

Investing in People: An Introduction to Human Capital

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Strive for excellence, not perfection. – H. Jackson Brown

The average company spends 36%-38% of its total revenue on its workforce but few companies really understand the ROI for such investment. Many accept this as the cost of doing business. This mindset has evolved because measuring the workforce's potential and abilities has been deemed impossible. While budget and workflow can be observed and measured by hard measures, variables such as employee morale, workflow, knowledge level, and beliefs fall under the term Human Capital.

But this is changing, as there is movement in many Fortune 500 companies to learn more about what Human Capital really is and how to capture and measure these variables to increase productivity, profit, and investor confidence. This is leading companies to move from just measuring the hardware (e.g., P & L) to understanding the software that runs the company (e.g., corporate culture). The main purpose is to better understand the corporate needs so the organization can put in place the strategies that are needed to increase productivity and efficiency. It appears the days of taking the short-minded solution and to implement massive budget cuts to present a better balance sheet to investors is changing. Today, many more corporations are looking for help with a better decision-making process that will positively influence their longevity.

One of the main challenges for corporations is getting people to execute effectively day in and day out and to be motivated to do so. Companies rent people's behaviors; they do not buy their souls. It is clear that when an employee is passionate, motivated, and committed to a cause they understand and believe in they will be more productive. But today it is clear that many companies are challenged in how they manage people and struggle to obtain effective execution and productivity. There are few companies that have all their people working at 70% of their potential. What would the ROI be if all employees worked at 80% of their potential? How much better would the company be? This is an example of a variable that the study of Human Capital looks to capture.

It is clear that the vast potential in every company is its people. People are what make a business successful or not – no leader alone can make a company profitable. A brand, product, or service

is only as good as the people that make it, but people are often not viewed as solutions. Too often they are looked at as an expense. Why? Without understanding and implementing the science of Human Capital, a company will not be able to fully understand from a people factor what is working and what is not within the organization. This lack of insight will expose the company to operating without a well thought out Human Capital initiative, which will leave it open to being unduly influenced by what can best be described as “the flavor of the month attitude” that often arises from the company taking shortcuts, such as making big decisions by benchmarking from external data alone that is often not 100% congruent to the corporation vs. having a process that develops its own internal intellectual property for decision making. Yes, benchmarking has its place but cannot be the sole source of making people decisions. Another example of taking shortcuts is when companies try to buy human capital solutions. Instead of developing people from within, the company goes out and tries to buy a people solution to gain a quick fix, for example by bringing in a top gun. The research reports that 50%-80% of all acquisitions of top guns fall short of the anticipated payback. Again, this may be a solution but one which can expose the company and devalue its people.

What is Human Capital?

Human Capital is the science that explores how people work together within one system toward the goal of business success. All the components of human capital are interconnected, so if you change one part you influence all the others.

Eight Components of Human Capital

1. People – refers to the knowledge, skills, and attitudes of the people and how this directly impacts the company’s overall performance in the marketplace.
2. Leadership – the senior leadership determines the temperature of the culture by their actions, behavior, and messages.
3. Knowledge Management – the flow of information and knowledge and how it moves impact productivity and efficiency.
4. Strategic Decision Making – the process of how business decisions are made impacts the corporate footprint and market share.
5. Management and Organizational Structure influences the day-to-day operations.
6. Reorganization Systems – the formal and informal rewards that impact employee motivation.
7. Process vs. Practices – controls how work process and workflow impact quality and operational effectiveness.
8. Measurement of Progress – this is the system to monitor and measure individual, group, and division expectations to ensure execution of the corporate business plan is being achieved. This impacts leadership and management’s ability to obtain clear accountabilities. As well, it makes the positive and negative consequences clear.

The goal of understanding the above eight factors is to provide a structure that will support the organizational strategy to help the company gain an advantage in the marketplace. Each company has its own unique challenges. Actively developing the eight factors will add value to the overall system to develop the corporation's "best practices" for maximizing human capital.

An important first step is to understand the present human capital situation. To do this, it is useful to ask some fundamental questions, such as:

1. What is our present strategy in each of the eight human capital components?
2. What is our human capital costing us?
3. What are we spending on monitoring and evaluating human capital today?
4. What is our present corporate footprint?
5. What is our senior leadership focus?
6. What is our ROI on human capital?
7. What can we improve by doing a process re-engineering review (a study that will determine the corporation's effectiveness at managing people in the workflow to determine if there is a need to combine roles, cut roles, re-allocate resources or invest in resources and infrastructure)?

10 Recommendations for Implementing Human Capital Management

For each organization it is critical to determine and give one senior leader the mandate to champion human capital and keep the CEO up to date on progress, as well as to provide recommendations for enhancing and developing human capital throughout the entire organization. Below are ten recommendations for the champion of Human Capital who has been given the mandate for overseeing this important initiative:

1. *Promote the Value of Beliefs* -- To get a sense of value in the world of business one would need to look at the return gained from the output for focusing on promoting values and beliefs. There is no limit to the potential of people and to tap into this endless resource is critical for a corporation to promote Olympic thinking and to take the industry lead. It is vital that people feel they are of value and important to the success of the company. The belief that people are important needs to be promoted and driven throughout the culture. People cannot be viewed just as expenses; they need to be seen as the lifeline of the corporation. It is important to craft and present one universal message and follow through on the corporate values and beliefs as to the kind of organization it is committed to be. All senior managers need to be promoting the same message.
2. *Monitor People's Attitudes and Behaviors* – Facts are critical for business success. This sounds obvious but many companies make too many decisions based on perception and history rather than hard facts. It is important to stay curious and implement a strategy to stay in touch with the workforce. To do this there is a need to ask lots of questions. These can be asked using surveys, focus groups, outside research, and so forth, to ensure

senior leaders have real facts and accurate information in real time. The goal is to keep clear optics on the perceptions and behaviors of the workforce so that leaders have the correct information to make the necessary decisions to keep the corporation on track. This is an on-going process that cannot be done only when crises occur. The strategy is to be proactive and avoid problems before they occur, as well as build loyalty within the culture to the point that each employee understands their opinions are important and are valued.

3. *Make the Study of Human Capital a Process, Not an Event* – It is important to stay current and be open to new ideas and research to enhance the organization’s human capital. There is no one theory or model that has been proven or that has been agreed upon that sets the best standard for all organizations. But saying that, it is becoming clear that focusing on human capital is an important initiative for the corporation’s long-term success. As Jack Welch taught the business world, one of the best ways to stay ahead is to promote the mentality that whenever a system appears to be working try to make it better. This will keep the corporation from becoming complacent.
4. *Become Effective in the Use of Human Assets* – Clearly determine the roles and functions of each person and ensure they have a clear EAC (expectations, accountability and consequence) standard so they know their place within the organization and what is expected from them. Job descriptions are not enough. This strategy will help the company in attracting, developing, and retaining talent. Too many employees are not clear as to how important they really are in the big picture. Business is changing daily and this directly impacts people’s roles and functions.
5. *Develop Core Competencies Standards* – For each role it is important to establish a clear competency profile for the knowledge and skills the role needs to be successful and to measure an employee’s performance based on how effective they are in each core competency. This profile, like the job descriptions and roles, needs to be adjusted as business needs change.
6. *Plan for Human Capital Initiatives in the Business Plan* – Research suggests that 3.6 percent of the total compensation of each role is one statistically sound number to use for determining a budget for professional development. In addition, the budget needs to include all the other core functions of human capital initiative to keep them alive and current. It takes resources, time and dedication to oversee this initiative over the long term to ensure it is done correctly and provides senior leadership with the data needed to make critical decisions. One of the best insurance policies a company can have is to be tuned in to each of the eight human capital components.
7. *Learn About System Thinking* – A corporation is a complex system that needs to be understood. It is critical that the champion of this program is able to define and have a strategy for developing each of the eight factors of human capital. This will help educate senior management as to what is really going on within the organization system to provide risk management and avoid unnecessary exposure, with the goal of increasing overall success.

8. *Establish Human Capital Strategy* – It is important to develop a corporate blueprint for senior leaders of all the workforce requirements, best practices, and management models so that the corporation has an opportunity to be in the best position to achieve positive business performance. Having a set of human resources policies will not be enough. This is a corporate strategy for utilizing its people capabilities, knowledge, skills, and attitudes to its maximum advantage, as well as enforcing protocols and standards that are managed and enforced by the traditional human resources group.
9. *Implement On-going Human Capital Internal Audits* – To keep a pulse on what is really going and to monitor the eight factors, it is important to have ongoing audits that measure the performance of the people. This is in addition to traditional performance reviews. This is not only coaching people where they can improve; it is also seeking information by asking how senior leadership and management are doing (single loop feedback) and asking employees what they are doing to fix problems and meet challenges (double loop feedback). As long as employees have evidence that their feedback is being used they will be responsive and open. But if over time they come to the point where they believe that their views are never acted on or heard, then there will be resistance. People want to be heard and for this model to work senior leaders must want the information and be willing to respond in a proactive manner. Debate is healthy, as long as it is two-way.
10. *Align Career Development with Human Capital Initiative* – A corporation that has an Organization Learning Group should ensure that this group is engaged and educated on recruiting, diversity needs, human resources, and review systems to ensure the professional development and career planning are consistent with current corporate issues (e.g., business practices and ethics) and long-term needs of the corporation. This group is critical for the Human Capital Initiative to be successful, as they have a direct influence on the development of knowledge and skills of the people within the corporation.

In closing, this brief is designed to provide an overview of what human capital represents and the considerations for implementing an effective human capital initiative. For companies that want to be successful over the long term, considering the human factor is no longer a luxury; it is a necessity.