

Institute for High Performance Business

Human Capital Development

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Recent surveys reveal that although business executives firmly believe that people are the most important asset, most executives are at a loss to prove that investments in people lead to improved business results.¹ Common metrics like economic value added (EVA™) and return on investment (ROI) shed little light on how an organization's human assets are performing. They say even less about whether an organization's people development processes are attuned to its business challenges.

Help is on the way in the form of new practices in the realm of human capital management. In this research note, we describe a project under way at the Accenture Institute for High Performance Business in collaboration with the Accenture Human Performance service line to link human capital management processes to financial performance. We refer to this as our Human Capital Development Framework (HCDF).

In subsequent research notes, we will detail key features of the HCDF, including its distinctive approach to measuring process effectiveness and results from its application in a panel of organizations. We believe any organization hoping to perform at the highest level needs to link investments in people to bottom-line business results.

The Measurement Paradox

Partial evidence abounds as to the connection between people development and financial performance. We know, for example, that companies that invest in "strategic human resource (HR) management" seem to achieve better financial performance than those that use approaches that are more traditional.² Unfortunately, correlation is not the same as causation. That is, it is still not clear whether

1. Accenture High Performance Workforce Study, 2002-2003, a survey of 311 CEOs, COOs and senior vice presidents. In addition, surveys Accenture has carried out on topics as diverse as intangible assets, business process outsourcing, and human resources strategy also reinforce that assertion.

strategic HR management drives superior financial performance or whether superior financial performance make it possible to take a more strategic approach to HR management. The same drawback appears in studies of employee satisfaction.³ That is, the ability of profitable companies to provide better pay and amenities than their competitors may lead employees to blur "engagement"—which connotes involvement and superior contribution—with satisfaction with pay.

What Needs to Be Measured?

Interviews we have conducted at Accenture clients and non-clients with senior HR executives, CFOs and financial analysts yield two recurring themes regarding the measurement of human capital. First, **measures need to be meaningful from an operational perspective.** That is, managers want measures that reflect the way value organizations create value. They want a measurement framework sensitive to differences in business models—particularly when an organization houses more than one business model, as is often the case in multi-division enterprises.

Second, measures need to be useful from an **investment perspective.** Executives want to know where they should be investing for the future—both in terms of the kinds of skills employees will need to achieve the organization's longer-run strategies and in terms of the kind of human resources

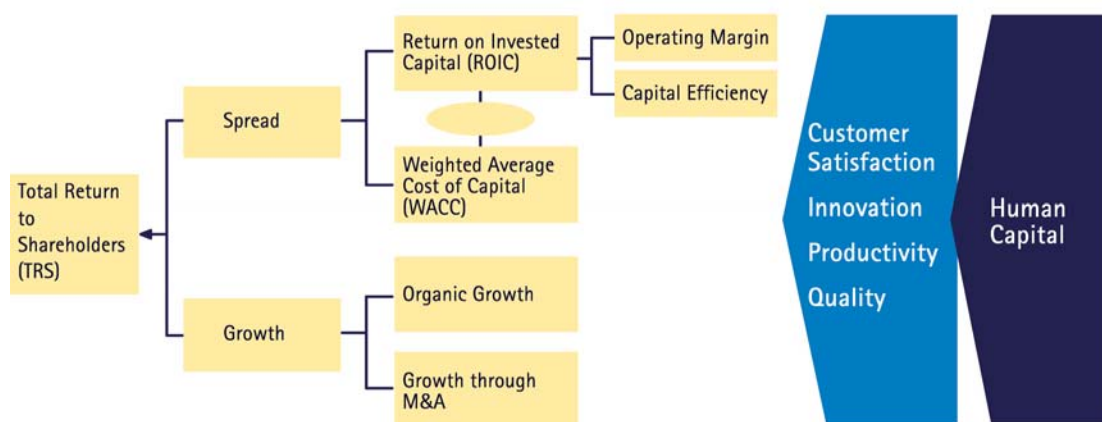
capabilities the organization will need to acquire, develop and retain employees with those skills. For example, HR executives and their counterparts in finance and operations want to assess the people-related risks associated with new technologies, new markets and new acquisitions.

We are hearing that superior performance requires managing human capital for today and for tomorrow—and to manage it in a fashion that is aligned with an organization's strategic objectives. To illustrate this point, consider diagram 1, below.

The left-hand side of the diagram is familiar to CFOs, the center is familiar to line managers and the right-hand side is familiar to HR professionals. An organization's relative emphasis on spread versus growth is a matter of both competitive environment and strategy, but behind its ability to create value is a finite set of capabilities or performance drivers, e.g., its ability to innovate, to satisfy customers and to produce quality. Behind those capabilities and beyond all its fixed assets, the most critical performance drivers are an organization's people, their knowledge and skill, and their ability and willingness to execute.

The challenge of effectively linking human capital development to financial performance is three-fold: (1) measures must capture direct and indirect effects; (2) the measurement process must be simple, repeatable and lead to actionable conclusions; and (3) results need to be compiled so that plans and forecasts can be built from them.

Diagram 1



2. For example: Brian E. Becker, Mark A. Huselid and David Ulrich, *The HR Scorecard: Linking People, Strategy, and Performance* (Boston: Harvard Business School Press, 2001); Jac Fitz-Enz, *The ROI of Human Capital: Measuring the Economic Value of Employee Performance* (New York:AMACOM, 2000); Jeffrey Pfeffer, *The Human Equation: Building Profits by Putting People First* (Boston: Harvard Business School Press, 1998); and David Ulrich and Norm Smallwood, *Why the Bottom Line ISNT: How to Build Value Through People and Organization* (Hoboken, NJ: John Wiley and Sons, 2003).

3. Marcus Buckingham and Curt Coffman, *First Break All the Rules* (New York: Simon and Schuster, 1999).

Accenture Human Capital Development Framework (HCDF)

The Accenture HCDF uses four distinct measurement tiers in arriving at an assessment of an organization's human capital practices. These tiers (diagram 2) reflect the key variables that influence the relationship between a company's human capital assets and its financial performance:

- Tier 1, **business results**, consists of measures of organizational performance (e.g., traditional financial analyses featuring EVA™, revenue growth, market share and stock performance).
- Tier 2, **key performance drivers**, consists of measures of intermediate organizational outcomes (e.g., productivity, quality, innovation and customer satisfaction) often captured on a balanced scorecard.
- Tier 3, **human capital capabilities**, consists of the most immediate and visible people-related qualities (including employee attitudes and abilities) that are necessary for achieving critical business outcomes. Their influence is felt through key performance drivers.
- Tier 4, **human capital processes**, consists of practices that lead to robust and effective human capital capabilities.

Included in this tier are core HR processes (e.g., competency management and performance appraisal) and broader human capital processes such as learning and knowledge management.

Of the four measurement tiers, Tier 4 is the most distinctive. Unlike other approaches to evaluating HR organizations (e.g., the HR Scorecard), we focus explicitly on the **maturity** of an organization's human capital development processes. That is, rather than look only at levels of spending to get a sense of an organization's approach to human capital development, we seek to understand how **complete** the underlying practices are and how **aligned** they are with the organization's competitive strategy and mission. Embedded in each of the Tier 4 variables is a multi-dimensional maturity scale grounded in industry best practices and modified as a result of employee evaluations.⁴

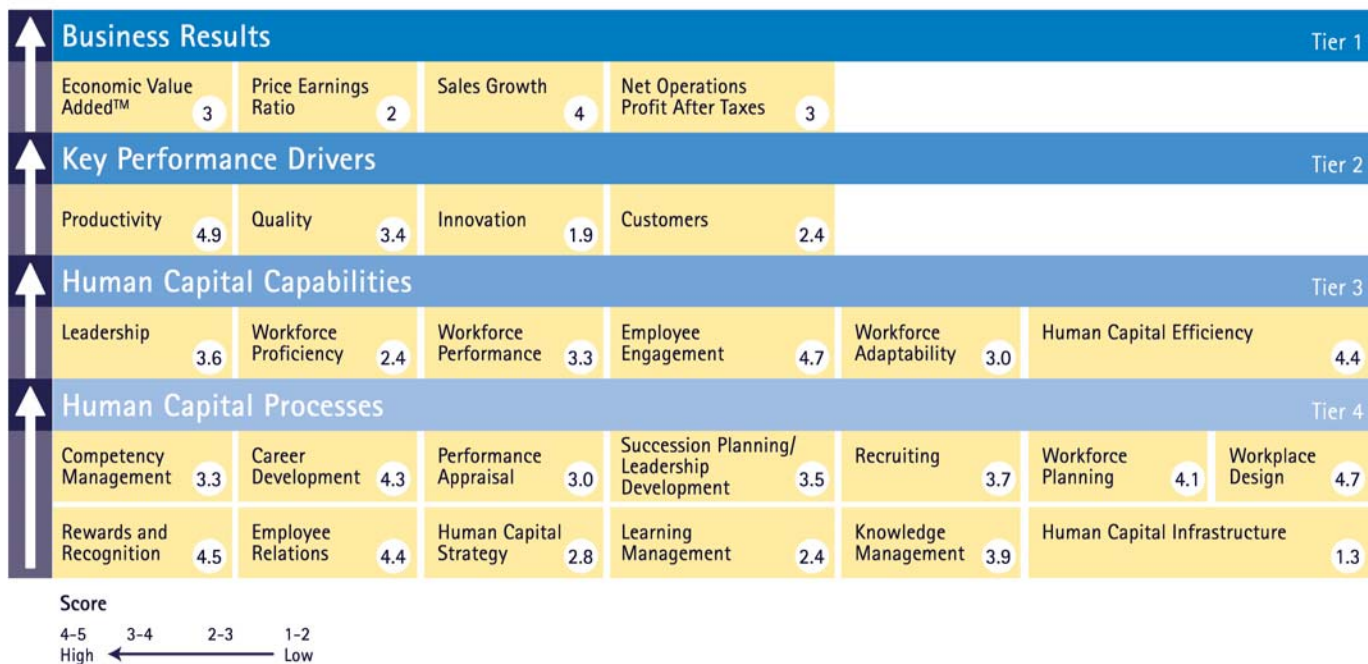
Once data are collected, an assessment is generated that represents—in numbers, graphs and against benchmarks—an organization's ability to use human capital to generate business results (see diagram 3). Each attribute in the model is scored to reflect the maturity of the factor to which it corresponds. Low scores indicate an absence of capability or maturity, and high scores indicate an extensive level of capability or maturity. These assessments can be compared across business units in the same enterprise.

Diagram 2



4. An upcoming Research Note will provide more detail on the construction of the maturity scales.

Diagram 3



Next Steps in Human Capital Management

We are now entering the second and most challenging stage of the effort: demonstrating empirically that investments in human capital assets and processes affect a company's growth and its value to shareholders. Fortunately, SAP has joined with Accenture in supporting the research, engaging leading-edge companies in testing its promise and in furthering the cause of measurement in human capital management (HCM). The research alliance's aim is to improve the model and accelerate its integration with next generation HCM software.

In upcoming Research Notes, we will describe the HCDF more deeply. For example, we lay out the logic behind our process maturity model and explain why we think maturity rankings should eventually be publicly reported. We will describe several instances of practical experimentation we uncovered in our background research. And, finally, we will report the results of our beta studies.

If you are interested in participating in the beta study of the HCDF, please contact us at institute@accenture.com. In return for your participation, Accenture will provide you with an HCDF report specific to your organization.

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