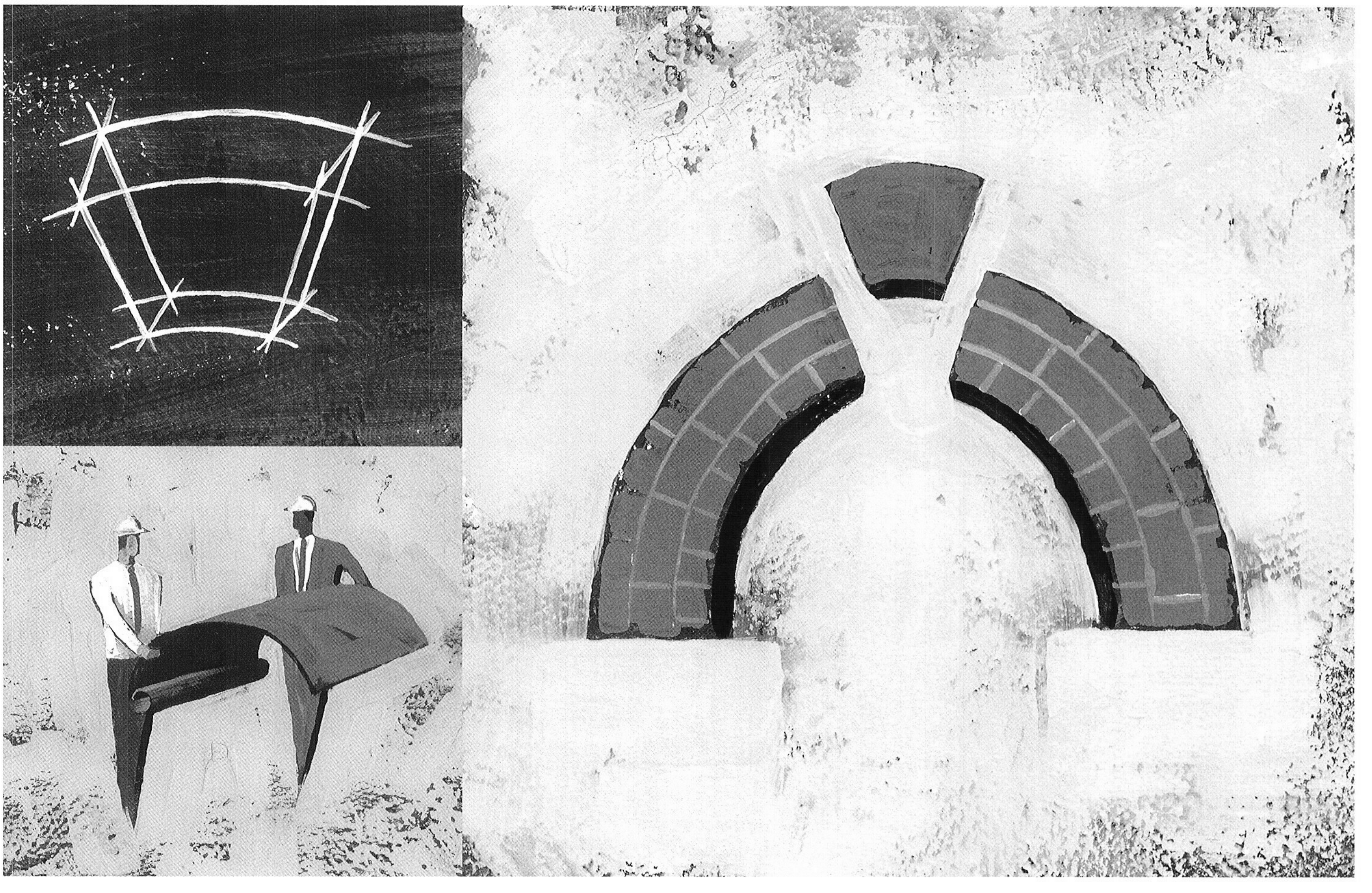
Building a Strategic HR Function: Continuing the Evolution

Jay J. Jamrog, Human Resource Institute and The University of Tampa; Miles H. Overholt, Human Resource Institute



This article traces the evolution of the HR profession over the past 100 years, then looks at its current role as strategic business partner and the lack of measurement to prove HR is adding value. For HR to continue to build a strategic function, it needs measurement tools that go beyond assessing HR's *output* to focus more on the *impact* HR is having on the execution of the business strategy. Our research on how all the various people components in organizations interact with each other, and how HR influences the various components, points to a need for a complex model for measuring the organizational effectiveness if HR is going to evolve to the next level. This article concludes with the theoretical grounding for just such a model.

Over the past 100 years the HR profession has been continuously evolving and changing, adding more and different responsibilities. While some historians go back to England and the guild movement when tracing the HR profession, most point to the early 1900s, when many of the components of modern human resources management were falling into place. Out of the Industrial Revolution came the birth of labor unions, the Civil Service Commission, the industrial welfare movement, and groundbreaking research in scientific management and industrial psychology. This led to the establishment of the first personnel departments during the 1920s. This new function employed specialists to oversee areas like employment, employee welfare (financial, housing, medical and educational), wage setting, safety, training, and health.

During the '30s, '40s and '50s the profession was enhanced by the human relations movement as well as the academic and applied disciplines from the behavioral sciences and systems theory. Despite this growing body of knowledge, in the 1960s the personnel professional was often viewed as little more than a glorified file clerk who planned the company picnic. This all changed with the passage of the Civil Rights Act of 1964 and the subsequent social, demographic, technological, and economic trends in the '70s and '80s. Top management began to take notice, and the modern HR professional was born.

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In the 1990s, experts noting the growing importance of human capital began to urge HR to evolve even further and become strategic business partners. While many HR professionals today still struggle to get a seat at the business table, the HR profession in the future should continue to evolve and take more responsibility for overall organizational effectiveness. To do this the HR professional will need to become better at utilizing systems thinking and systems measurement.

The Past

The Industrial Revolution

Some historians trace the origins of personnel/human resource management to medieval times, when masons, carpenters, leather workers, and other craftspeople organized into guilds in order to improve their work conditions (Gilbertson, 1950; Ling, 1965; Megginson, 1972). Students of personnel history point out, however, that prior to 1900 first-line supervisors handled most personnel problems (Eilbert, 1959; Hagedorn, 1958). Not until the early 1900s did factors come together to accelerate clearly the development of what would become the first personnel departments (French, 1990).

The Industrial Revolution fueled most of the early development of the HR profession. The Industrial Revolution began in the mid-18th century with the substitution of steam power and machinery for time-consuming hand labor. This led to the establishment of factories where large numbers of people were employed. The result was a tremendous increase in job specialization as well as in the amount of goods that workers could produce. The "division of labor" became the rallying cry of this period (Cascio, 1992). As a result, working conditions and social patterns were significantly altered (Ivancevich & Glueck, 1989).

With these changes also came a widening gap between workers and owners. Owners generally did quite well for themselves, but the average worker fared poorly in comparison in terms of purchasing power and working conditions. Labor was considered a commodity to be bought and sold, and the prevailing political philosophy of laissez-faire resulted in little action by governments to protect the worker (French, 1986). Because of the abuse it was inevitable that workers would attempt to organize to protect themselves and improve their lot in life. The Industrial Revolution fostered specialization and the need for workers within each specialization to organize against the abuse of workers, especially children. As a result, organized trade or labor groups spread rapidly during the latter half of the 19th century, and so did the incidence of violent strikes (Cohen, 1960).

Scientific Management

The call for "division of labor" during the Industrial Revolution gave rise to the scientific management movement. The prophet of scientific management was Frederick Winslow Taylor, and his "bible" was the stopwatch (Bell, 1975). Working in the steel industry in the late 1870s, Taylor believed that the same techniques used by scientists in the laboratory could be used by management to increase efficiency in the workplace (French, 1990). While he is best known for pioneering the scientific study of jobs (time-and-motion studies), he also pointed out the inefficiency of the foreman-oriented personnel system. Taylor put forth three important concepts that provided the foundation for the modern HR profession. He believed that individuals selected to do the work should be as perfectly matched, physically and mentally, to the demands of the job as possible and that overqualified individuals should be excluded. Second, employees should be trained carefully to ensure that they performed the work exactly as specified and that in no case should employees work at a pace that would be detrimental to their health. And, finally, there should be incentives for employees to follow the detailed procedures specified (Taylor, 1911).

The Civil Service Commission

Another early influence on the development of the HR profession was the Pendelton Act of 1883, which established the U.S. Civil Service Commission. Drawing many of its ideas from the British civil service system, the Pendleton Act established the use of competitive examinations for admission into public service; provided job security for public employees, including those who refused to engage in politics; prohibited political activity by the civil service; and encouraged a nonpartisan approach to employee selection (Van Riper, 1958). Perhaps the major impact of this act was to foster employment promotion policies in the federal government on the basis of merit.

The Industrial Welfare Movement

Toward the end of the 19th century, more organizations seemed to take note of and do something about the conflict between employees and management. At the time Taylor was bringing attention to "scientific management," many firms began involvement in the "industrial welfare movement" (Eilbirt, 1959; Hagedorn, 1958). This movement consisted of "voluntary efforts on the part of employers to improve, within the existing industrial system, the conditions of employment in their own factories" (Gilberth, 1914). As an outgrowth of this movement, many firms began to employ staff members called *social secretaries* or *welfare secretaries*. The job of these early personnel administrators was to bridge the gap between management and worker; in other words, they were to speak to workers in their own language and then recommend to management what had to be done to get the best results from employees (Ivancevich & Glueck, 1989).

Early Industrial Psychology

Applications of industrial psychology began to emerge in the 1890s and early 1900s as psychologists studied selling techniques and ways to test job candidates. The most notable early industrial psychologist was Hugo Munsterburg. In 1913, he published the results of experiments in selecting streetcar operators, ships' officers, and telephone switchboard operators. In this groundbreaking work he showed: 1) the importance of putting more emphasis on the analysis of jobs in terms of the abilities required to do them and 2) the development of testing devices to match individuals to jobs (McAfee & Poffenberger, 1982; Moskowitz, 1977). Paralleling these developments were advances in checking references, in the use of rating sheets for interviewers, and in statistical methods for estimating validity of selection devices. World War I accelerated the development of intelligence tests so that each individual could be matched more effectively with job requirements. Other kinds of psychological measures also appeared during and after World War I, such as measures of aptitude, interest, and personality (Ivancevich & Glueck, 1989).

The Birth of the Personnel Department

While historians disagree on the specific date assigned to the appearance of the first personnel department, most agree that, between 1900 and 1920, more organizations were employing specialists to assist with personnel matters. The term "personnel" began to appear about 1909. It was a major index entry in the Civil Service Commission's report of that year, and in 1910 the secretary of commerce and labor used the term in a major heading in his annual report (Eilbert, 1959). By the 1920s a number of *personnel specialist* jobs began to emerge. In 1911, U.S. Steel created a Bureau of Safety, Sanitation, and Welfare. By 1918, International Harvester Co. had established a Department of Industrial Relations, and Ford Motor Company had created a Sociological Department that combined medical, welfare, safety, and legal aspects of employee relations. In 1917, Standard Oil of New Jersey established a retirement income plan, substantial insurance benefits, a safety program, and a medical division (Boettiger, 1923). To coordinate many of the new programs, Standard Oil created a personnel and training department. This specialization formed the basis for the modern HR department.

The Human Relations Movement

What came to be known as the human relations movement has been a major influence on modern human resources management. This movement was characterized by the focus on group behavior and workers' feelings as they relate to productivity and morale. In 1923, the Hawthorne Works of the Western Electric Company in Chicago was the site of one of the most famous behavioral research efforts of all time. In one experiment, production increased when the lighting was improved, but in another it also increased when the lighting was severely reduced (Johnson, 1975). After three years of experimentation with such "illogical" results, some observers concluded that productivity was directly related to the degree of group teamwork and cooperation. The level of teamwork and cooperation, in turn, seemed to be related to the interest of the supervisor (or researcher) in the work group, the lack of coercive approaches to productivity improvement, and the participation afforded the workers in changes affecting them (Pennock, 1930; Roethlisberger & Dickson, 1939).

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The conviction that group behavior and workers' feelings were associated with morale and productivity characterized much research and theory in the human relations movement for the next two decades. These new concepts were, unfortunately, popularized as the "Pet Milk Theory." Based on a commercial for the Pet Milk Company indicating that their contented cows produced better milk, the Pet Milk Theory put forth that happy workers are productive workers, and it provided the rationale for trying to improve the workers' social environment with company picnics, newly created status symbols, employee coffee rooms, and other gimmicks. This approach was widely discredited during the late 1950s. Failure to find evidence that these programs made a difference in workers' satisfaction or that happy workers were productive workers helped kill this approach to human resource management (Cascio, 1992).

The Labor Movement

If, as some historians say, personnel has risen and fallen in prestige with the power of the trade unions (Glueck, 1974), then 1935 clearly advanced the HR profession. Although the labor movement started before the turn of the century, prior to 1935 the courts tended to side with management and adopted a decidedly anti-union stance. In 1935 the Wagner Act, technically called the National Labor Relations Act, was passed, allowing union employees to choose representatives who would exercise exclusive bargaining rights for all employees in that union. It became an unfair labor practice for an employer to coerce or restrain employees in the exercise of their rights, to dominate or interfere with a labor organization, or to refuse to bargain collectively with a legal representative of the employees. After 1935, organizing activities by labor unions increased greatly, and in many companies the job of either keeping unions out, monitoring the organizing efforts, bargaining with the recognized union, and ensuring that the collective bargaining agreement was enacted often fell on the personnel, legal, and/or labor relations department.

The Birth of the HR Professional

Despite the development of a greater body of knowledge and understanding of how people behave in organizations, in the 1960s the personnel function was still viewed as a record-keeping unit that handed out tenure awards and coordinated the company picnic. Peter Drucker, a respected management scholar, stated that the job of personnel was "partly a file clerk's job, partly a housekeeping job, partly a social worker's job, and partly fire fighting, heading off union trouble" (Foulkes, 1975). The passage of the Civil Rights Act of 1964 accelerated the rise in importance of the personnel/HR function. Class-action suits and the large financial settlements of winning suits illustrated the costs of improper personnel management. Managers outside the personnel function began to take notice because top management made it clear that ineptitude in this area would not be tolerated. Within the function, HR specialists with particular competencies began to appear, and considerable resources were devoted to compliance activities.

Behavioral Science Research

An outgrowth of the human relations movement, the behavioral sciences approach to managing people embraced a wider base of disciplines (industrial/organizational psychology, organization theory, organization behavior, and sociology) and concerned itself with a wider range of problems. As a result, much of the knowledge about human resource management and many of its practical applications have come from the behavioral sciences (French, 1986). Through research conducted by these academic and applied disciplines we now know that the way people behave in organizations cannot be explained simply by human relationships. The organization itself, its unique culture and constraints, all impact and modify human performance. The way the organization is structured, the authority in different positions, and job and technology requirements also clearly affect behavior.

Systems Theory

Since the late 1940s, and especially during the 1970s and 1980s, HR professionals have drawn on the emerging knowledge from systems thinking. Systems thinking is a conceptual approach that views all events as interrelated and part of a greater whole. By emphasizing the relationships among the parts of the whole, HR professionals could understand how a change in one component of an organization can have repercussions throughout the firm. For example, if a corporation hires people with greater skills and more education than those it has hired previously, it may also need to upgrade its training programs and pay more attention to opportunities for advancement.

Historically, systems theory can be traced back to the concept of "natural philosophy" in the early Renaissance. Naturalists were describing their perception and discovery that all aspects of nature are interrelated and interdependent. Over the centuries, this abstract, non-linear thinking was incorporated into the sciences, particularly in what are now known as the biosciences. Ludwig von Bertalanffy, an Austrian biologist and an international scholar from 1930 through the 1960s, is acknowledged as the modern founder of general systems theory (Bertalanffy, 1968). In the social and organization sciences, James G. Miller articulated the basic principles of systems thinking (Miller, 1972). He carefully applied Bertalanffy's thinking to organizations, describing the basic principles in axioms and postulates. His is the foundational work for most of today's proponents of viewing organizations as systems. Famous organizational theorists such as Ackoff, Deming, Beers, Lawrence and Lorsch, Schein, Argyris, Mohrman, Lawler, and Porter (Ackoff, 1981; Deming, 1993; Galbraith, 1973; Lawrence & Lorsch, 1969; Mohrman & Lawler, 2003; Schein, 1987; Senge, 1990) have built their theories on a foundation of systems thinking.

In Eastern thought, systems thinking can be traced back at least 5,000 years in the roots of classical Chinese medicine. In the 3,000-year-old text *The Yellow Emperor's Classic of Medicine*, the Chinese emperor listens to his advisors detail how lifestyle, eating choices, and thought are interrelated to create health and disease. This theoretical foundation is the basis for acupuncture and for the practice of moving one's personal energy to create health, as in QiGong and Tai Chi.

With the current convergence of Western and Eastern thought, few organizational experts are surprised at the emergence of systems theory as the best way to view organizations. In 1999, David Nadler opened his keynote address to the HRPS Annual Conference by stating that we all understood that systems thinking was the basis for intelligent discussion of organizations.

The Present

Strategic Business Partner Model

In the late 1970s and early 1980s, many firms struggled with the combined impact of high interest rates, growing international competition, and shrinking productivity, which led to the demand for greater accountability in all functions of the company. The new HR function was not exempt from this trend, and while methods for assessing the costs and benefits of HR programs were available, they were not widely utilized. Because of the lack of accountability, many commentators and executives began to view HR activities as nonproductive drains on overall organizational performance. A few even advocated that the HR function should be blown up and the activities should either be outsourced, allocated to the legal and finance departments, or given to line managers. Amid the criticism the external environment was also changing. Social and demographic trends (more women and minorities in the workforce, growth of immigrants, older workers, and poorly educated workers) accelerated the demands for improving the quality of work life, for managing cultural and ethnic diversity, and for continual training and retraining.

As a result, during the '70s and '80s the HR profession was put under the microscope. While many companies still viewed HR professionals as personnel administrators, a growing number of professionals were responding to their changing environment, and in their firms they were seen as people who were truly adding value to the company and giving the company a competitive advantage. As a result, about 15 years ago, many HR experts began to urge HR professionals to adjust to the times by changing their role once again. The HR function, these experts felt, should add value to the firm in everything it does, and to this end they advised the HR function to move from transactional to strategic activities and to become strategic business partners. Human resource professionals must think of themselves as business people first and HR people second. HR professionals should be so well-versed in the operations side of the business, these experts argue, that the HR department is taken seriously when it offers insights.

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Today there is widespread agreement that HR professionals have indeed accepted the role as strategic business partner. The fourth iteration (2002) of the Human Resource Competency Study conducted by the University of Michigan Business School found that 43 percent of HR's impact on business performance came from its strategic contribution. A smaller study conducted in the same year by the Human Resource Institute (HRI) found that business partner and strategic thinker had become the most important roles of HR professionals in respondents' organizations.

Yet, there's something elusive and ambiguous about this widely touted goal of becoming a strategic business partner. At a recent conference on the future of HR, a panel of experts was asked to define "strategic business partner." After much hesitation, they finally agreed with the statement: "I can't define it, but I know it when I see it." Although a growing number believe they fill this role, they seem to be spending no extra time doing so, according to a study conducted by the Center for Effective Organizations. It found that a greater proportion of respondents (41.1%) said they were full partners in the development and implementation of business strategy in 2001 than in 1998 (29.4%). This statistic suggests HR is changing, but the authors of the study do not agree. Even though more HR professionals say that they are strategic business partners, the expected increase in time devoted to this role is not reflected in the data from 1995, 1998, and 2001. "It seems that instead of responding to the calls for change, HR responded by maintaining the status quo" (Lawler & Mohrman, 2003).

Other studies also point out that becoming a strategic business partner remains an elusive goal for many HR professionals. In a 2002 survey conducted by the Society for Human Resource Management, respondents were asked to select the best description of the view of HR held by the executives in their organizations. Only 34 percent indicated that HR was viewed as a "strategic partner." Helen Drinan, the former president and CEO of the Society for Human Resource Management, believes the HR profession is at a crossroads. "If HR does not force its way into the heart of strategic planning in organizations, it will default to a technical and transactional dead end," she said. She believes upper management in most organizations is finally willing to recast HR into a role as equal business partner, but HR managers have to be willing and able to step up to that bigger role. "There is a seat at the table. Is that seat going to be filled by an HR pro or someone else?" (Drinan, 2002).

Given the immense amount of attention over the years to the need for HR to change its role in the organization, why has progress been so slow? It is not because HR lacks the will to move in that direction: In an effort to free HR to become more strategic, traditional transactional activities have been either put online, centralized, or outsourced. It does not reflect a lack of knowledge: The competencies needed to transform the HR professional have been described in detail and made a top priority for most HR departments. And, as the preceding data show, it is not for a lack of effort; more and more HR executives believe that they *are* being business partners.

Is Measurement the Problem?

The problem may well be in the area of measurement—proving with data that HR is adding value. *The Accenture High Performance Workforce Study 2002/2003* found that a major shortcoming in many companies is "a lack of measurement on the impact of HR, which is preventing executives from understanding where and how they should best apply resources." The report went on to say that some companies are achieving success in this arena and that these organizations are more likely to see the HR function as valuable and strategic. This premise also is supported by the research conducted by Ed Lawler and Sue Mohrman. "When organizations have a strategy that focuses on knowledge and information, HR is much more likely to be a full strategic partner. Knowledge and information strategies inevitably lead to a focus on human capital and the degree to which the company possesses the knowledge and information it needs in order to implement the strategy" (Lawler & Mohrman, 2003).

Why should the measurement of HR's performance be the problem? After all, measurement strategies for HR have been around for over 30 years. During the 1970s, research and development using human resource accounting principles led to formulas for measuring the return on investment and value of human capital (Woodruff, 1970; Pyle, 1970; Lickert & Pyle, 1971; Baker, 1974; Scarpello & Theeke, 1989). This, in turn, led to the development of hundreds of efficiency and effectiveness ratios for measuring virtually every aspect of HR. The proliferation of these ratios made benchmarking against other organizations possible (Fitz-enz, 1995). In 1985, the Society for Human Resource Management and the Saratoga Institute started publishing an annual *HR Effectiveness Report*, which compares ratios across hundreds of companies. Technological advances allow companies to gather data quickly and to use dashboards to distribute the results. Today, many companies also have completed HR audits and implemented balanced scorecards for HR (Kaplan & Norton, 1996). In addition, surveys of workforce satisfaction or engagement are common in most large organizations. There are many other measurement strategies (e.g., *Watson Wyatt's Human Capital Index*), so why is a lack of metrics keeping HR from being a fully integrated strategic business partner?

The Future

Organizational Effectiveness

Maybe HR is simply not measuring the right things and therefore fails to gauge accurately its value proposition or its impact on the business. To be seen as strategic business partners, the HR profession must evolve to the next level: organizational effectiveness. Organizational effectiveness is the measure of how successfully organizations achieve their missions through their core strategies. Organizational effectiveness studies are concerned with the unique capabilities that organizations develop to assure that success (McCann, 2004). To understand how human resources impacts organizational effectiveness, these approaches to organizational effectiveness must embrace systems thinking and systems measurement.

As discussed earlier, a systems theory approach views all aspects of the organization as interrelated. And all systems have a larger system that they reside in and have smaller systems that reside within them. But what is the system? The system is any size group within the organization that has a natural affinity. For example, a training function within HR is a subsystem of the larger HR system, which is a subsystem of the company, and so forth. The interdependency between the company, the HR department, and the training function is easy to see. When the company rolls out a new quality process approach, such as Six Sigma, the HR department will assign the task of designing, developing, and delivering the training to its subsystem specialists in the training department. To be able to design and develop the Six Sigma program, training will need to coordinate with a group of other functions, such as research and development, engineering, and manufacturing. All these functions are interdependent on each other to design, develop, and deliver the needed training.

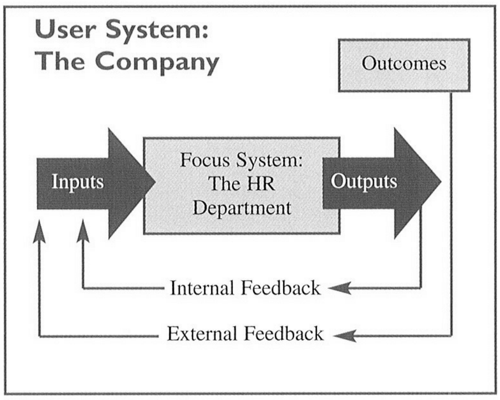
From a systems perspective of HR, the concept of *outputs* and *outcomes* (see Exhibit 1) must be understood. Outputs are generally considered to be things produced within the focus system (the HR department), and they cross the system boundary into the user system or systems (the company or other functions). Outcomes, on the other hand, are the effects that outputs have on the user system or systems. Alignment creates a system in which all inputs and outputs are balanced and used efficiently and effectively.

Systems exchange information continuously, a dynamic labeled *feedback*. Feedback (measurement) can be thought of as two types, internal and external. Internal feedback loops occur entirely within the focus system and contain information about the *output(s)*. In external feedback loops, the feedback information is obtained from outside the focus system and contains information about the *outcome(s)*. This external feedback finds its way back into the focus system and so is able to modify the process.

In our example, the training functions output is

EXHIBIT 1

Systems



how efficiently the Six Sigma training program was delivered and the outcome is the impact it has on increasing the product quality. The internal feedback is the training participants' feedback on how well the program was taught. The external feedback is the degree of improvement in product quality (see Exhibit 2).

Some of the best HR departments develop human capital objectives that clearly position them to be strategic business partners, e.g., the drive to win, be flexible, embrace risk, be creative, think globally, and be fast. The problem is that most, if not all, of the feedback that HR measures is the output of HR—the efficiency of a specific HR activity: headcount, turnover rates, number of succession candidates, time-to-fill, cost reduction, training completed, grievances, client satisfaction surveys, performance ratings, sales per employee, and best practices recognized (Boudreau, 2002). Knowing how many hours of training have been delivered with the current budget provides pretty much the same amount of information as knowing how many advertisements the marketing department is running. In either case, nothing is said about the impact (outcomes) that those investments had on achieving the organization's strategy. Just as marketing needs to know the campaign's impact on sales and brand recognition, HR needs to know the impact that the HR activities are having on the business (Cabrera & Cabrera, 2003).

If organizational effectiveness is the measure of how successfully organizations achieve their missions through their core strategies, then for HR practitioners to be true strategic business partners in the future, they must develop processes that directly measure the impact HR has on organizational effectiveness and the execution of the business's strategic priorities. Because of the pace of change, the need for this type of measure has been growing. Over the past three years, nearly 40 percent of the top 2,500 global CEOs have been removed from their posts. The vast majority of them were let go because of a failure to execute. "The main reason companies do so poorly at execution is that their leaders have either been unable or unwilling to make a connection between their company's goals and the realities of how their companies actually operate, how the market is actually performing, or how their customers' needs can change almost every day" (Charan, et al., 2002).

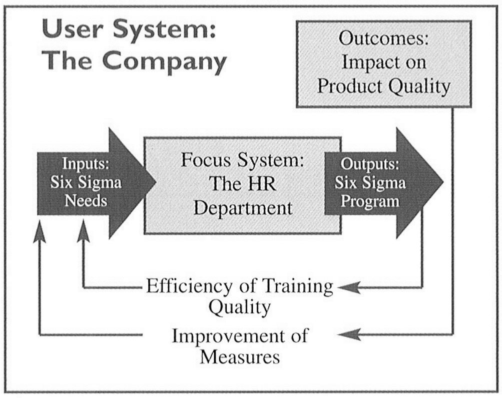
Good execution requires leaders to manage three interrelated and interdependent business components: people, strategy, and operations. Normally, executives devote a lot of time, money, and energy into developing a good strategy. And they often do a good job of aligning operations to support that strategy. The most common set of problems stem from leaders' failure to align their people processes with the strategic priorities of the company.

Measuring Organizational Effectiveness

Academicians, researchers, and consultants are rapidly developing ways for executives to assess and guide alignment to increase organizational effectiveness. Among these approaches are the search for correlations between HR practices and business performance measures (Huselid, 2001), the identification of links between human capital

EXHIBIT 2

HR Training Systems



resource practices with shareholder value measures (Pfau, 2002), and longitudinal studies that identify factors differentiating top-performing companies (Collins, 2001). In one form or another, these approaches attempt to measure the HR outcomes and their impact on how well the company performs. They are attempting to capture the interdependencies and interrelationships of the organization as a system.

Over the last three years, HRI, in collaboration with Elena Granell (University of Madrid) and Al Vicere (Pennsylvania State University), has been conducting research into the efficacy of measurement tools that assess how the larger business environment interacts with the company and how all the components of the company interact with each other, including how HR interacts with all the components and the company as a whole.

Once HR executives are comfortable in systems thinking, they need to develop a process for monitoring that complex whole—a process that listens for, and is actually attentive to, the alignment of the company's human capital with its strategic priorities. This process should help executives confront reality, analyze data, and conduct relentless follow-ups in order to find and solve problems quickly. The objective is to build a process that enables HR easily to see the linkages among the business environment, strategy, and execution. This process should work much like a global positioning system (GPS) in a new car. It shows where you are in relation to the larger system, the regional map, at all times, and it allows you to see not only where to make the next turn but where the alternative routes are as well. You can also see the whole region at one glance, understanding where you are within the region. When executives have the ability to see the whole system, as in a GPS map, and the direction they are headed, then their ability to align the organization with market shifts is greatly increased. This GPS for HR is a two-phased process that consists of what has been known historically as environmental scanning and the emerging field of organizational systems capabilities analysis.

In the first phase, HR (and the entire organization) must continuously scan the environment with the greatest impact on HR. A regular and consistent scanning process helps to develop insights into the changing ebbs and flows of the external environment and into how these changes affect strategic priorities and HR's work. To do this well, HR must have a deeper understanding of their company's business past, present, and future environment. Only by understanding the business environment can they understand how to influence where the organization meets the environment and where the strategy meets the market space. A SHRM study of eight leading consulting firms (SHRM, 2002) found that demographics, economics, technology, globalization, competition, customer focus, and the political environment are key indicators influencing HR's work. It is especially important today for HR leaders to scrutinize economic indicators carefully so that when the economy moves from recession to recovery, they are prepared to move with it.

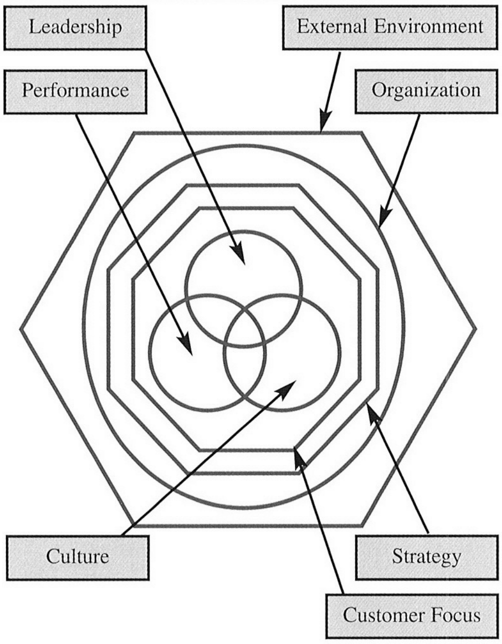
In the second phase, HR must be able to assess the organization's capabilities. HR and other executives need to know how all the organization's subsystems interact so they can create and maintain alignment, rebalancing the organization as the market shifts. In the past, leading companies have addressed this need in a variety of ways. For years, culture assessments have been state-of-the-art, serving as a way to see some of the whole organization. To supplement the culture assessments, most companies flood executives with survey results from leadership, customer satisfaction, employee behavior, and traditional business outcomes measures. The hope is that the executives will be able to integrate this data into a "map" of the whole organization. While some executives have been able to do this in the past, they have been unable to share it readily with others.

In the future, HR will use a measurement tool that creates a "map" of organizational effectiveness that enables executives to see quickly where the company's human capital is, or is not, aligned. This map should be able to locate key gaps in the company's connecting alignments and linkages, and should indicate which combination of factors makes one unit better than another. Our research indicates that information and knowledge around the interactions and interrelations of five key components are critical for determining alignment (see Exhibit 3):

1. Strategic alignment: How well the strategic priorities are transmitted, shared, and made consistent with people's values and behaviors.
2. Customer focus alignment: The strategic, performance, and people approaches needed to focus successfully on the customer relationship.
3. Leadership and talent management alignment: How the leadership style, communication, motivation, commitment, and behaviors create

EXHIBIT 3

Organizational Effectiveness



the necessary climate for the organization to be productive.

4. Performance alignment: How the processes and day-to-day behaviors and activities match and support the strategic priorities.
5. Cultural alignment: The values and beliefs of employees and the processes that directly link them so that their behavior supports the strategy.

Using this as a theoretical model, HRI also has developed an approach to measuring the organization as a whole system. Initial results from alpha testing of our Organizational Capabilities Index are very revealing. Executives and managers readily understand systems theory when the feedback is given in typical business language. They can easily see the impact of misaligned programs and policies and quickly develop strategies for change. So the concept of providing a GPS reading truly works, and now the HRI team is looking forward to conducting extensive applied research.

Our work so far has led us to several conclusions. First, companies are always in a state of flux and need to be continuously realigned. Second, organizations always have their own unique alignment. Thus, organizational capabilities analysis will simply identify where the organization is at a particular time. No organizational capabilities analysis will be couched in terms of good or bad. Third, technology enables us to see the complexity that surrounds us more than ever. We need to be ready to understand and manage the complexity because our era demands it. In the future, systems measurement should be about prediction—strategic planning—and the ability to do "what if" analysis. For example, if external environmental shifts (economy, customers, competition, etc.) cause the organization to shift its strategic priorities, then what organizational capabilities also must shift (culture, leadership, performance, etc.) in order to align the people to support the new strategic direction? And if HR shifts certain dimensions of leadership, what will the impact be on customer focus or other key components?

Conclusion

Returning to our historical perspective, we need to address the broader question of what this means for the HR profession. What is the bottom line for HR? For at least the last decade, Dave Ulrich (Ulrich, 1997) has been writing about and demonstrating the need to become a strategic business partner. He has been a true visionary, accurately seeing the need for HR to become a more powerful influence in companies as human capital becomes the key strategic differentiator. The need for this role will only increase in the future. To become strategic business partners, he believes, HR professionals need competencies that fall within a three-domain framework: 1) knowledge of business (which includes financial, strategic, and technological capability), 2) knowledge of HR practices (which includes staffing, development appraisal, rewards, organizational planning, and communication) and 3) management of change (creating meaning, problem-solving, innovation and transformation, relationship influence, and role influence) (Ulrich, 1997).

Given the complexities of managing people in organizations today, and even more so in the future, we would add a fourth domain to this competency framework: the ability to measure organizational effectiveness. This tool helps show the necessary alignments and linkages among strategy, people, and daily work, and the influence and interaction of these components with each other. In short, HR professionals need the ability to think and measure in terms of systems. Of course, more research and application is needed before it will become the accepted way for measuring the HR professional's value and contribution.

Biographical Sketches

***Jay J. Jamrog** is the executive director of the Human Resource Institute and distinguished lecturer at The University of Tampa. As a futurist, he has devoted the past 20 years to identifying and analyzing the major issues and trends affecting the management of people in organizations. Jay is the associate articles editor for the "building a strategic HR function" key knowledge area of* Human Resource Planning, *has had articles published in major business magazines, and is frequently quoted in business publications and newspapers. He often collaborates with, and speaks before, other organizations and associations (e.g., HRPS, SHRM, The Mayflower Group, The Conference Board, ASTD, ABA, AGA, NEDA) on major research topics related to the future of people management. Prior to joining HRI in 1982, Jay held numerous management positions, including vice president of purchasing for a large import/export wholesaler. He has an MBA and taught labor relations in the School of Management at the University of Massachusetts.*

***Miles H. Overholt**, PhD, is the director of systems measurement at the Human Resource Institute. His research expertise is in organizational design, change, and behavior. He is the author of* Building Flexible Organizations: A People-Centered Approach *and has written numerous articles on change processes. He is also a lead researcher on a comparative organization project on alignment, congruency, employee behavior, and organizational performance. He is the co-developer of the* Organizational Flexibility Profile® *and the* Organization Behavior Database *and the author of several copyrighted instruments for assessing organizational culture. Additionally, Miles is a practicing psychotherapist, hypnotherapist, and family therapist. His undergraduate degree is from Lafayette College, and he earned his doctorate at the University of Pennsylvania.*

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