1 Introduction

> No institution can possibly survive if it needs geniuses or supermen to manage it. It must be organised in such a way as to be able to get along under a leadership composed of average human beings.
>
> Peter Drucker

Introduction

The purpose of this book is to emphasise the role of strategic human capital in the development of stronger global business strategies. This book is specifically aimed at helping business leaders understand the essential elements of human capital in their organisations. Human capital, the performance and the potential of the people in an organisation, is a critical issue for leaders to address. We will examine how the critical elements of human capital such as culture, leadership, talent, structure, change, and performance metrics are essential to strategic learning and the continued evolution of the firm's strategic positioning.

Strategy is the expression in practice of the strategic intent or aspiration that stretches the organisation to innovate, change, leverage resources, and develop new skills. Intent is an architecture or framework used to develop the distinctive competencies of an organisation, which can be leveraged for competitive advantage. Strategy encompasses the formulation and articulation of a strategy through a planning process or strategic analysis, a set of goals, and the associated processes of strategic implementation and execution enacted by policies to achieve the goals. It follows that a good strategy is achieved through an understanding of not only how to achieve strong competitive advantage, but also how to execute that position and the competitive vision over time.[1]

The strategy implementation process must be closely aligned with the strategy formulation process to create results. Alfred Chandler, a renowned business historian at the Harvard Business School, defined strategy as: 'The determination of the basic long-term goals and appropriate objective of an enterprise coupled with the adoption of courses of action and the allocation of resources necessary for carrying out these goals.'[2]

In strategy execution there is clear attention on the role of strategic leadership to set the direction, develop solid plans, and carry out the necessary strategic change processes. Critical to the execution is the identification of resources that will comprise the distinctive core competencies, dynamic capabilities, and strategic assets that support the firm's sustainable competitive advantage.[3]

The resource-based view suggests that the firm can be considered as a collection of resources or assets that are unique drivers of strategy and growth of the firm.[4] With this orientation, it is the resources of the firm that are of primary importance, rather than the external factors. A resource is an asset with an important relationship to the execution of a strategy: for example, geographic location, patents, innovation, strong brand, established distribution network, or skilled human resources. In the case of human capital, the strategic value is infrequently stressed in many of the strategy textbooks as it can be more challenging to quantify.

It is one thing to make note of resources available to the firm, but another to use them to actively create value. Strategic capability is the ability to perform an activity that involves complex patterns of coordination between people and other resources. Capabilities are non-imitable, intangible, rare, and non-tradable.[5] Examples include expertise in research and development (R&D), high-quality manufacturing, and superior customer reputation and service.

For example, in the airline industry there are low-cost carriers that sell air travel at the lowest possible price as a means of gaining customers. Ryanair and Southwest are good examples of this approach, offering a no-frills flight experience at a low price. Their target customers tend to be travellers looking for an economical way of getting from point A to point B. At the other extreme we find the 'five-star' airlines such as British Airways, Singapore Airlines, and Qatar Airways, which provide full service on the ground and in the air, aimed at the business traveller. Both types of air carrier are in the business of moving passengers but their strategies are very different. Ryanair and Southwest do it by being low-cost carriers while full-service carriers provide extra services and capabilities with either a national or international orientation. They constitute different strategic groups.[6] The services provided are different, as is the price charged. But, importantly for the purposes of this book, the type and nature of the human capital will also be different. Whereas a low-cost carrier would tend to address management processes designed to take costs out of the overall system, a full-service carrier concentrates on how to improve the overall travel experience for its passengers, resulting in the ability to charge a price premium. As a result, the organisational culture, leadership, structures, and talent must be aligned to enable employees to fulfil the strategy and change the organisation's direction.

The use of terms such as strategic assets, core competencies, and dynamic capabilities are used interchangeably in the literature and in practice. Here we will use the notion of core competence, widely accepted in practice and based on the work of Prahalad and Hamel.[7] They propose that organisations can create distinctive resources that can bring significant value through collective learning in the firm. This notion of building organisational competence is difficult to put into practice as it defines the way that things get done inside the firm. A key element of achieving distinctive core competence is the capabilities of the people in the organisation, or *human capital*.

Just as the literature defines dynamic capabilities, we can also reflect on these in light of the human capital of the organisation. Since the time that Chandler introduced the notion of structure and strategy in his 1962 book, *Strategy and Structure: Chapters in the History of the American Industrial Enterprise*, thinking about the nature of firms and strategy has continued to evolve and there is a much needed link between human capital and strategy in the literature and in practice.[2] Globalisation and new operating models have been driving changes in talent, human capital, and human capital strategy. For our purposes, we will use the following definition: 'Human capital is the people, their performance, and their potential in the organisation.'

The key emphasis of human capital is therefore not only the bundle of skills, but also the integration of a diverse set of skills. Human capital is generally considered of value when it makes a disproportionate contribution to customer-perceived value. To be considered unique, the human capital of the organisation should be considered distinctive relative to that of its competitors or at a superior level with respect to others. The notion of human capital for competitive advantage (the ability to open new markets and find new sources of value) is seeded in the basis of dynamic capabilities. Human capital is an important part of the ability to execute strategy.

The office products giant 3M has long been credited with having not only the right ideas but the right people to execute them. A main staple of 3M's strategy continues to be that a certain percentage of their revenue must come from products introduced by the company in the last five years. This strategic emphasis on innovation forces the company not only to hire the most creative talent possible, but also to accept failures when a potential new idea does not work so that these creative people can continue searching for more ideas.

As a consequence, there is a real and commonly shared concern about more clearly identifying and understanding human capital in an organisation from a strategic standpoint. Leaders want to determine gaps and significant areas that can be better leveraged to sustain competitive advantage, and untapped potential. Finding ways to leverage the strategic human capital of the firm has the potential to create new core competencies as firms look to find new ways to improve the speed at which they respond to the marketplace, foster more innovation, adapt to the competitive landscape, enable consistency of performance, develop the right future talent, and create a global mindset.

Thinking differently about business strategy

Sometimes strategists look too closely at the external factors affecting the firm and pay too little attention to internal capabilities. This imbalance can lead to inadequate framing of the strategic problems, leading to unrealistic strategic decisions, false sets of assumptions, or simply failed strategies, as the internal capabilities may not allow the plans to be implemented. While popular frameworks such as Porter's five forces model and environmental scanning provide models to address elements of the strategic context, they can direct too much attention to the external and economic factors that are affecting the firm.

A strengths, weaknesses, opportunities, and threats (SWOT) analysis can help to provide a balanced view on both internal and external factors. While this framework has been criticised for being too broad or lacking sufficient rigour in addressing competition, most would argue it is of value in determining an organisation's relative strengths and matching them with available opportunities.

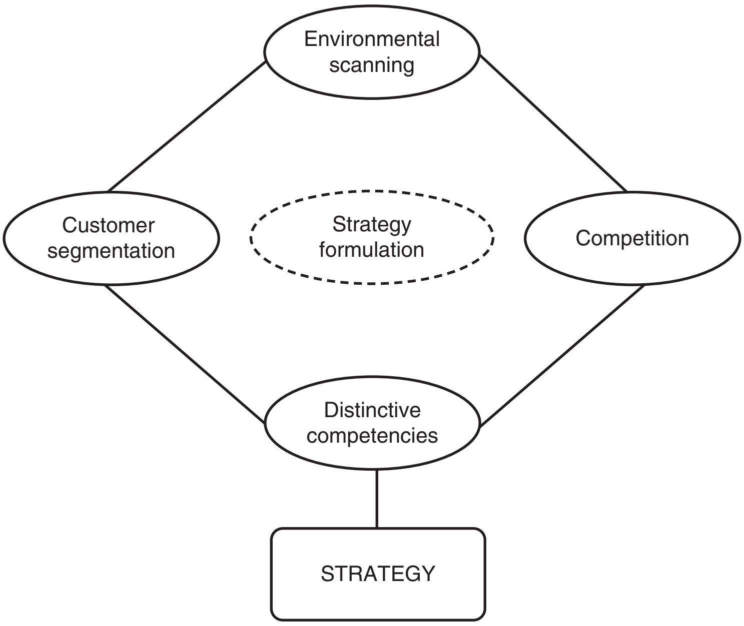

Figure 1.1 Strategy formulation
Source: adapted from McGee, Thomas, and Wilson, *Strategy Analysis and Practice* (McGraw Hill, 2010)

Strategy formulation typically involves some level of environmental scanning, a review of competitive positioning, an analysis of customer segments, and the key distinctive competencies of the firm. Many organisations develop a strategy based on these factors, yet often do not consider the factors associated with the availability and the value of human capital. Based on the work of McGee, Thomas, and Wilson, we note the strategy formulation process as illustrated in Figure 1.1.

The output of strategy formulation is usually a business strategy that defines the performance goals the organisation seeks to achieve and sets parameters for the decisions and investments it will make to support those goals.

It has been noted that strategic organisation change is often difficult to implement. In fact, some estimates indicate that 50 to 70 per cent of all new change efforts fail to reach their objectives.[8] One of the many reasons for this startling statistic is the lack of alignment of 'fit' between the organisational context of strategy and the strategy implementation process. A successful strategy requires appropriate linkage between strategy analysis and the processes of implementing that strategy effectively in the practical context.

Strategy implementation must consider the culture of the organisation, leadership capability, structures and organising mechanisms, and the management

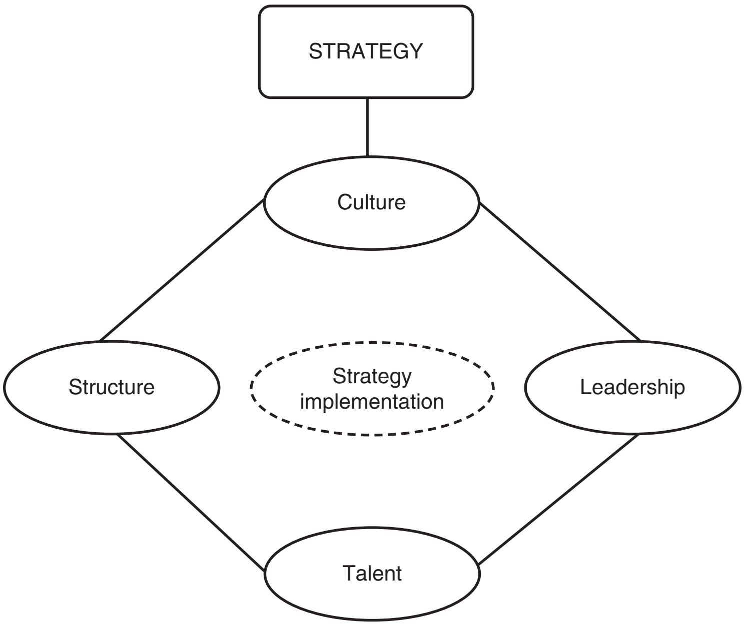

Figure 1.2 Strategy implementation or human capital strategy
Source: adapted from McGee, Thomas, and Wilson, *Strategy Analysis and Practice* (McGraw Hill, 2010)

of talent, as shown in Figure 1.2. These elements each play, individually and collectively, a critical role not only in shaping the strategy, but also in determining the success of implementation.

Another way to think about strategy implementation is to view this essentially as a 'human capital strategy'; as a way we can largely address the people side of the business (along with the organisational configuration) to implement strategy successfully. Therefore, human capital strategy is defined as a unique set of prioritised choices about people investments that enables the organisation to achieve its business strategy and performance goals. This may be called a 'people strategy' or 'talent strategy' in some organisations.

Human capital strategy should not be confused with a human resources (HR) strategy. An HR strategy typically reviews the human capital strategy to determine the appropriate actions for the human resources function (HRF). Typical areas that are addressed in an HR strategy include: compensation programmes, development initiatives, incentive programmes, hiring plans, HR data management, and HR effectiveness planning. At the same time, some are taking a broad view of HR strategy, such as Cascio and Boudreau in their recent book on strategic human resource management.[9] They argue that HR strategy must incorporate and consider environmental factors as well as organisational factors since HR influences and is influenced by organisational context. For example, an organisation may determine that a new strategy requires the company to upgrade talent quality in critical roles, build workforce pride and commitment, clarify expectations to drive performance, and build strong front-line management. The HR function strategy would then deliver on those imperatives and in turn deliver programmes to support these areas. While the HR strategy is a critical component, we suggest that the human capital strategy can be more closely aligned with strategy execution.

When business strategy evolves, so must the human capital strategy, to ensure that the significant people investments being made reinforce each other and collectively drive new, desired business outcomes, and effect strategic change. Keeping strategic decision-making in step with the human capital strategies is a key element in driving successful strategy implementation efforts. As illustrated in Figure 1.3, the human capital strategy is an essential part of the strategy process and drives the implementation efforts.[10]

Throughout this book we will address each of the key aspects of human capital strategy as it relates to business direction and strategy. Human capital is often an essential element of the strategic change and execution processes.

Recognition of human capital as a source of value

For decades, economists have considered human capital as a source of competitive advantage for nations, following Gary Becker who popularised the concept.[11] As they examine education levels, workforce demographics, and general availability of skills, the idea of human capital has become one of the most important factors in the production and growth of economic wealth. Increasingly, the idea of national human capital also points to important linkages between human capital and long-term economic growth, as the strength of a nation can only be sustained by the strength of the next educational generation. Several nations have launched human capital initiatives as they recognise the importance of human capital as a part of the national agenda.

One such example can be found in Malaysia. In 2011 the Prime Minister created a new initiative to address the human capital of the nation. The primary purpose is to develop initiatives and direction to address the availability of talent in line with the country's economic growth and transformation plans. For a country like Malaysia, the availability of human capital can be either a driver

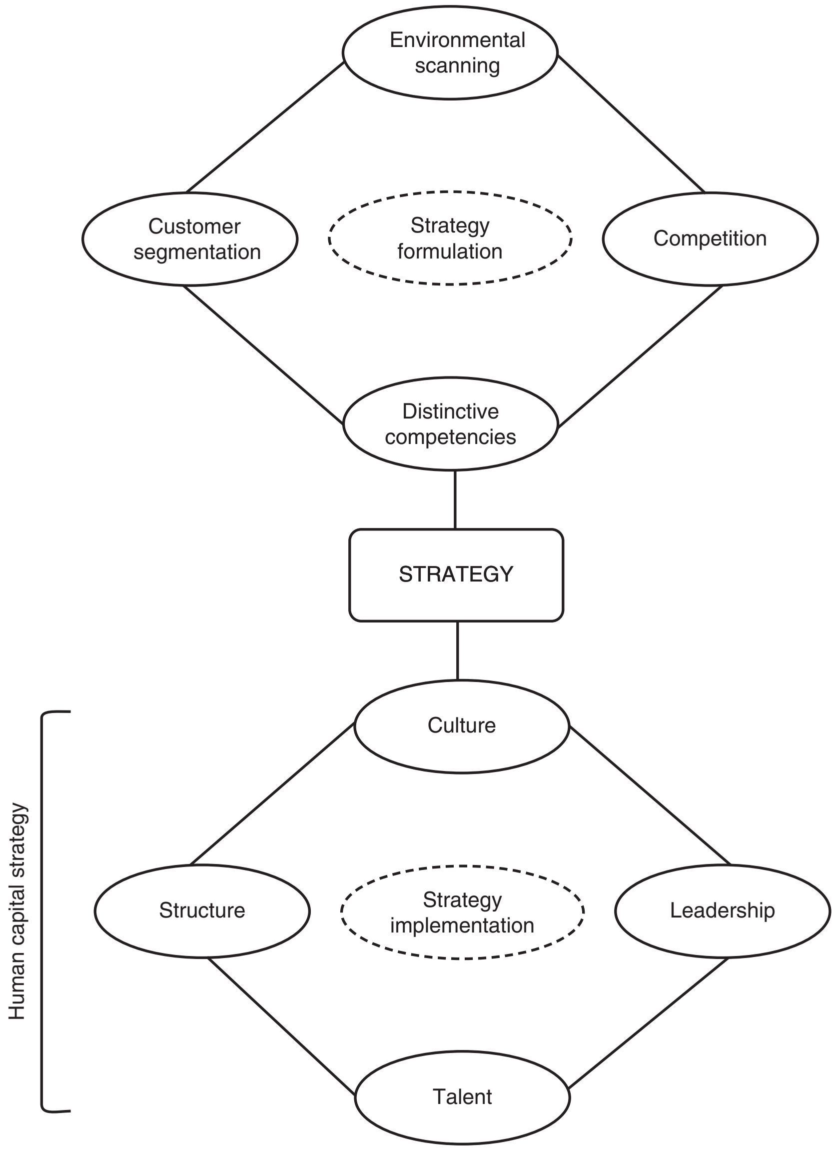

Figure 1.3 Holistic view of strategy
Source: adapted from McGee, Thomas, and Wilson, *Strategy Analysis and Practice* (McGraw Hill, 2010)

for success or a barrier to growth. To drive this initiative, Malaysia created TalentCorp, a new organisation with the mission of building effective partnerships and making a difference in addressing Malaysia's talent needs. The aim is to enable the country to reach its aspiration of being a high-income nation. For many countries similar national human capital initiatives are coming to the forefront of political-economic agendas.

A recent report by the World Economic Forum highlights that collaboration in talent mobility among stakeholders on all sides of the employment equation is most effective in addressing labour market shortages.[12] The report points out that talent markets are impeded by four key problems: widespread unemployment, skills gaps, information gaps, and private and public constraints. The report includes many examples of collaboration among companies, governments, academic institutions, and non-profits to address talent challenges.

In Canada, the Toronto Financial Services Alliance was established by the City of Toronto as a public–private partnership between government, academia, and financial services organisations to attract talent and thereby strengthen the Toronto financial services sector. The partnership aims to close information gaps by identifying specific skills and talent needs of the industry at college and university levels. The creation of the Centre of Excellence in Financial Services Education in 2009 was a result of this ongoing partnership.

Saudi Aramco, the world's largest oil and gas company, relies on rigorous workforce planning methods, substantial targeted investments in education and training, and expansive talent mobility programmes that give its employees exposure to the management practices and tools used by other major firms around the world. These programmes contribute to internal mobility at all career levels. Saudi Aramco also works closely with the government of Saudi Arabia and key academic institutions to secure a steady flow of talent to the company and throughout the country.

Strategic human capital is generally classified as an 'intangible asset', as it is often team-embedded in an organisation and built up as a strategic capability over time. Other intangible assets include brands, trademarks, and customer goodwill. While these assets are not physical or listed on a balance sheet, they are organisationally determined and growing in importance in economic and business activity.[13] This can be commonly seen in the valuation of assets in cases involving acquisitions or asset sales that include intangibles.

The relationship between human capital and the resource-based view (RBV) of the firm has been explored in recent years.[14] Some of the RBV strategists have linked various aspects of human capital to business strategy, for example, Barney's work on organisational culture as a potential source of sustained competitive advantage.[15] From the human resource management discipline, researchers and practitioners have long viewed the nature of human capital from different vantage points. While some address the link to strategy and the resource-based view, others take a performance-based view of human resource management (HRM) practices.[16] Boxall and Purcell summarised the interplay of strategy and human resource management to help bridge the disciplines in their book, *Strategy and Human Resource Management*.[17] While more research is needed in this area, it seems clear that the attention to human capital as a part of global business strategy has come of age.

Human capital as a part of business strategy

Regardless of the type of business strategy, the need to successfully implement strategy is important. Business leaders are increasingly recognising that whether the strategy is based on acquisition, differentiation, cost leadership, or a niche area, human capital is critical to success of that strategy.

One good example of implementing change by addressing the core elements of human capital is provided by Carlos Ghosn, then COO of Nissan, as he led the successful turnaround of the company against the backdrop of crisis for the Nissan–Renault alliance in the early 2000s.[18] Ghosn took stock of the situation when he arrived and reviewed the business practices, culture, talent management practices, leadership and structures. In addition to fundamental financial challenges due to re-engineering product development and the costs of production and the supply chain, the human capital assumptions on how work was organised and performed had to be rethought. He made major changes to the organisation structure by establishing cross-cultural teams across Nissan and Renault to identify common potential synergies in R&D, engineering, marketing, manufacturing, etc. and nine cross-functional teams in each company including most business areas that would then drive the major changes that had to be made. These teams became the catalyst for the turnaround as they broke traditional paradigms and began to change the culture of the organisation. Leadership through these teams coupled with the open and authentic leadership of Ghosn made a powerful difference in helping managers see beyond former functional boundaries. Ghosn notes that the success of this organisation change was built on establishing trust through transparency, with strong attention to nurturing a new corporate culture that remained sensitive to the history of Nissan and the best elements of Japan's national culture.[19] At the same time, he challenged current assumptions in the Nissan system such as lifetime employment (a luxury that Nissan could not afford), the orientation towards seniority versus meritocracy in rewards, and the use of *keiretsu* suppliers versus open bidding. He challenged these assumptions to effect appropriate