on more than seven measures at a time.[32]

Widening the audience for HCM results

When asked who received the internal human capital report in a 2004 survey conducted by The Conference Board, 78 percent of the respondents said that top management received the "people measure" report and only 19 percent indicated that all business managers were given the findings.[33] Responses to a similar question in the survey conducted for this report indicated that nothing had changed: the percentage of companies offering these documents to all business managers still stood at 19 percent.

Companies who do broadly release their HCM reports are working to make sure that the results are spread throughout their organizations. According to one research working group member, her organization plans to cascade HCMs downward through the company to increase their impact on core, strategic, and people-plan specific KPIs.

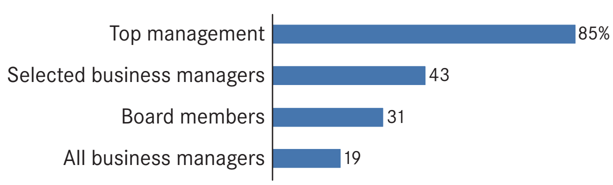
Chart 6

Frequency of reporting to top management*

* Multiple answers allowed

Chart 7

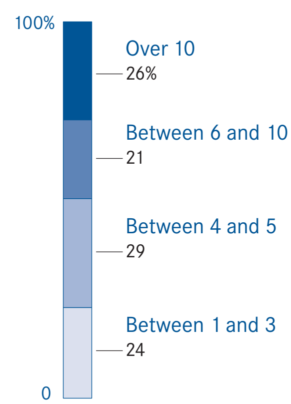
Distribution of the HCM internal report*



* Multiple answers allowed

Chart 8

How many HCMs do you report to top management?



32 See Antonio Davila, Robert Kaplan, and Robert Simons, *Performance Measurement and Control Systems for Implementing Strategy*, (Upper Saddle River, NJ: Prentice Hall, 2000), pp. 239-240.

33 Gates, *Measuring More Than Efficiency*, p. 30.

Linking Metrics Performance to Compensation

Embedding HCMs in managers' bonus plans is another way to sharpen managers' focus on human capital metrics and targets. While they might not agree with the construction of the metrics or the measures as targets, managers will certainly become more aware of the company's people goals. Results from a 2003 survey by The Conference Board showed that many survey respondents believed putting HCMs in bonus plans correlated with successful links between business strategies and certain measures (turnover, leadership, and health and safety).[34] Despite their confidence in these measures, only 39 percent of participating companies in that survey said they included these measures in bonus plans. In the survey conducted for this report, 57 percent of respondent firms rewarded managers based on HCMs and 60 percent used them in setting managers' management by objectives (MBO). Moreover, 48 percent reported that HCMs received over a 15 percent weighting in bonus plans. At that level of weighting, managers should have a strong interest in taking HCMs and people activities more seriously.

One working group member says his company's performance evaluation process relies heavily on HCMs: "First, we update divisions regarding their degree of overall differentiation in terms of the percentage and number of high/core/low performers. Second, we provide details around that differentiation by key demographic groups to help divisions get a better sense for how performance has been evaluated across groups. Finally, we provide similar information for actual bonus/merit dollars that have been allocated to determine whether the financial rewards are equally differentiated."

When respondents who included HCMs in bonus plans were asked if their metrics were aligned with business targets, 64 percent admitted that they were "moderately or less than moderately" or even "not at all or slightly" aligned with bonus plans. Roughly the same percentage of respondents—65 percent—reported moderate or less strategic alignment of HCMs in managers' MBOs. This lack of alignment does not bode well for the role of HCMs in helping managers achieve their strategic business goals or KPIs. Such imprecision can lead to dissatisfaction with the measures used and result in poor manager evaluations of the HCM program.

Chart 9

Does your company use HCMs in managers' bonus plans?

If yes, what weighting do you give to them?

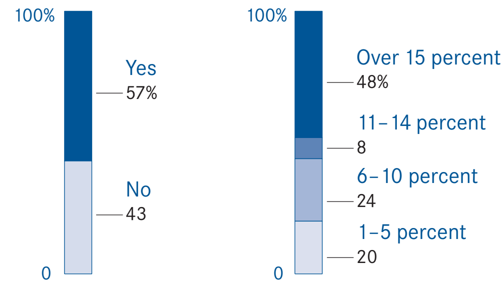


Chart 10

Does your company use HCMs in determining managers' MBOs?

If yes, how well aligned are these HCMs with business targets?

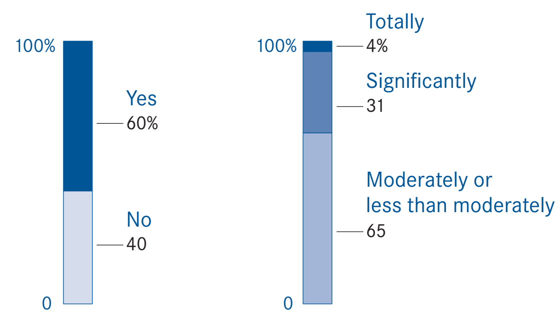
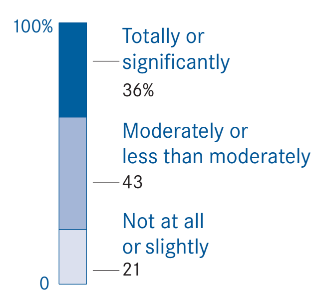


Chart 11

How well aligned are HCMs with business targets?*



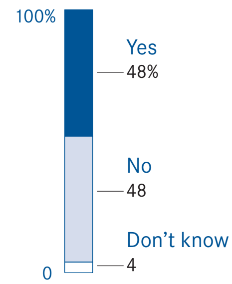
* Results are only for those who indicated they used HCMs to determine MBOs.

34 Gates, *Linking People Measures to Strategy*, p. 26.

Once again, it is not enough for managers to buy into or be "sold" on the idea of HCMs; they must also understand the measures well enough to use them to improve on their own performance. Training programs and concrete action plans are two ways to help generate greater acceptance among managers. One working group member from a global IT company also suggested it might be easier to "sell" HCM projects to managers if they are positioned as a means to help business leaders manage their workforce rather than as a way for the human resources department to improve its own functional activities. Managers at Marriott Vacation Club International (MCVI) were trained to coach their employees toward higher engagement and performance. The HCMs used in this process provided both guidance and proof that their talent relationship management program delivers higher business performance. (For more information on how they achieved this result, see the case study on page 24.)

Chart 12

Do you report HCMs outside of the organization?



If yes, are your HCMs verified by an external audit?

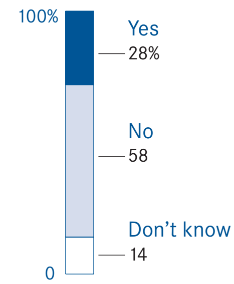
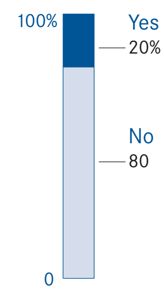


Chart 13

Have investment analysts asked your company to report or discuss HCMs?



Broadcasting HCM Results Externally

HCM reports also have potential uses for when a company needs to provide findings about its human capital activities to outside organizations and interested individuals. While the primary reason for external reporting may be to help in recruitment efforts, companies can also target investors—especially socially responsible investors—NGOs, and local governmental authorities. Just under half of the survey respondents—48 percent—released HCM reports externally, a significant improvement over the 15 percent of companies who released reports in this manner in the 2004 survey.[35] Over one-quarter of the respondents also said that their HCMs were verified by external audit.

Although traditional financial analysts have difficulty incorporating information about human capital into their valuation models, there are encouraging signs that suggest long-term and socially responsible investors take HCMs into consideration. In the survey conducted for this report, 20 percent of respondents said that investment analysts asked their companies to report or discuss HCMs.

35 Gates, *Measuring More Than Efficiency*, p. 30.

CASE STUDY

Marriott Vacation Club International

Enhancing Engagement and Performance through Talent Relationship Management

When Marriott Vacation Club International (MVCI) was established in 1984 as the vacation ownership division of Marriott International, Marriott became the first branded hospitality company to enter the time-share industry. Today, MVCI operates 57 resorts across four distinct brands: Marriott Vacation Club, Horizons by Marriott, Grand Residences by Marriott, and The Ritz-Carlton Club. In 2006, in addition to delivering its 10th consecutive year of 20 percent or greater average annual growth, it also collected the award for "Best Sales Organization in America" at the 2006 American Business Awards.

According to Karl Sweeney, MVCI's senior vice president and chief administrative officer, the use of talent relationship management tools to achieve higher performance has been a driving force behind the company's positive performance. He explains, "The credo for Marriott has always been take care of your associates and they'll take care of your customers, who, in turn, will take care of the bottom line." Sweeney also notes that the support of Peter J. Watzka, former executive vice president and chief customer officer for MVCI, for several cutting-edge initiatives over the past several years has led to greater investment in associates as a strategy for increasing associate engagement and driving financial outcomes.

More specifically, the company has found that there is a compelling correlation between (1) selecting the right associates for customer-facing positions, focusing managers on associate engagement through frequent engagement surveys, and training associates and managers to focus on their strengths; and (2) engagement and multiple performance outcomes. This connection is the result of a process that MVCI has been creating, implementing, and tracking since 2002.

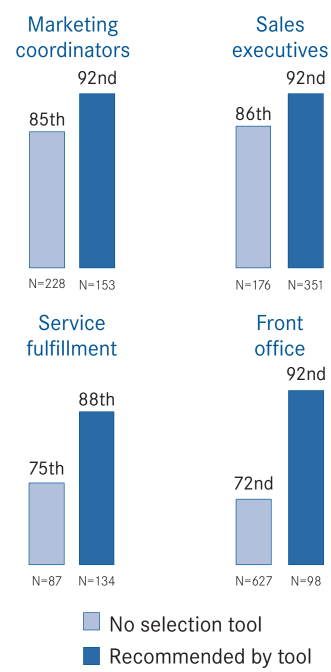
Looking for the Right Fit

In the spring of 2002, Watzka's customer relationship management organization (CRM) turned its focus to finding employees with the "right fit" as a way of increasing performance. In its initial project, the CRM collaborated with The Gallup Organization on applying the latter's talent-based hiring process to associates in sales roles. Over the next several years, MVCI rolled out similar selection tools for its customer acquisition, service fulfillment/delivery, and customer experience subprocesses. On every associate engagement survey and across multiple business outcomes (such as productivity, customer metrics, and turnover), associates that were selected using these tools were found both to be more engaged than associates not selected through these tools (Chart 14) and to outperform their less-engaged counterparts.

Chart 14

Associates chosen using selection tools are more engaged

FQ2 grand mean relative to Gallup database, fall 2005



Source: MVCI

Two years later, MVCI piloted the use of Gallup's 12-question (Q^{12}) survey tool as a way to find out its associates' levels of engagement and the impact their engagement had on business outcomes. The Q^{12} identifies those elements that matter most to employees, starting with basic needs and then advancing through leadership, support and teamwork, and aspirations for growth. By measuring associate engagement in these categories at six-month intervals, MVCI was able to accumulate data that showed a clear correlation between increased engagement and business metrics of productivity, profitability, customer satisfaction, retention, and safety. By 2005, the Q^{12} was being offered to approximately 100 percent of MVCI's almost 10,000 associates, and the survey enjoyed an 85 percent reply rate. Comparisons between the 2004 and 2005 test dates showed improved scores.

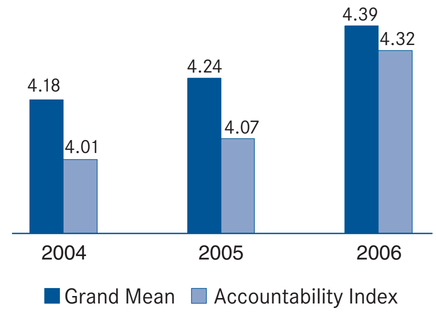
When MVCI is compared to other companies in Gallup's database, almost seven out of 10 MVCI work groups are at the 75th percentile and 3.6 out of 10 are at the "world-class" level (95th percentile compared to Gallup's worldwide database). Sweeney says that the ability to benchmark MVCI against the more than 400 companies, 4,000 work groups, and 4 million employees in Gallup's worldwide database is one of the greatest values of this measurement. The company's efforts have also resulted in an engaged to actively disengaged ratio that is 4.5 times better than the overall U.S. working population.

As MVCI administered repeated Q^{12} surveys, the data showed that managers who took certain steps in conjunction with each survey were able to positively impact associate engagement. MVCI leadership has not only aggressively trained its managers to perform the steps, but has included three questions (called the "Accountability Index") as supplements that measure manager performance to the semi-annual Q^{12} survey.

The steps managers took were (1) providing one-to-one feedback on the work group's survey results to each of his or her associates, and, following these discussions, (2) letting the work group formulate an action plan that it then strives to achieve. Associates then rate their managers on the subsequent Q^{12} survey Accountability Index which asks whether they received feedback, if an action plan was made, and, if so, what progress was made against that plan.

Chart 15

Grand Mean and Accountability Index move concurrently



Source: MVCI

This feedback loop to MVCI's associates is strongly correlated with higher engagement. The Accountability Index has also been incorporated into the balanced scorecard measures that are used to report on the company's achievements against goals. By doing so, the company ensures that this remains a focus for management (Chart 15).

Developing Strengths across the Company

Along with the implementation of talent selection tools and Q^{12}, MVCI has also adopted two other Gallup tools. The Clifton StrengthsFinder®, a newly-created developmental assessment tool, was added to help associates discover how they can maximize their performance. MVCI also began using Gallup's two-day StrengthsCoaching curriculum and certification program, which allows associate-facing managers the opportunity to understand their own talents and strengths and improve their ability to coach associates to success, build effective relationships, and acknowledge associates in an appropriate manner.

CRM led the way in using both of these processes. These tools had unique descriptors of Gallup's 34 themes, and personalized plaques displaying associates' signature "themes" soon began dotting CRM offices, creating internal momentum for change. By late 2004, MVCI had created an additional intervention called Great Manager Fundamentals. During this four-day training session, managers learn more about selecting for talent, building one-to-one associate relationships, coaching for performance, and problem solving in the context of team building. This program is taught in the "Strengths" vernacular and ideally follows three to five months after StrengthsCoach certification.

Under the direction of Roy West, MVCI's master strengths trainer and vice president, customer acquisition talent, the company has now trained 1,200 strengths coaches and given over 5,000 of its associates the opportunity to complete the StrengthsFinder assessment. Each associate completing the StrengthsFinder process takes part in a one-to-one strengths interview with his/her certified coach or manager. Also, over 500 of MVCI's coaches, managers, and leaders have gone through the Great Manager Fundamentals program.

Higher Engagement Equals Higher Performance

Analysis of the results of the first survey of managers that had been trained on StrengthsCoaching and Great Manager Fundamentals confirmed that higher associate engagement was linked to higher associate performance. Participation in Great Manager Fundamentals has also been found to correlate with manager and associate engagement. Managers trained and certified as StrengthsCoaches were not only more engaged than those managers who had not taken part in the program, their associates were also more engaged and outperformed associates who were managed by noncertified managers (Chart 16). Because of these results, other parts of the MVCI organization started asking for access to these programs. In 2006, West's Talent Relationship Management (TRM) training group led MVCI's efforts to deploy the new tools throughout the company.

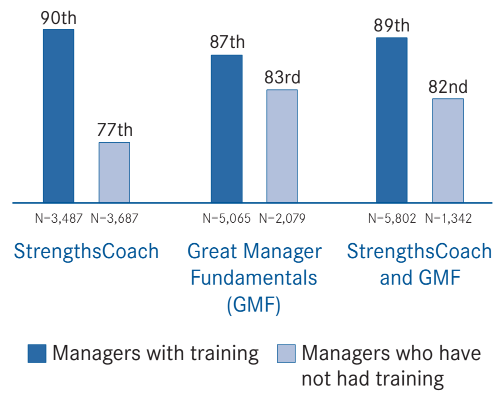
When employee engagement is correlated with various business metrics, its impact is clear. For example, if employee engagement scores from the bottom quartile, middle 50 percent, and top quartile are correlated with two key MVCI business metrics (sales volume per guest (VPG) and percentage of tours closing on time-share contracts), those who are most engaged are also the highest performers (Chart 17).

MVCI is now using this fully-integrated approach to Talent Relationship Management, a group which was formerly viewed as not having a direct impact on financial results, as the means to achieve many of the targets set within the quadrants (associate, process, customer, financial) of its Balanced Scorecard. Concludes Sweeney, "Our parent company's CEO, Bill Marriott, is fond of saying, 'Success is never final.' In that vein, while we're excited about our progress to date, we're just beginning to harvest value from linking our TRM initiatives with engagement."

Chart 16

Managers with talent relationship management training have more engaged employees

Q12 grand mean

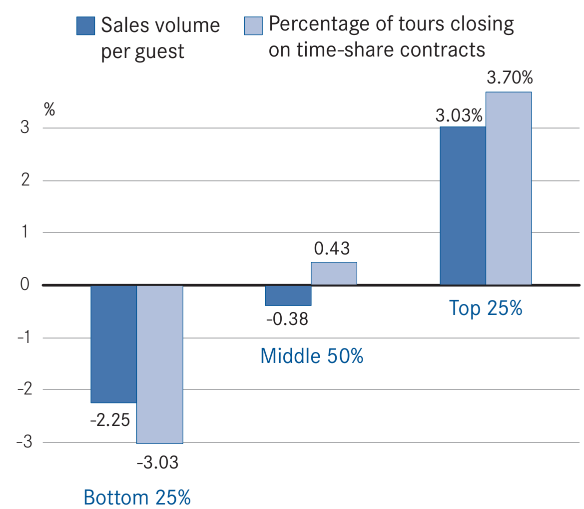


Source: MVCI

Chart 17

Most engaged sales executives are more productive

Percent difference from sales location averages



Source: MVCI

HCM Programs at Most Companies Are Still in Transition

When the survey results, research working group member comments, and outside sources are taken together, they reveal that much is left to be done in the successful creation, application, and innovation of HCMs. This is especially true for using HCMs in the implementation of a strategic human capital orientation, which remains a high priority for many human resources directors. The strong ties that should exist between HCMs and a company's overall strategy, which by definition should be unique and inimitable, are often weakened by a reliance on standardized HCMs and the overuse of benchmarks against competitors. Instead of developing HCMs to support a differentiation strategy, most companies keep their efforts concentrated almost exclusively on cost measures of human capital.

As for HCMs' predictive abilities, there is little scholarly consensus about which HCMs are most effective at predicting future performance. This uncertainty may be why respondents to our survey prefer retrospective measures over forward-looking metrics. The Royal Bank of Scotland and Marriott Vacation Club International case studies provide in-depth examples of how companies can use employee engagement—the single prognostic measure used by a significant number of companies—to enhance performance. Companies hoping to go beyond "just keeping score on a scorecard" should also consider the use of causal models to ascertain the impact of human capital on business problems.

Companies must also struggle to have business managers take accountability for the application of HCMs. To do so, companies will have to equip managers with the knowledge they need through investments in training. If such education is provided, managers will more readily understand how these metrics relate to KPIs and how the measures can help them meet the human capital targets set in their bonus plans and/or MBOs. Another way to raise awareness would be to increase the frequency and the breadth of distribution of HCM reports. Making monthly HCM reports available throughout the management ranks would increase managers' familiarity with how they are used and allow them to more easily take corrective actions based on the results. This principle of greater dissemination is also applicable to stakeholders outside of the company, who can use the reports to learn how the workforce can create value for both the company and the larger community.

About This Report

During 2006, The Conference Board organized a series of working group sessions to address the topic of human capital strategy and measurement. Key questions included:

- How can HCMs align people investments with business strategy?
- Which people measures can be used as prospective indicators of performance?
- How can human resources make business managers accountable for their performance on people measures?
- How can people measures be used to improve communication about strategic people priorities?

Through responses to a 2006 survey of 104 human capital executives, a review of relevant secondary sources, and company examples and observations, this study provides provisional answers to these questions. It illustrates how companies are successfully applying human capital metrics to add value to their workforce's ability to implement strategy.

All findings and data in this report register the collective experience of survey participants and reflect the overall results of the study, not necessarily the views of individual companies or employees, unless otherwise specifically indicated.

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About the Author

Dr. Stephen Gates, CFA, is professor of strategy at Audencia Nantes Ecole de Management and the author of a series of reports on performance measurement: performance measurement during merger and acquisition integration, strategic performance measurement systems, performance measurement in European executive compensation, and human capital measurement. He is currently council director for the European Council on Corporate Strategy and the European Council on Investor Relations.

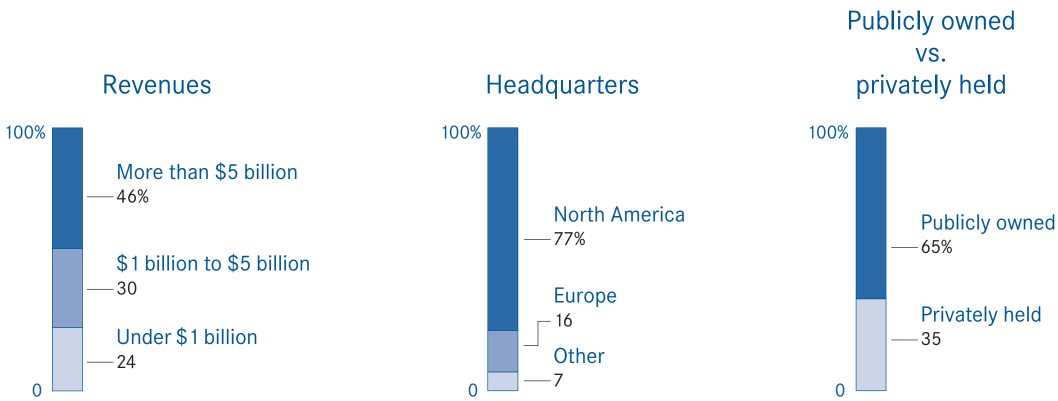
Gates was a principal researcher at The Conference Board from 1993 until 2005. A Certified Financial Analyst, he worked for seven years as an investment and securities analyst at JP Morgan Chase and Crédit Agricole Indocam.

Gates holds a Ph.D. and MBA from New York University's Stern School of Business, where he taught graduate courses in international business strategy, as well as at various business schools in France (HEC, ESCP-EAP, EM-Lyon, and EDHEC). His publications have appeared in such journals as *MIT Sloan Management Review*, *Long Range Planning*, *World at Work*, *Journal of Applied Corporate Finance*, and *Journal of International Business Studies*. He is a member of the Academy of Management and the Association for Investment Management and Research.

Publications Team

Publishing Director **Chuck Mitchell**
Author **Stephen Gates**
Editor **Timothy Dennison**
Design **Peter Drubin**
Production **Andrew Ashwell**

About the Survey Participants



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The Conference Board, Inc.
845 Third Avenue
New York, NY 10022-6600
United States
Tel +1 212 759 0900
Fax +1 212 980 7014
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The Conference Board China
Beijing Representative Office
7-2-72 Qijiayuan,
9 Jianwai Street
Beijing 100600 P.R. China
Tel +86 10 8532 4688
Fax +86 10 8532 5332
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The Conference Board Europe
Chaussée de La Hulpe
130, box 11
B-1000 Brussels Belgium
Tel + 32 2 675 5405
Fax + 32 2 675 0395
www.conference-board.org /europe.htm

The Conference Board Asia-Pacific
22/F, Shun Ho Tower
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Hong Kong, SAR
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Fax + 852 2869 1403
www.conference-board.org /ap.htm

The Conference Board of Canada
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Canada
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