# From Strategic Human Resources to Organization Performance

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#### **Abstract**

Much has been written about the link between HR and performance, however consensus has yet not been found concerning the understanding on how that relationship comes together. Empirically, no direct impact has been found and research has only suggested an indirect impact. Consequently, the Strategic HRM field is particularly interested on the understanding of the mediating variables that impact the organization performance. Besides the integrated and business strategy alignment of the HR function, it should be considered that it is the people (HR) of the organization and not their practices that determine the company's competitive advantage. (Messersmith & Guthrie, 2010) argue that it is the impact of those practices that represent "the true resource and enable a sustainable advantage over industry rivals". The objective of this research proposal is to study the impact of strategic human resources practices on the organization performance through a case study methodology, supported by longitudinal data. Namely, the project aims to achieve a deeper understanding of the variables that affect the process stream during strategy implementation. How the HR practices impact on people? And why human resources are the most valuable asset? These core premises are in line with the most recent economic concerns about people productivity, employment policies and labor flexibility.

Keywords: Strategic Human Resources Management, Organizational Effectiveness, Human Capital

#### Introduction

During the last years, companies and businesses had to face enormous challenges due to several competitive pressures. This transformational context affecting the organizations required a paradigm shift and new business designs need to be adopted to pursue more agility and flexibility. Business models require a new focus at the human resources role: from the administrative role to a more strategic one aligned with companies' business plan.

Although there are several empirical studies confirming the relationship between HR and Performance, there is no consensus on literature about this issue. "Methodologically, there is no consensus regarding which practices constitute a theoretically complete set of HR practices; how

conceptually categorize these practices; the relevance of business strategy; the appropriate level of analysis; or how HR performance and firm performance need to be measured...theoretically, no consensus exists regarding the mechanism by which HR practices might impact on firm outcomes" (Wright and Gardner, 2003 cited in Katou & Budhwar, 2010).

The demand of a new hr role at the organizations

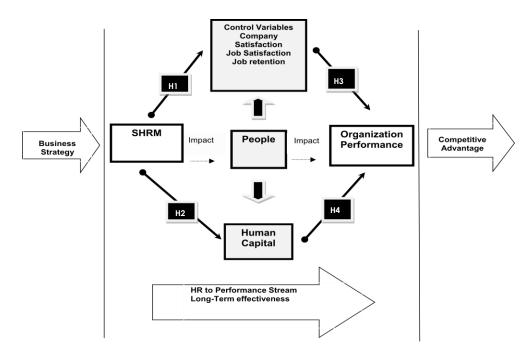
As the contribution to the firm's competitive advantage increases, human resources function is assuming a much higher role into the organization and it's expected that HRM became a strategic function affecting all the organization performance.

This requires a new HR positioning as profit-maker, helping to generate revenue and designing HR initiatives accordingly, as stated by Ulrich (1997), "one of the most common weaknesses of HR professionals is fear to quantitative, measurable results... should be able to talk explicitly about how they add value to business results".

There is no consensus concerning the relationship between HR and Performance. However, this subject has been studied recently due to profitability and cost-saving pressures under the present economic environment and the accelerated growth of emerging markets, "A clearer articulation of the "black box" between HR and firm performance is the most pressing theoretical and empirical challenge in the SRHM literature. This requires a new emphasis on integrating strategy implementation as the central mediating variable in the HR-firm performance relationship. It goes to the core of what makes HR strategic, and not simply a traditional HR perspective with a new set of dependent variables" (Becker & Huselid, 2006).

## Operational model and hypotheses

Fig 1. Conceptualization for the HR-Performance link



Source: Author

# Hypothesis 1: How does SHRM impacts on people? Is there a positive relationship between SRHM and people survey variables (company satisfaction, job satisfaction and job retention)?

What makes HR strategic? Design integration or differentiation?

The scholars of the approach that link human resources management practices with organizational performance always have in common one thing: people as a strategic resource and the most powerful one. "The HR system that develops and maintain a firm's strategy infrastructure should be considered as an investment" (Becker & Huselid, 1999).

Most has been written about the need of an integrated HR approach, meaning that all the HR practices must be connected and aligned. If the HR is not aligned with the Business Strategy will produce effects just because the HR practices are integrated? Strategic Human Resources Management (SHRM) researchers found the need of a strategic, integrated and differentiated HR design. Empirical research examining HR-performance link stated the need of integration, because "no single HRM practice has direct causal connection with organization financial performance" (Paul & Anantharanam, 2003).

As stated by Becker & Huselid (2006) the SHRM is "being mature" and new approaches must be undertaken to study the HR-performance link in a way that can support the competitive advantage in one organization. "We need more theoretical work on the black-box between the HR architecture and firm performance, and less emphasis on the black-box within the HR architecture...this requires a new emphasis on integrating strategy implementation as the central mediating variable in the HR-firm performance relationship". It highlights the significance of a differentiated HR architecture not just across firms but also within firms" (Becker & Huselid, 2006).

## Direct or Indirect Impact between HR and Performance?

Besides the need to align HRM practices with organization performance, this research field requires a good understanding of the mediating variables that impact the performance process and the outcome results. Empirically, no direct impact was found between HR and Performance, studies have showed only an indirect impact. According with (Paul & Anantharanam, 2003), "Despite the HRM-performance connection having been proved ... there could be a possibility of ignoring all practices that did not have a direct connection with organizational performance... this demands the identification of the intervening process that links HRM practices with organizational performance".

Numerous models have been proposed on literature, suggesting mediating variables between HRM and performance. Becker and Huselid (1998), for example, suggested that HRM policies shape employee behaviors that consequently have an impact on business performance. Wright & Snell (1998) suggested that HRM policies improve employee skills that affect employee behaviors, which in turn have an impact on business performance. Similarly, Becker et al (1997) suggested employee skills, employee attitudes and employee behaviors to form discretionary

effort, which in turn affects business performance. However, the influence of HRM policies on business performance directly or indirectly through HRM outcomes (employee skills, attitudes, and behaviors) are not necessarily mutually exclusive, but on the contrary, they can be complementary (Youndt et al, 1996; Purcell & Hutchinson, 2007 cited in Katou & Budhwar, 2010).

Best- Practices stream or Best-Fit Stream?

During years 90's the literature was dominated by the best-practice approach, but the Resource-Based View theory stresses that "firms can have different 'best practices' in HRM as long as these practices allow the firms to obtained competitive advantage", (Ji, L. 2003, Pfeffer, 1994, cited in Becker & Gerhart ,1996).

As stated by Becker et al (1997) HR systems should be a source of shareholder value and "must be tailored carefully to each firm's individual situation to achieve optimum impact". The benchmark between companies and the best-practices analysis must be applied carefully due the fact that "it could be replicated by competitors and therefore not likely to provide source of sustainable competitive advantage" (Becker et al, 1997).

Thus, between the two fundamental approaches in the HRM-performance debate, i.e., the "best-practices stream" and the "best-fit stream", we are focusing on the second approach as being preferable (Boselie et al, 2003 cited in Katou & Budhwar, 2010). Furthermore, "infusing the strategy construct into the research system can aid understanding both the determinants of HR practices and also how an alignment of HR practices with strategy can provide a significant incremental effect on performance" (Wright and Gardner, 2003 cited in Katou & Budhwar, 2010).

The integrated effects of various HRM practices might affect the same work characteristic, "the holistic system of employment model rather than specific individual practices... is designed to work in concert to motivate superior performance that positively affects firm performance", (Messersmith & Guthrie, 2010).

In summary, besides the integrated approach and the business strategy approach it is not the HR practices that determine the organization performance but "the source of competitive advantage... it is the **people** who are selected, developed, and so forth via these practices that

represent the true resource and enable a sustainable advantage over industry rivals" (Messersmith & Guthrie, 2010).

# Hypothesis 2: How SHRM does impact the generation of human capital? Is there a positive relationship between SHRM and human capital?

People as Strategic Assets - "VRIN" concept

VRIN resources has been defined on literature as "valuable, rare, inimitable, and non substitutable", Barney (1991) cited in Locket et al (2009). Researchers defined strategic assets as a "set of difficult to trade and imitate, scarce, appropriable, and specialized resources and capabilities that bestow the firm's competitive advantage" (Ami & Schoemaker, 1993 cited in Becker & Gerhart, 1996).

Strategic HRM scholars stated that "the source of competitive advantage... it is the people who are selected, developed via SHRM practices... HPWS (high performance work systems, are not the source of organizational advantage, while presumably the human and social capital created by these HR systems" (Messersmith & Guthrie, 2010).

# Hypothesis 3: How do the SRHM effects on people impact the organization's performance? Is there a positive relationship between people survey variables (company satisfaction, job satisfaction and job retention) and outcome performance?

Resource based view framework and the Dynamic Capabilities

Theoretically, the Resource-Based View (RBV) is the conceptual framework that considers the organization's ability to configure value-added resources that differentiate the firm from their competition. As stated by Crook et al (2008), the "resource based theory has become one of the most influential perspectives guiding strategic management research. In contrast to a recent review that concluded that Resource Based View theory, has 'received only modest support overall', (Nerbert, 2007 cited in Crook et al 2008).

Literature has been used the term 'resources' as a general term that refers to inputs into organizational processes, but within Resource Based View theory, the term 'strategic resources' is used when meets several criteria "it is valuable, such that it reduces costs or increases value to customers, rare enough that competitors do not use the same resource to compete away the value, and difficult to imitate or substitute, which keeps competitors from gaining parity" (Barney,

1991 cited in Crook et al 2008). On contrary, several authors argued that the Resource Based View theory did not "provide a specific structure that defines the precise mechanisms through which HRM policies influence business performance" (Wright & Gardner, 2003).

In response to these criticisms, a growing stream of literature has developed that attempts to build upon the RBV perspective to discuss dynamic capabilities as a source of enduring success (e.g. Eisenhardt & Martin, 2000; Helfat & Lieberman, 2002; Teece, Pisano & Shuen, 1997, cited in Messersmith & Guthrie, 2010).

Dynamic capabilities enable the companies to refresh themselves towards results achievement and they "impact firm value via their impact on the resource base value. These impacts can result in competitive advantages which may be temporary or sustained, depending on the dynamism in the environment. It is possible, then, that the resource-based advantages might be short-lived, owing to changes in customer and/or competitor behavior" (Ambrosini & Bowman, 2009).

# Hypothesis 4: How does human capital generated by SRHM impact on organization performance? Is there a positive relationship between human capital and organization performance?

The concept of human capital has been used to "represent the value of human resources (human capital) as well as with other concepts (e.g., intellectual capital, social capital, cultural capital), (Luthans & Avolio et al, 2007).

As described above on this page, several authors described human capital as an intangible resource, related with company performance outcomes and company competitive advantage that refers to the skills and knowledge obtained through education, training and experience. (Sturman & Cheramie, 2008). Consequently research on human capital is recently increasing due to economic situation, cost pressures and the need for increasing efficiency at the marketplace.

As stated by Luthans & Avolio et al (2007), "there was a positive relationship between PsyCap and performance and job satisfaction and that PsyCap was a better predictor of these outcomes than the individual components were supported". PsyCap is a "composite" construct that "so far include hope, resilience, optimism and self-efficacy" and that besides other criteria "have a positive impact on work-related individual-level performance and satisfaction". This "composite construct" itself is more powerful to predict job satisfaction and performance at work than each

one of their components. (Luthans & Avolio et al , 2007; Avey , Luthans & Smith et al, 2010; Avey et al, 2010).

At the present study, we want to consider the long-term performance efficiency, because one of the major criticism in human capital area is the "preoccupation with individual-levels" instead of "short-term organizational effectiveness (e.g., return on investment, stock value) and long term organizational effectiveness (e.g. long-term growth, increased market share, innovation, social responsibility), (Avey et al, 2010).

#### Methodology

#### Case study method

In this study we want to employ a longitudinal research design to analyze the impact of the Strategic Human Resources Management (SHRM) on company performance, using the case study method. Selection of this method takes in consideration the literature review about the appropriate methods on social sciences.

Since the study scope is the HR-Performance link, there is a need to be close to the implementation context at the organizations tracking company evolution. Consequently, the use of one qualitative research method will bring to this study a "description of the different types of changes that take place or the different outcomes that result" in order to explain how and why they arise, (Ritchie & Lewis, 2003).

Besides the need of company implementation tracking, this study involves decision about data collection schedule and that's why the decision was the case study method, as stated by Richie & Lewis (2003), "case study design also involves decision about the time frame for research, particularly the period of time which the research will relate, and the number of episodes of data collection required", (Ritchie & Lewis, 2003). A qualitative design needs to be flexible and allow changes during the phenomenon understudy takes place, as stated by Patton (2002), where the challenge here is "to figure out which design and methods are most appropriate, productive and useful in a given situation" (Pattou, 2002).

According to the literature, the quality of qualitative research studies are judged by the scope for generalization, that means, whether they can be generalized to a similar population "representational generalization", to other contexts "inferential generalization" or that builds theoretical statements that can be used in another studies "theoretical generalization" (Ritchie & Lewis, 2003).

A case study "is an empirical inquiry that: (1) Investigates a contemporary phenomenon within its real-life context; when (2) The boundaries between phenomenon and context are not clearly evident; and in which, (3) Multiple sources of evidence are used" (Yin, 1984).

#### Advantages and Limitations of the Case Study Method

According with literature, one of the major limitations of the case study it is that the conclusions only can be applied at the research scope studied and might not be able to generalized the conclusions to other contexts. Some methodological researchers have the position that the case studies are weak for theory building, however, this position have at the bottom "the mistaken application of a correct principle – a principle that applies more, but still imperfectly, to the discovery of theories in data than to their testing" (Gomm & Hammersley, 2000).

On the opposite way, some authors recommend data testing as a complementary approach to the case study method, "investigators should maximize four aspects of the quality of any design: (1) construct validity, (2) internal validity (for explanatory or causal case studies only), (3) external validity and (4) reliability (Yin, 1984).

To make a case study an "exemplary research", the study must "be significant" with enlarged resources, "be complete" with distinction between the study and its context, "consider alternative perspectives", through the design study, "display sufficient evidence" with methodological treatment, and "be composed in an engaging manner", where the communication efficiency it is a key issue (Yin, 1984).

The selection of the case method considers the investigation issue characteristics. As we can see on Fig 2, we want to investigate a contemporary phenomenon within real-life organizations; where the limits between the phenomenon and context are not clearly evident (due to competitive pressures and the need of competitive advantage at the organizations).

In order to draw relationships conclusions, the data should not be only cotemporaneous. In fact, we want to challenge the study design by using longitudinal data, in order to have a predictive design. Research about HR-Performance relationship has been "paid inadequate attention to temporal precedence and/or alternative explanations", (Wright et al, 2005). Most of the studies are post-predictive and few studies consider a predictive design, where "HR practices assessed at one point in time were related to subsequent firm performance", (Huselid, 1995, Youndt et al, 1996 and Youndt & Snell, cited in Wright at 2005).

In summary, due to these research characteristics above mentioned the decision of the case study seems to be the appropriate method, when combined with the longitudinal proposed design.

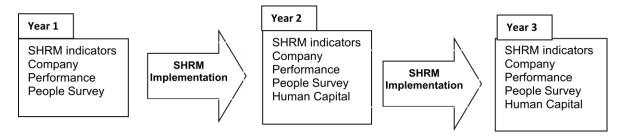
#### Sample

The study intends to be done with a sample of companies operating on the same activity sector at the Portuguese labor market, in order to have nationality significance.

### Data Collection Plan (longitudinal research)

The data collection will be done during a 3 years period (3 business cycles), before and after SHRM implementation, and, at the same time tracking SHRM indicators, company performance, people survey data and testing human capital indicators.

Fig 2. Data Collection timeframe



Source: Author

The proposed data collection method and timeframe takes in consideration the empirical findings. As emphasized by (Wright ,1997 cited in Avey et al , 2010), "the importance of time as a main effect variable in organizational behavior research, and proposed stability over 6 months as an operationalization of the temporal distinction between traits and states".

#### Measures

Organization performance and outcomes will be assessed by the company financial reports (e.g. Gross Margin, Operational Costs, EBITDA and Market Share). Strategic human resources management practices will be assessed through company HR records (e.g. performance records, training participation, competencies assessment, bonus and merit increases).

To isolate the effects of human capital on company performance, we want to control several variables that are considered drivers of employee performance: company satisfaction, job satisfaction and job retention, assessed through the company employee surveys.

The selection of the above mentioned measures, takes in consideration the empirical findings, as "several potential outcomes, in addition to direct, objectively measured performance, such as productivity, work sampling, organizationally administered performance appraisals, merit-based salary increases, and rated performance by supervisors and self, have been explored as relevant to work related outcomes". (Luthans and Avolio, 2007; Youssef & Luthans, 2007).

Human Capital created by HR practices will be measured through a questionnaire.

#### **Expected results and contributions**

The Strategic Human Resources field, in their search for common research have been studying the HR-performance link and examining the mediating variables between them since a direct impact has not yet been proved.

This study aims to achieve a deeper understanding of the variables that affect the process stream, starting with HR practices and their impact on people and the consequent human capital creation that impacts business performance.

This study aims to give a contribution to increase knowledge in one of the major criticism that presently exists concerning the relationship between human capital and performance. Specifically, it focuses on the lack of relationship with short-term and long term performance outcomes. It also aims in contributing human resources improvement, enabling it to be prepared to act more strategically, thus increasing the companies competitive advantage and therefore allowing them to be prepared to face major challenges in the near future, having in consideration the present economic constraints of the Portuguese economy.

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