Section 3.5 Assessing competitiveness

21 Human resources

Definition

Human resources is a common term for the personnel function of a business. HR professionals think of their role as central to the overall goals of the business, and set their HR objectives accordingly.

Linked to: Corporate strategy, Ch 2; Corporate culture, Ch 16; Causes and effects of change, Ch 22; Key factors in change, Ch 23; Scenario planning, Ch 24

21.1 Introduction

People are a resource of the business. Like any other resource, they have to be managed. Many organisations claim their people are their 'most important asset' and that HR management makes a significant difference to business success. All too often, though, staff are treated like a cost, not an asset.

21.2 The management of people

The management of people (otherwise known as human resource management) involves a wide range of activities. These begin with identifying the workforce requirements of an organisation in the future so that the appropriate plans can then be developed. For example, more staff may need to be recruited, existing staff may need training or redeployment, or redundancies may be needed.

In addition to managing the flow of people into and out of an organisation, human resource management involves activities such as those listed below.

- Designing the jobs that people do: this can have a big effect on their motivation and effectiveness; poor job design may be demotivating and lead to increased labour turnover.
- Developing appropriate reward systems: this will have a big impact on how employees behave. For example, a commission-based system is likely to push employees to make sales, but staff may be unwilling to do tasks that do not directly lead to a sale.
- Developing effective communication systems: these may include bulletins from managers, newsletters, systems of meetings or consultation with employee representatives. The communication systems will be designed to inform employees and at the same time achieve a desired level of consultation with staff.

The decisions taken by the human resource function will be linked to the overall business objectives and strategy. For example:

- If the business is growing, the HR function may need to recruit more staff; if it is expanding abroad, it will recruit staff with language skills.
- If the business is changing the nature of its operations, HR staff may need to invest more in training to ensure employees have the right skills; alternatively, it may mean some jobs are lost and others are created.
- If the business is trying to reduce its costs, then HR will be looking for ways of helping to bring this about; for example, combining jobs, boosting productivity or reducing the training budget.

'We treat our people like royalty. If you honour and serve the people who work for you, they will honour and serve you.'

Mary Kay Ash, American entrepreneur

'We have always found that people are most productive in small teams with tight budgets, time lines and the freedom to solve their own problems.'

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21.3 Monitoring the effectiveness of human resources

Staff costs are usually between 25 and 50 per cent of a firm's total costs. So firms try to measure the performance of their people objectively (that is, in an unbiased way). Accurate data can help point to areas of strength or weakness in the way staff are managed. Companies focus on calculating and interpreting the following personnel measures:

- labour productivity
- labour turnover and retention
- absenteeism.

21.4 Labour productivity

Labour productivity is often seen as the single most important measure of how well a firm's workers are doing. It compares the number of workers with the output they are generating. It is expressed through the formula:

$$\frac{\text{output per period}}{\text{number of employees per period}}$$

For example, if a window cleaning business employs ten people and in a day cleans the windows of 150 houses, then the productivity is:

$$\frac{150}{10} = 15 \text{ houses per worker per day}$$

Any increase in the productivity figure suggests an improvement in efficiency. The importance of productivity lies in its impact on labour costs per unit. For example, the productivity of AES Cleaning is 15 houses per worker per day; MS Cleaning achieves only 10. Assuming a daily rate of pay of £45, the labour cost per house is £3 for AES but £4.50 for MS Cleaning. Higher productivity leads to lower labour costs per unit. And therefore leads to greater competitiveness both here and against international rivals.

Figure 21.1 Higher productivity leads to more windows cleaned in a given time and therefore lower labour costs per unit

Real business

The UK's largest recruitment firm is 'on the front foot for the first time in years,' says its boss. Perhaps white-collar recruitment group Hays can teach Britain's economic policymakers a thing or two. While they fret about the country's low productivity, the UK's biggest recruitment firm has been investing heavily to ensure it becomes more productive.

That effort is now paying off, according to chief executive Alistair Cox, and helped Hays post a forecast-beating pre-tax profit up 10 per cent at £62.5 million as it delivered first-half results yesterday. 'We've had a diligent focus on productivity,' said Mr Cox. 'As a recruiter, we're the ultimate people business. We've brought in quality people, we've trained them, managed them, equipped them to do the job as best as is possible. We're the only recruiter to bother investing in technology.

Cynics might argue that he's taking the credit for an improving global economy that's actually driving the performance. However, credit where credit's due: net income rose by just 1 per cent to £363.4 million, so the 10 per cent profit increase was impressive. During the half-year in question, total operating costs fell by just over 1 per cent.

(Source: adapted from the Telegraph, 27 February 2014)

21.5 Labour turnover

This is a measure of the rate of change of a firm's workforce. It is measured by the ratio:

$$\frac{\text{number of staff leaving the firm per year}}{\text{average number of staff}} \times 100$$

So a firm which has seen five people leave out of its staff of 50 has a labour turnover of:

$$\frac{5}{50} \times 100 = 10 \text{ per cent}$$

As with all business data, it is best to find a means of comparison: either with a rival business or with previous years' figures. Sometimes it will be hard to make a realistic comparison between labour productivity at two rival companies. After all, Nissan UK may produce more cars per employee than BMW Mini, but if Nissan uses more imported car parts, is its productivity really any higher?

There are other effective measures of productivity. In retail businesses a favoured measure is sales per square foot. This measures sales revenue in relation to the sales area of the business. Tesco might have found the decline in this figure quite depressing:

	2011	2012	2013	2014	2015
Tesco weekly sales per square foot	£24.95	£24.86	£24.15	£23.33	£22.41

Table 21.1 Tesco productivity measured by sales per square foot of shop-floor space

Fortunately it can easily find comparable data in the annual reports of Sainsbury's and Morrisons – both plcs. This makes better reading. Despite its decline between 2011 and 2015, Tesco still beats its rivals on this measure of productivity.

	2011	2012	2013	2014	2015
Sainsbury's weekly sales per square foot	£20.04	£19.47	£19.27	£18.93	£18.24
Morrisons weekly sales per square foot	£22.38	£22.52	£21.62	£20.58	£19.11

Table 21.2 Comparable data on productivity measured by sales per square foot of shop-floor space

Factors affecting labour turnover

If the rate of labour turnover is increasing, it may be a sign of dissatisfaction within the workforce. If so, the possible causes could be either internal to the firm or external.

Internal causes

Internal causes of an increasing rate of labour turnover could be:

- A poor recruitment and selection procedure, appointing the wrong person to the wrong post. When this happens, frustrated workers leave to find a job better suited to their particular interests or talents.
- Ineffective motivation or leadership, leading to workers lacking commitment to this particular firm.
- Wage levels that are lower than those being earned by similar workers in other local firms. If wage rates are not competitive, workers are likely to look elsewhere to find a better reward for doing a similar job.

External causes

External causes of an increasing rate of labour turnover could be:

- more local vacancies arising, perhaps due to the setting up or expansion of other firms in the area
- better transport links, making a wider geographical area accessible for workers. New public transport systems enable workers to take employment that was previously out of their reach.

Consequences of high labour turnover

Negative effects

A high rate of labour turnover can have both negative and positive effects on a firm. The negative aspects would be:

- the cost of recruiting replacements
- the cost of training replacements
- the time taken for new recruits to settle into the business and adopt the firm's culture
- the loss of productivity while the new workers learn the new ways of working (reach the peak on their learning curve).

Positive effects

On the positive side, labour turnover can benefit the business in several ways:

- New workers can bring new ideas and enthusiasm to the firm.
- Workers with specific skills can be employed rather than having to train up existing workers from scratch.
- New ways of solving problems can be seen by workers with a different perspective, whereas existing workers may rely on tried and trusted techniques that have worked in the past.

On balance, then, there is a need for firms to achieve the *right* level of labour turnover, rather than aiming for the lowest possible level.

Another way of measuring the loyalty and commitment of staff is to look at labour retention rates. This calculation is based on exactly the same raw data as labour turnover, but uses the information differently.

Formula for labour retention:

$$\frac{\text{staff not leaving in the past year}}{\text{average number of staff employed in the year}} \times 100$$

A high level of retention means a low level of labour turnover. The figures are based on the same raw data, but perhaps a focus on retention helps managers realise the importance of looking after existing staff. As Liverpool FC found out when Luis Suarez left the club, staff retention matters.

21.6 Absenteeism

Absenteeism is measured solely on the basis of staff days absent per year (or staff absences as a percentage of the available working days). The key point here is that the figures ignore the question of whether the absence was avoidable or unavoidable. It is simply time off – whether or not it is justifiable. According to the Chartered Institute of Personnel Management (CIPD), the correct formula is:

$$\frac{\text{Total absence (hours or days) in the period}}{\text{Possible total}} \times 100$$

According to the CIPD's own research, in 2014, the average workplace absenteeism level was 7.4 days which translates into 3.3 per cent of all working days. Out of their sample of 342 employers they found seven workplaces where absenteeism was higher than 10 per cent, i.e. three or more times higher than the average. For the average business, then, absenteeism is a relatively small issue; but there are some companies that put themselves at a serious competitive disadvantage because of high absenteeism.

21.7 Using employee performance data to help make business decisions

For young, dynamic companies such as Fever-Tree and Just Eat, each with annual growth rates of 50 per cent, the key to success is a working environment that fosters creativity, team working and intensity of effort. These qualities may not translate into measures such as productivity. After internal discussion, Just Eat's chief executive announced in August 2015 that 'Our competitors want to be in 50, 60 or 70 markets. That is not our strategy. We're about identifying the best 15 or 20 markets in the world and being the big winner in those markets.' This is a strategic decision that will determine whether Just Eat continues to be a success over the coming ten years or so.

For almost all companies, the heady days of youth are replaced by a more stable period of maturity. Think Coca-Cola, easyJet, Prêt à Manger and Next. In a more stable period, brilliant ideas may be largely irrelevant. Launching 'green' Coke Life, for example, made little difference to overall sales of Coke. In a company's maturity phase, efficiency becomes all-important. In 2015, the insurance company Direct Line declared first-half revenues that were unchanged on 2014; but because the business had

	Formula	Interpretation	Intervention
Labour productivity	$\frac{\text{output per period}}{\text{number of employees per period}}$	The higher the figure the higher the productivity (and therefore the lower the labour cost per unit).	Boosting productivity requires involved, motivated staff plus heavy investment in new technology, training and R&D.
Labour turnover	$\frac{\text{staff leaving per year}}{\text{Average number of staff}} \times 100$	The higher the figure the greater the threat to the culture, the efficiency and the consistency of the customer experience.	When recruiting it's vital to get staff who fit the culture and the ambitions of the workplace; otherwise they leave before they settle in.
Labour retention	$\frac{\text{staff \textbf{not} leaving per year}}{\text{Average number of staff}} \times 100$	The higher the figure the better, though 'new blood' can inject new creativity – so 100% retention is unlikely to be successful for long.	To avoid established staff leaving, job enrichment and fair treatment are key (in effect, bosses should follow Herzberg's two-factor theory).
Absenteeism	$\frac{\text{Days absent per year}}{\text{Toatl number of working days}} \times 100$	Absenteeism implies something voluntary. A brilliant employee with elderly, sickly parents may have high absence levels, but still be invaluable.	It could be argued that this is an old-fashioned measure. The key is whether an employee does their job well; if someone works twelve-hour days for a week and then takes a day off, are they really 'absent'?

Table 21.3 Calculating and interpreting key measures of human resource effectiveness

cut its costs by almost 8 per cent, pre-tax profits jumped by 49 per cent to £315 million. In this world of mature companies, performance measures such as productivity and absenteeism may be crucial. After all, how is it possible for a big business such as Direct Line to cut costs by 8 per cent? Finding greater efficiencies will be the answer.

Two of the world's biggest car makers are Toyota (Japan) and General Motors (USA). Each produces about 10 million cars a year, generating revenues of \$150–200 billion each. But in 2014/2015, Toyota made a pre-tax profit margin of 10.62 per cent while General Motors (GM) made 2.72 per cent. In other words, Toyota is four times more profitable than GM. This is unsustainable for GM in the long term. The American car maker needs to consider decisions such as the following:

- Addressing productivity levels head on; Toyota is the innovator behind much of lean production; perhaps GM needs to find new ways to boost productivity that fit in with lean production, such as minimising re-work by getting things right first time; high quality production means jobs are done once and once only – which helps boost productivity.
- Labour turnover and retention levels are affected by Toyota's support of the Japanese philosophy that a job is for life. Japanese firms like to have a big core of full-time, permanent staff who feel committed to the company; in America (as in Britain) there's a greater instinct by companies to treat workers as costs, not assets. This leads to short-term contract staff and therefore high labour turnover.
- Absenteeism is virtually unknown in Japan; this is partly cultural but also rooted in the teamwork approach prominent at companies like Toyota; to be absent would mean letting down your friends and those you respect (your bosses). In some western businesses it just means letting 'them' down – 'them' meaning management.

21.8 Human resource strategies to improve employee performance

In order to improve productivity, lower labour turnover and minimise absenteeism, businesses need to consider appropriate strategies. As mentioned above, the approach to personnel taken by Toyota may be an important element in the company's superior performance to General Motors. Among the possible strategies are:

- financial rewards
- employee share ownership
- consultation strategies
- empowerment strategies.

Financial rewards

Human resource managers are constantly on the lookout for a system of financial rewards that will raise productivity, boost participation and increase employee retention. Governments follow the same approach, believing that teachers or doctors can be motivated by a payments-by-results financial package. There is some excuse for this on the part of the HR professionals, because they need to justify their employment. For government there is no excuse, because research over many years has done little more than confirm Professor Herzberg's dictum from 1959: beware of meddling with hygiene factors (such as pay and working conditions that can cause job dissatisfaction).

Herzberg warned that manipulation of employee behaviour through financial means risks creating wrong incentives or even 'revenge psychology' on the part of staff. Ask Lloyds Bank. In July 2015, the bank upped its provisions for compensation payments on 'PPI' misselling to £13.4 billion. The bank's own financial reward system had encouraged its own staff to sell payment protection insurance (PPI) to people who didn't need it. Losing £13.4 billion may have persuaded Lloyds that financial reward systems distort behaviour. Better by far to employ good, honest people, train them well and pay them a decent salary.

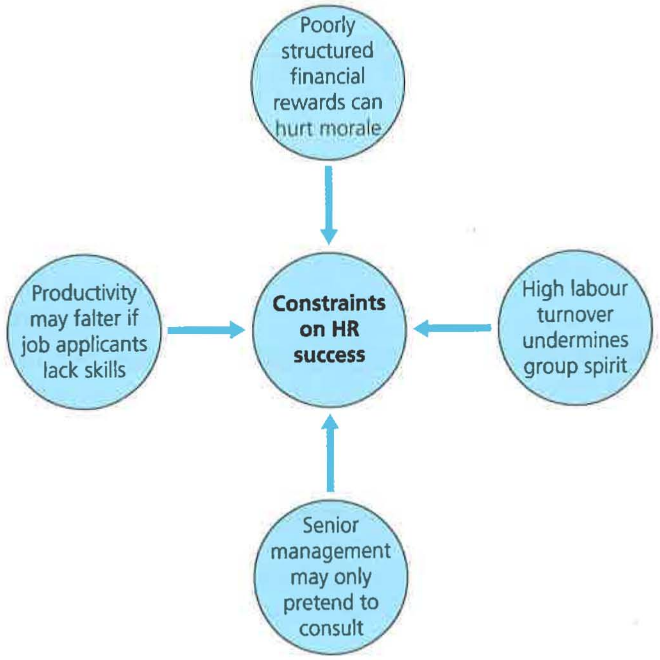

Figure 21.2 Logic circle: HR management isn't easy

Employee share ownership

The theory is clear: give staff a stake in the business and they'll feel part of the whole instead of seeing a them-and-us divide between management and staff. Therefore staff will be more motivated and more committed to long-term employment. *Financial Times* journalist Tim Harford says that 'A study by Alec Bryson and Richard Freeman of the Centre for Economic Performance at the London School of Economics found that employee ownership was positively correlated with productivity ... Mr Bryson and Mr Freeman also surveyed other studies and conclude that none found any negative impacts of employee share ownership and some found positive effects.'

It would be a mistake to overestimate the value of employee ownership, though. Every week the *Grocer* magazine does a 'mystery shopper' rating of a branch of the Big Five supermarkets. In the 25 July 2015 issue, the top rated store was Morrisons, Beverley, Yorkshire with 81/100; bottom was Waitrose, Beckenham, London with 47/100. The company's own data shows that labour turnover at Waitrose was 34.1 per cent in 2014/2015, which is far from impressive. So employee ownership (Waitrose is part of the John Lewis Partnership) proves little.

Consultation strategies

In its 2014/2015 annual report, John Lewis quotes a survey finding that 75 per cent of partners (full-time staff) agree with the statement 'we create real influence over our working lives'. For any business this would be an encouraging finding.

The John Lewis strategy for achieving this is to have a consultation forum called 'Partner Voice' that feeds through 'Divisional Forums' into the 'Partnership Council'. In effect, this is a fusion of democratic and consultative procedures. It certainly gives a theoretical input from the shop floor into the boardroom. However impressive the structures, though, the real issue is whether suggestions or complaints from the shop floor are acted upon by those at the top.

At a global giant such as Unilever, consultation becomes that much harder. With nearly 200,000 staff spread over more than 100 countries, the business chose in 2014 to use social media as a mechanism for a two-day management conference. Four hundred senior managers held a two-day online meeting with 16,000 **line managers**! Of the 16,000 employees invited to be part of the event, only 3,680 were active users of the company's internal chatsite before the event. During the conference this number rose to 7,520.

Employees also reported feeling more included and motivated thanks to the initiative. When asked directly how useful participants found the experience, 86 per cent of respondents shared feedback like: 'It did provide real-time information on key programme results. It was like following an internal Twitter feed', 'I felt as though I were actually attending the event!', 'A big step in democratisation of information in Unilever'.

Empowerment strategies

Important though consultation can be, empowerment is at another level. Empowerment means delegating not only the power to decide how to tackle a task, but also to decide which task to tackle. In other words, it means allowing junior staff to set their own objectives and then the strategy for achieving them. A great example is at Google, where staff are allowed 20 per cent of their working hours to work on their own projects. They don't have to get approval for what those projects are (so designing a new bathroom might be someone's priority). In fact, important breakthroughs such as Gmail have come from this open approach to empowerment at the company.

The key to an effective empowerment strategy is to have such strong, clear organisational aims and culture that staff will know what's relevant and what's unacceptable. When Google staff started working on a self-drive car it probably seemed a wild gamble – but the staff knew that it was a way of leveraging various Google corporate strengths – notably a mastery of complex software algorithms.

Many other firms have followed (or preceded) Google's approach. In the 1990s, an inward-looking South Korean company called Samsung decided to send its best young staff to live for a year in different foreign countries. They returned with a good understanding of local habits – and this must surely have made it easier for Samsung to take on Apple in the global market for smartphones.

> 'There was a time when people were "factors of production" managed little differently from machines or capital. No more. The best people will not tolerate it.'
>
> *Robert Waterman, business writer*

> 'Companies used to be able to function with autocratic bosses. We don't live in that world anymore.'
>
> *Rosabeth Moss Kanter, business guru*

Five whys and a how

Question	Answer
Why might productivity fall during a period when sales are rising?	Management might get complacent, recruiting more staff than the revenue increase warrants.
Why does rising productivity tend to push labour costs per unit down?	Because employees' wages are being spread over more units of output.
Why might staff retention figures improve during a recession?	Staff are scared to risk unemployment, so they stay put even if they get little satisfaction from their jobs.
Why might a company's labour turnover figures have worsened steadily over the past four years?	There may be a new management approach that puts more pressure on staff, encouraging increasing numbers of them to look for work elsewhere.
Why might the Chancellor of the Exchequer be concerned if UK productivity figures failed to rise?	He or she would worry, because without productivity gains our economy has no prospects for sustained economic growth; rising efficiency makes it easier to export, and easier to fight off imported goods.
How might a head teacher view a big rise in labour turnover since his/her arrival?	He or she would probably ignore the possibility that staff are leaving due to disappointment with him/her; but that might be the real reason.

21.9 Human resources – evaluation

The term 'human resources' is a controversial one, smacking of treating people no differently from other resources such as land and capital. In fact, most successful companies see their staff as the beating heart of the organisation – to be paid well and treated well. If your people come up with sufficiently brilliant new products or new routes to market, competitive issues such as productivity and absenteeism will become minor matters.

The hard thing, though, is to move from a weak to a strong position. When David Potts took over at Morrisons in early 2015, he inherited a demoralised staff. To his credit, consulting with staff and acting quickly on staff grumbles allowed him to make a real impact. Interestingly, one of the new boss's first actions was to scrap 'scan rates' at checkouts as a measure of productivity. Staff objected to the conflict it created between speed and being friendly to customers. In the best organisations, measures of employee efficiency are used intelligently, not as a stick to beat managers.

Key term

Line managers: staff with responsibility for achieving specific business objectives, and with the resources to get things done.

21.10 Workbook

Revision questions

(25 marks; 25 minutes)

1 What may be the effects of managing human resources in the same way as all the other resources used by a business? (3)

2 Identify three important features of the job of a human resource manager. (3)

3 How could an increase in labour productivity help a firm to reduce its costs per unit? (3)

4 In what ways could a hotel business benefit if labour turnover rose from 2 to 15 per cent per year? (4)

5 Some fast food outlets have labour turnover as high as 100 per cent per year. What could be the effects of this on the firm? (4)

6 Explain two ways in which a human resources manager may be able to help increase productivity at a clothes shop. (8)

Revision activities

Data response

Employers face high staff turnover in 2014

A fifth of employees plan to quit their job this year, according to a survey from the Institute of Leadership and Management (ILM). The study, of 1,001 workers, found that of the staff who are preparing to change job, 16 per cent want to leave because they do not feel valued. Of this group, the vast majority would like a similar job (40 per cent) or a different post (39 per cent) at a new company, while one in ten would like to start their own business.

However, in addition to the fifth of workers planning to leave, a further 31 per cent are unsure about whether they will stay in their current roles, suggesting employers face a high staff turnover in the coming months.

Charles Elvin, ILM's chief executive, said: 'The New Year is always a popular time for workers to look ahead and think about how they can progress. Our findings show that UK employees are beginning to reassess the job market and look into a range of new opportunities, from starting a new job to developing a new business.

'The survey illustrates just how crucial it is that workers feel valued in the workplace. As many workers like to make a change at this time of year, it is important that organisations adapt to this phase by offering the chance to learn new skills and opportunities to progress wherever possible.'

The survey also asked employees about their workplace resolutions for the New Year. Most respondents (31 per cent) said improving their work–life balance was a top priority for 2014; this was closely followed by a desire to receive more training or attain a new qualification (28 per cent), to become a better manager (13 per cent), and be more productive at work (11 per cent). The ILM said that the findings revealed a desire to improve the standards of leadership in organisations, with 19 per cent hoping to improve their own leadership skills this year and 17 per cent hoping for more transparent leadership from their boss.

'The survey reinforces the importance of leadership to workers in the UK, and in particular the desire for greater transparency in the workplace,' Elvin added. 'This should be an important consideration for both current managers and those looking to improve their leadership skills.'

(*Source:* People Management Magazine *online, January 2014*)

Questions (40 marks; 45 minutes)

1 During the recent recession labour turnover fell. Assess two possible reasons why. (8)

2 Assess why labour turnover was expected to rise in Britain in 2014. (12)

3 Is high labour turnover always a course for concern? Evaluate the potential benefits and drawbacks of a high labour turnover for either Primark or Jaguar Land Rover. (20)

Extended writing

1 Evaluate the ways in which a firm may respond to an increasing rate of labour turnover. In your answer, refer to one retail business and one other organisation you have researched. (20)

2 In 2014, Tesco announced that it planned to open a supermarket chain in India, one of the world's fastest growing economies. Evaluate the extent to which Tesco's success or failure in India might depend upon a successful HR strategy. (20)