HR strategy and competitive advantage in the service sector

Peter Boxall, University of Auckland
Human Resource Management Journal, Vol 13 No 3, 2003, pages 5-20

While taking its cue from studies of high-performance work systems in manufacturing, this article examines theory and research on the potential for HR advantage in the service sector, building directly on recent studies of market segmentation and HR strategy in the sector. The article uses these studies, along with strategic management theory, to put forward a new typology of market characteristics, competitive dynamics and HR strategy in services. Three broad types of competition, ranging from mass market to knowledge-intensive services, are identified. This framework helps the article to explore the issue of whether competitive differentiation through human resources is possible only in high-skill areas such as professional services. It argues that opportunities for HR advantage are broader; they exist where quality and/or knowledge are important in competitive strategy. However, seeing the opportunity is not the same as achieving the result. Service firms that identify and pursue these opportunities face the problems of building and maintaining barriers to imitation, and of managing the 'politics of appropriation'.
Contact: Peter Boxall, Department of Management and Employment Relations, University of Auckland, Private Bag 92019, Auckland, New Zealand. Email: p.boxall@auckland.ac.nz

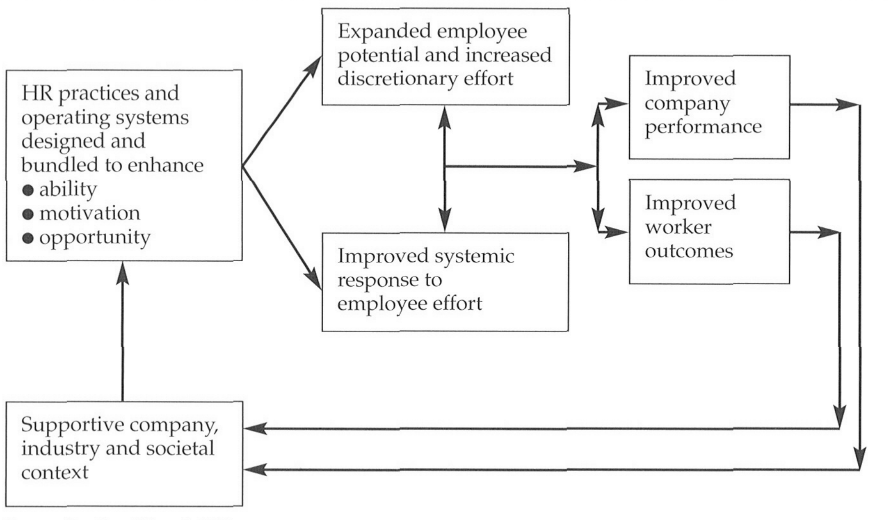
One of the most important developments in the literature linking HR strategy and business performance is the growth in studies of high-performance work systems (HPWSs). The publication of *The New American Workplace*, by Appelbaum and Batt (1994), helped to popularise this term. A subsequent book on HPWSs in US manufacturing, *Manufacturing Advantage* (Appelbaum *et al*, 2000), has built on this foundation. This book examines three US industries – steelmaking, clothing manufacture and medical electronics manufacture – and provides consistent evidence of mutually beneficial ('win-win') outcomes for firms and workers:

> Plant performance in each of the three industries examined is higher on the measures that matter to managers in those industries.[1] The opportunity-to-participate scale derived from the worker survey has a positive effect on worker outcomes as well. ... We find no support for the view that more participatory workplaces increase worker stress. Importantly, we find a significant improvement in wages associated with the extent of the opportunity to participate.

According to these authors, the work systems and employment models seen as supportive of high performance imply a mix of key practices: more rigorous selection and better training systems to increase ability levels, more comprehensive incentives (such as employee bonuses and internal career ladders) to enhance motivation and participative structures (such as self-managing teams and quality circles) that improve opportunity to contribute (Appelbaum *et al*, 2000: 26-7, 39-46, 103-4). While there is significant debate about the particular mix of high-performance practices, one of the key arguments running through the literature is that the relevant practices work much better when 'bundled' together (Ichniowski *et al*, 1996; MacDuffie, 1995). The idea is that productivity is best served by the systemic interactions among the practices. Adding only one of the practices is likely to 'have little or no effect on performance' (Ichniowski *et al*, 1997: 311). Thus, HPWSs imply a high and consistent investment in human resources in order to reap greater benefits in the productivity and possibly in the agility of the firm. A map of the commonly hypothesised linkages in HPWSs is shown in Figure 1 (Boxall and Purcell, 2003). As with the work of Appelbaum *et al* (2000), the figure relies on the 'AMO' rubric: performance is seen as a function of employee ability (A), motivation (M) and opportunity to participate or contribute (O). If practices fostering these variables are enhanced, better use will be made of employee potential and discretionary judgment. In an organisational system that is truly receptive to this kind of work reform, the argument is that outcomes should be superior for both parties.

While there is ongoing debate over the extent to which HPWSs generate mutually beneficial outcomes (*see*, for example, Godard 2001a, 2001b; Osterman, 2000; Ramsay *et al*, 2000), the evidence on the employer side is that there are certain contexts in which such systems are likely to be cost-effective. While some would argue that the key contingency in manufacturing is competitive strategy, a close reading of the evidence suggests that employers more often find HPWSs cost-effective in high-technology or capital-intensive manufacturing (Arthur, 1994; MacDuffie, 1995; Osterman, 1994; Youndt *et al*, 1996). This seems to be true irrespective of whether cost leadership or differentiation (or some mix of the two) is being pursued in competitive strategy (Boxall and Purcell, 2000, 2003). In other words, there are clearly parts of manufacturing where employers seek to complement high investment in physical capital with high investment in human capital in order to enhance total factor productivity. To understand this point, it helps to remember that a strategy of cost leadership in high technology or capital-intensive manufacturing rarely means that labour costs are in competition – a key point of contrast with the typical situation in services. On the other

FIGURE 1 *High-performance work systems: commonly hypothesised linkages*



Source: Boxall and Purcell, 2003

hand, in labour-intensive parts of manufacturing, competition is increasingly driven by plant location decisions in order to take advantage of lower labour costs, provided that quality and delivery standards are adequate. Tayloristic work systems and inexpensive HR practices are prevalent in these environments and are likely to remain so as long as they are cost-effective (Boxall and Purcell, 2003).

This article is concerned with the possibilities for HPWSs or, expressed more generally, HR advantage in services. HR advantage occurs where a firm builds and sustains competitive advantage substantially through the quality of its human capital and organisational processes (Boxall, 1996). The article examines the links between HR strategy and business performance in the service sector, asking two key questions:

- How do differences in market characteristics (including the knowledge content of services) lead to different competitive dynamics in services?
- In what circumstances can service firms build and sustain advantage through superior investments in human resources?

The article is structured as follows. It begins by reviewing the literature linking competitive positioning and HR strategy in services. The research discussed here is not an exhaustive review of the literature on work systems and employee relations in services. Rather, it selects those studies that show an awareness of market segmentation or strategic groups in services and which link these to HR strategy. The next section builds on this basis to create a new map or typology of the links from market characteristics to competitive dynamics and HR strategy in services. This analysis helps the article to explore the issue of whether competitive differentiation through human resources is possible only in high-skill areas such as professional services. The article concludes with a set of propositions on the conditions firms must meet to achieve and sustain HR advantage in services. These propositions are offered as a basis for further research, preferably of a longitudinal nature.

MARKET SEGMENTATION

It is a commonplace to observe that the service sector covers a huge range of human services, varying significantly in the nature of the work and the level of skill required (Frenkel, 2000; Frenkel *et al*, 1999). After many years of domination by manufacturing studies in HRM and industrial relations (IR), more scholars are beginning to analyse the links between competitive strategy and HR strategy in services (*eg* Batt, 2000; Keltner *et al*, 1999; Lashley, 1998; Peccei and Rosenthal, 2001).

The only way we can make any serious progress on the nature of the links between competitive and HR strategies is through frameworks which help us handle the range of service markets and the reality of segmentation within service markets. Studies of markets that allow us to identify competitive segments (on the customer side) (Keltner *et al*, 1999) and/or strategic groups (on the firm side) are very important (Bogner and Thomas, 1996; Fiegenbaum and Thomas, 1993; Gorman *et al*, 1996; Peteraf and Shanley, 1997).

An industry may have several segments/strategic groups. In each group, firms are seeking to serve a particular set of customer needs in much the same way.[2] As a result, they become significant organisations for each other; benchmarking against other members of the group has obvious benefits. In other parts of the industry, firms are seeking to serve other client groups. It is not that easy to shift strategy from one of these groups to another; mobility barriers tend to be quite significant (Tallman and Atchison, 1996).

Major studies in the HR/IR literature which explore market segments or strategic groups include Batt (2000) on call centres in US telecommunications, Eaton (2000) and

Hunter (2000) on US rest homes, Haynes and Fryer (1999, 2000) on New Zealand hotels, Rispoli (1996) on Italian hotels, Lashley (1998) on UK fast-food restaurants, and Doorewaard and Meihuizen's (2000) research on Dutch and German management consultancy firms. These studies show that there are discernible segments in each of these industries where competitive and HR strategies tend to co-vary.

Batt (2000), for example, analyses four segments in call-centre work in the US telecommunications industry. These segments vary in terms of the complexity and value of the employee-customer interaction. At the low end there are low-margin interactions of short duration, typically with predetermined scripts and with strong technological monitoring of employees. At the high end there are high-margin, low-volume interactions relying far more on employee skill and discretion and where technology is much more of an enabler than a monitor. One statistic alone is telling: at the low-margin end, operators deal with an average of 465 customers a day; in the two midrange segments they deal respectively with 100 and 64, and at the top end they deal with an average of 32 (Batt, 2000: 550). Batt finds significant differences in the contours of HR strategy across these market segments:

> Implementation of high involvement work practices varies systematically, according to the demand characteristics of the customer segment served, with the use of these systems more likely in higher value-added markets. Work practices that correlate with customer segment include the type of interaction with the customer; the extent to which technology is used as a control device versus a resource input; the skill requirements of jobs; discretion to influence work methods and procedures; and types and levels of compensation. ***Batt, 2000: 555***

Sectoral studies such as Batt's (2000) uniformly support the point that HR strategy is closely connected to competitive differentiation in services. Other compelling examples can be found in the US studies of rest homes cited earlier (Eaton, 2000; Hunter, 2000) where HR investments (in training, pay, career structures and staffing levels) are greater in firms that target higher value niches.

Lest these examples be criticised for focusing on less skilled service industries, it is worthwhile pointing out that customer differentiation can also be discerned in professional services. Doorewaard and Meihuizen's (2000) study of Dutch and German management consultancies is instructive. Here the authors discern two broad strategic types: firms oriented to efficiency and firms oriented to expertise. The former offer standard solution(s) to familiar problems in an efficient way, while the latter promote an individual professional's ability to offer new, client-specific solutions to new, unusual problems (Doorewaard and Meihuizen, 2000: 43). These are tendencies, not hard and fast categories, but they are associated with differentiation in HR strategy. Expertise-driven firms try to hire highly intelligent free spirits and retain them through challenging, high-discretion work, while those oriented to efficiency have a more bureaucratic model of HRM. Starbuck's (1992) discussion of knowledge-intensive firms can be used to add a dynamic element to this picture: management consultancies and similar firms may start up as expertise-oriented organisations. Some choose to stay small and stick with their expert culture, while others grow through routinisation and become efficiency-oriented in their production systems and HR strategy.

There ought to be more research based on longitudinal studies, but there is enough in these studies to suggest that we can do some productive theory-building at this point in time. This is the objective of this article.

MARKET CHARACTERISTICS AND COMPETITIVE DYNAMICS

Two building blocks help us to create a typology linking market characteristics, competitive dynamics and HR strategy in services. One is a typology of work systems developed by Herzenberg, Alic and Wial (1998) (cited approvingly by Batt (2000) and Frenkel *et al* (2000)). This typology is shown in Figure 2 (*overleaf*). While not recognising all complexity, it has the value of summarising four readily discernible categories of work, both in service and in manufacturing environments (Herzenberg *et al*, 1998: 41). Work systems are a critical dimension of HRM and need to be incorporated in any model of the links between HR and competitive strategies (Boxall and Purcell, 2003).

The framework developed by Herzenberg *et al* (1998) stretches from Taylorist work design to high-discretion systems, such as professional work, where Taylorism has rarely intruded. In-between are two other categories: one recognising the large amount of work which is labour-intensive, less skilled and unrationalised by management systems, and another recognising semi-autonomous work that requires midrange skills and is neither high in discretion nor highly constrained. This latter category, covering a lot of sales, clerical and associate-professional work, becomes important in the argument in this article.

The other building block is shown in Figure 3 (*overleaf*). It provides important theory from strategic management, including (but not only) the resource-based view, which is needed to understand competitive dynamics in services. The figure plots service differentiation against business outcomes. Cost leadership is one of the two main competitive strategies analysed by Porter (1985). While ensuring 'cost parity or proximity' is an issue in any strategy (Porter, 1985: 14), firms can also differentiate in various ways. Miller's research (1992: 403) concurs with Porter's view that cost leadership is one strategic option and provides evidence of three broad types of differentiation: pioneering, salesmanship and quality leadership. His research also argues that possibilities for differentiation vary across industries. Thus, we can expect to find that some service sectors offer greater niche possibilities and have more strategic groups exploiting them than others.

Figure 3 recognises variation in the degree of service differentiability and argues that differentiation doesn't necessarily lead to sustained competitive advantage. It helps to define two broad business outcomes – viability and sustained competitive advantage (Boxall and Steeneveld, 1999). Viability with normal profits is the primary goal of the firm, but the figure notes that in certain cases firms remain viable with sub-normal profits (*eg* because of family financing). Sustained competitive advantage only occurs where there is a sustained source of superior profitability, despite the best efforts of rivals to imitate or outflank it (Barney, 1991).

We should start at Quadrant C. This is the standard picture of perfect competition, as described in any basic economics textbook. In highly competitive markets (and many low-skill services fall into this category), firms need to be able to offer the relevant bundle of services at adequate quality, but costs are always in competition. Service firms in mass markets need to pay the market-clearing wage for the labour they employ, but are unlikely to pay much more than this because labour costs constitute such a significant proportion of total costs (Batt, 2000: 547). Over time, rents will be competed away and profits will tend to normalise. In this process, firms that are under-capitalised (which carry excessive financing costs) or which carry some other form of excess cost will fail (Tallman and Atchison, 1996).

In Quadrant A, first movers in mass-service markets can enjoy temporary windfalls. However, they fall back to Quadrant C, and normal profitability, as others execute good

FIGURE 2 *Herzenberg et al's (1998) typology of work systems*

Work systems	Tightly constrained	Unrationalised labour-intensive	Semi-autonomous	High-skill autonomous
Examples	Telephone operators, fast-food workers, cheque proofers	Some nurses' aides, hotel maids, domestics, long-distance truck drivers, childcare workers, clerical homeworkers	Clerical and administrative jobs with relatively broad responsibilities, low-level managers, some sales workers, UPS truck drivers	Physicians, high-level managers, laboratory technicians, electricians, engineers
Markets served	High volume, low cost; standardised quality	Low cost, low volume; often low or uneven quality	Volume and quality vary	Low volume (each job may differ); quality is often in the eye of the beholder
Task supervision	Tight	Loose	Moderate	Little
Formal education of workers	Low to moderate	Low to moderate (skill often unrecognised)	Moderate	High
On-the-job training	Limited	Some informal, unrecognised learning from other workers	Limited to moderate	Substantial

Source: Abridged from Herzenberg *et al*, 1998: 42-3

FIGURE 3 *A typology of competitive strategies and business outcomes in services*

	Low	High
Sustained competitive advantage (*ie* sustained above-average profits)	QUADRANT A 1 Premium-branded services in mass markets 2 Firms with unique cost-reduction skills in mass markets	QUADRANT B 1 Scarce, inimitable service strategies based on esoteric knowledge 2 Legally and/or physically protected service monopolies
Viability with normal or subnormal profit	QUADRANT C 1 Efficient strategies in competitive markets	QUADRANT D 1 Personal niches with lowered profit goals 2 Firms with inimitable strategies but poor appropriability

Extent of service differentiation

imitation strategies (Reed and DeFillippi, 1990; Tallman and Atchison 1996). The only firms that sustain their presence in this desirable space are those that build outstanding brand recognition or which develop unique cost-reduction skills (Bogner and Thomas, 1996; Miller, 1992; Porter, 1985). Those that dominate market share may enjoy reputational advantages in the labour market which help them become more selective than other firms employing low-skilled, highly mobile labour. Lashley's (1998) analysis suggests we might place McDonald's fast food restaurants in this category.

Quadrant B contains two stable options. One is the terrain envisaged by Barney's (1991) description of resource-based advantage. The firm is doing something rare, valuable and hard to imitate or out-flank. The classic case here is the knowledge-intensive firm, which competes through valuable but esoteric expertise (Starbuck, 1992). Starbuck's case study of the elite New York law firm, Wachtell Lipton, is a celebrated example (Starbuck, 1993). As Coff (1997, 1999) and Kamoche (1996) have pointed out, it is also important to ensure that shareholders appropriate a healthy share of these rents, not an easy thing because key value generators are often well placed to exploit their special knowledge or negotiate for themselves. This is well demonstrated in the second category, where scarce resources stem from legal or physical protections. A famous historical example concerns the early chartered companies (such as the English East India Company and the Hudson's Bay Company) which were granted monopoly privileges in the 17th century (Jones and Ville, 1996). These companies experimented with various ways (such as bonds and oaths) to curb the opportunism of managers intent on amassing personal fortunes. Principal-agent problems were the constant travelling companion of the companies' rent-seeking behaviour.

Quadrant D notes that service differentiability does not necessarily lead to superior performance. There are two categories here. Small, specialist businesses at the edge of markets can survive as long as it remains sub-economic for the dominant firms that occupy the middle ground to move out to the edges, as argued by organisational ecologists who have developed the theory of resource partitioning (Carroll and

Hannan 1995: 215-21). It is quite possible that some of these firms develop funding regimes (such as family financing) and adopt profit goals that are less demanding than would be the case in public companies. A second category involves firms in which there are sources of rent, but executives and/or other value generators capture them. This typically occurs through key executives using the special knowledge and power their positions confer to negotiate exceptional levels of remuneration and bonuses. Sometimes it is accompanied by fraud, as is graphically illustrated in several recent US cases of corporate collapse. Whether or not fraud is involved, these firms fail to deal effectively with what might be called the 'politics of appropriation'.

PREDICTIONS: COMPETITIVE DYNAMICS AND HR STRATEGY

Figures 2 and 3 help to lay the basis for Figure 4 (*opposite*), which aims to relate market characteristics in services to competitive dynamics and HR strategy. The first two columns in Figure 4 define the nature of the market: the type of knowledge used is an inherent feature of the service. Note that key variables referred to in the figure (such as differentiation and discretion) are really located on continua. To simplify things for theory-building, however, it helps to talk about three types.

The four types of work organisation referred to in Figure 2 are spread across the three categories here, largely because the 'tightly constrained' and 'unrationalised labour-intensive' systems are typically found in low-cost, mass-service markets (Type 1 in Figure 4) and, to some extent, in Type 2. Both these forms of work organisation are identifiable in service sectors, where labour costs are in stiff competition. One simply sees more attempts at Taylorism in some low-margin service sectors than in others. Employers find Taylorism useful for cost-effectiveness in some sectors, but they see no use for it in others.

Similarly, the four types of business outcome identified in Figure 3 are all incorporated into the final column of Figure 4, which outlines predictions for HR strategy. For example, both Quadrant C and A1 in Figure 3 are noted in the Type 1 category in Figure 4 and both Quadrant B1 and D2 are noted in Type 3.

Type 1: mass-service markets

In mass-service markets, such as gas stations, fast food outlets and supermarkets, key managers or franchisees have critical knowledge, but general labour uses limited, mostly generic 'know-how'. Work design here typically involves one of two types in Herzenberg *et al's* (1998) framework. Some firms adopt Taylorism, while others use unrationalised practices. In both cases, costs, including labour costs, are in competition because customers are very price sensitive. Firms do not generally pay above market-clearing wages unless persuaded to do otherwise by unions and state regulation (*see*, for example, Hunter, 2000). In their quest to survive in a cost-conscious environment, firms typically substitute labour for technology and self-service. While cost leadership and branding strategies are possible, the dynamics of cost-based competition in mass services have the effect of imposing major constraints on the HR strategies of firms. The key prediction here is that managers fit HR strategy to their cost-based competitive strategies through paying only the market-clearing wage and complying minimally with labour laws. There are very limited prospects for HR advantage, except where premium brands can be created and sustained. Apart from the latter case, firms find that investments in HPWSs are not cost-effective, as Batt (2000: 547, 555-6) argues. This is not an entirely deterministic argument (*ie* market structure determining HR strategy). It does not rule out firm-level creativity, and certainly not elements of managerial idiosyncrasy (good, bad and

FIGURE 4 *Market characteristics, competitive dynamics and HR strategy in services*

Service market type	Knowledge content of service	Typical work design	Competitive dynamics in the sector	Predictions for HR strategy in firms
Type 1 Mass-service markets (*eg* petrol stations, fast food, supermarkets)	Low. Key managers or franchisees have critical knowledge, but general labour uses limited, mostly generic 'know-how'	Low discretion. May be highly 'Taylorised' in international franchises or major chains; otherwise unrationalised, low-skill work	Cost-based except to the extent limited by unions and state regulation; substitution of labour for technology and self-service; some branding strategies possible	Firms typically fit HR strategy to their cost-driven competitive strategies through paying only the market-clearing wage and complying minimally with labour laws; very limited prospects for HR advantage, except where premium brands can be created and sustained
Type 2 A mix of mass markets and higher value-added segments (*eg* elder care, hotels, call centres)	Low-to-moderate knowledge levels; mix of skill level needed in the workforce	Traditionally low-to-moderate discretion, but potential for job enrichment and HPWSs	Mix of cost and quality-based competition; greater profit opportunities for firms that identify higher value-added segments	In mass markets, HR strategies are Type 1, but possibilities exist for HR advantage in higher value-added segments; potential problems with imitability and appropriability
Type 3 Very significantly, if not totally, differentiated markets (*eg* high-level professional services)	High knowledge intensity	High discretion – the natural home of HPWSs	Expertise and quality-based competition, but with some anchors on relative pricing; some services may be routinised and migrate back to Type 2 competition	Extensive opportunities for HR advantage in expertise-driven niches; potential problems with imitability and appropriability; use of lower cost HR strategies where expertise is routinised

indifferent) (Purcell, 1999; West and DeCastro, 2001), but it does underline the severe economic constraints when firms operate in these kinds of service market.

Type 2: mix of mass markets and higher value-added segments

The case studies cited above show that it is possible to break out of the Type 1 pattern in segments of certain service markets, such as elder care, hotels and call centres, where there is much greater variation in customer preferences and higher value-added customers can be targeted. A mix of skill levels is needed in the workforce (*eg* nurse aiding, nurses and other professionals in elder care). Jobs are traditionally low to moderate in discretion, but there is clearly potential for job enrichment (*see*, for example, Eaton 2000). Competitive dynamics, then, are based around a mix of cost and quality-based competition. The key predictions for HR strategy are twofold. In mass-service segments, HR strategies will remain Type 1, but firms can discover possibilities for HR advantage in higher value-added segments. In these segments, investments in creating HPWSs are likely to be economically justified. The existence of high skills is not the necessary condition. Skill levels are variable. It is simply necessary that there are profitable higher value segments and that it is cost-effective to invest in developing greater employee skills and higher levels of motivation to serve them.

Type 3: very significantly, if not totally, differentiated markets

In high-level, professional services and other knowledge-intensive services, work organisation has always involved high levels of employee discretion. This is the natural home of high-performance work systems in the service sector. Firms typically invest in building employee skills, enhancing motivation and providing opportunities to participate. However, following Doorewaard and Meihuizen (2000) and Starbuck (1992), there are two predictions in this model about competitive dynamics and HR strategy. Where high-level services are based on esoteric expertise (with some anchors on relative pricing), competitive strategy and HR strategy virtually merge. It seems silly to make much distinction between them. Committing to hiring certain experts (*eg* bringing them into partnership) will lead to emergent competitive strategies in their fields of expertise: they are the business. This is why it is helpful to think about competitive strategy in professional service firms in a federalist rather than top-down kind of way (Boxall and Steeneveld, 1999; Greenwood *et al*, 1990). There are extensive opportunities for HR advantage in these expertise-driven niches (admitting that firms may experience problems with appropriability). Where services become routinised (Doorewaard and Meihuizen, 2000), however, firms end up migrating back to Type 2 competition and one can expect to see greater use of lower cost HR strategies.

Barriers to imitation and the problem of appropriation

The discussion so far identifies opportunities for forms of HR advantage. However, it tends to suggest that seeing the opportunity will consistently lead to the result. This is obviously not the case. We need to push our dynamic analysis further. Management will need to foster barriers to imitation because sources of HR advantage will inevitably become subject to competition – from without and also from within. Imitative forces may set in more quickly in Type 2 competition because quality strategies are more easily imitated than those based on esoteric knowledge (Type 3) (Barney, 1991; Coff, 1999). As an aside, this has certainly been the case in automotive manufacturing, where quality is now a 'table stake' rather than a source of advantage (Leonard,1998).

External competition for rents (sources of superior profitability) implies the firm needs to foster such barriers to imitation as path-dependence, social complexity and causal ambiguity (Barney, 1991; Wright *et al*, 1994). Arguably, path dependence, or unique timing and learning, plays the primary role in creating barriers to imitation because it generates firm-specific assets and leads to social complexity and some degree of causal ambiguity (Boxall and Purcell, 2000, 2003). This argument is supported by the Tallman and Atchison (1996) model of competence-based competition in which the timely and sustained investments of innovators and fast followers in a strategic group progressively exclude others from the game. Both innovators and fast followers have good targeting and timing: other firms don't. They then need to exploit this timing with a system of resources (physical, human and organisational) that further differentiates the firm from others outside and, to some extent within, its strategic group (Tallman and Atchison, 1996: 355-7). Management skills in fostering ongoing, systemic learning must play a large role in any successful story of sustained competitive advantage (Boxall and Purcell, 2003; Leonard, 1998). Such skills need to be strongly embedded in the firm's routines and meta-routines (such as environmental sensing and strategic planning), and not solely dependent on heroic leaders, if they are to withstand imitation (Boxall, 1998; Mueller, 1996). There is thus an important role for an astutely formed HR strategy, for a blend of people-management practices and investments which helps the firm to develop innovative and agile behaviour, while not neglecting the stable harvesting of its existing operations.

Internal competition for rents (Coff, 1997, 1999; Kamoche, 1996) implies that the firm will need to negotiate a suitable appropriation regime (Kamoche and Mueller, 1998: 1033). As with the problem of external competition for rents, HRM (broadly defined) plays an important role. Governance systems in the firm, including methods of managing managers, will need to ensure that rents are fairly split between investors, managers and other value creators. Clearly, executive management should not be the sole author of these systems: management is both an asset and a liability where appropriation is concerned. Executive managers have serious bargaining power because they have oversight of the production of tacit knowledge – the very tacit knowledge that generates sustained advantage gives key managers the power to dominate appropriation (Coff, 1999). As a result, investor representatives need to play a key role in the politics of governance, but contemporary debate about executive pay shows that this is far from easy.

CONCLUSIONS

The broad argument in this article is that the match, or fit, between competitive strategy and HR strategy is greater in services than it is in manufacturing. This is because competitive strategies of cost leadership and differentiation are both likely to imply high HR investment in capital-intensive or high-tech manufacturing. A strategy of cost leadership should not be equated with wage-based competition at this end of manufacturing. Management thinking about HR strategy in manufacturing is influenced by the employee-technology interface, not simply by the firm's desired competitive position. As in any sector, it is also, of course, influenced by employee responses, and by labour markets and labour law, among other factors (Boxall, 1996).

In services, however, one learns more about the likely shape of management strategy in HRM by looking closely at what is occurring at the employee-customer interface (Batt, 2000: 542). Studies of market segments and strategic groups in services demonstrate the strong links between competitive and HR strategies. This article argues that cost-based, low-margin competition in mass services tends to drive out the possibilities for HR advantage, except where firms can fund greater HR investment out of premium branding. Where labour is plentiful, the only real constraints on this form of competition stem from effective forms of unionism and enforced regulation.

It is outside cost-based service competition that we can talk about possibilities for sustained advantage through the quality of human capital and organisational processes. The analysis here suggests that it is not simply high-level, knowledge-intensive services where the possibilities for HPWSs exist. Wherever there are important customer segments that extend beyond mass, low-cost services, there is potential for a pay-back from greater investment in human resources. Key studies on service markets such as call centres (Batt, 2000) and elder care (Eaton, 2000; Hunter, 1999) lead directly to this thesis. We ought, then, to avoid the impression that high-performance work systems are a category that is exclusive to certain elite industries. Rather, HPWSs are potentially available to a wide range of sectors. Putting the point more generally: there are work reform possibilities in many industries, where both parties might benefit or where one party might benefit while the other is not, overall, disadvantaged.

As a basis for further research, preferably of a longitudinal or history-sensitive nature, this article implies that five conditions must hold for HPWSs to be feasible in a firm operating in services.

1 **The customer proposition** A viable group of customers (an economic segment) must value some form of differentiation (*eg* higher quality of service or unique expertise). This can occur in midrange (Type 2) as well as knowledge-intensive services (Type 3). It can also occur in mass services (Type 1), where a firm creates and sustains premium branding, but the nature of Type 1 competition is such that this is much less likely.

2 **The HR proposition** Skills of workers do not have to be absolutely high, but the increments in know-how and in motivation that support the competitive differentiation must be a) achievable and b) economically worthwhile (cost-effective).

3 **The non-HR proposition** The business must have sufficient financial capital to support an HR premium (a higher level of investment in selectivity, training, pay, career structures *etc*).

4 **The cognitive and political proposition** Management needs the insight and political will to identify and meet the customer proposition through the right mix of HR and non-HR investment.

5 **The inimitability and appropriability proposition** In order to sustain and exploit a source of HR advantage, management will need to foster barriers to imitation, particularly those associated with path dependence: astute targeting and timing, and ongoing, systemic learning. The firm will also need to effectively manage the politics of appropriation.

The argument, then, is that the potential for higher value market segmentation, not absolutely high skill levels, is decisive in creating a rationale for HPWSs – or space for HR advantage – in services. This is the point expressed in propositions one and two. Proposition three is needed because human and non-human resources are bundled in the firm (Penrose, 1959; Mueller, 1996): greater financial capital is needed to fund an HR premium. The fourth proposition is added because firms are managed entities, where cognitive limits and internal politics can always get in the way of a good idea (Simon, 1947; Child, 1972, 1997). Finally, not only must management be able to identify and act concertedly on the HR opportunity, but proposition five reminds us that management will also need to foster barriers to imitation and the firm will need to develop a suitable appropriation regime (Kamoche and Mueller, 1998). These are critical elements in any dynamic explanation. In other words, sources of HR advantage become subject to competition from without and, not least, from within (Coff, 1999). Management has a vital role to play, particularly in decisions about the targeting and timing of strategies and the related bundling of resources, and in the orchestration of ongoing, systemic learning. However, the centrality of management in this process also creates significant agency risks which, it goes without saying, should not be managed exclusively by executives.

All of this implies a critical role for astutely formed HR strategy. It helps to think about this role on two levels. On the first level, there is clearly a strategic question about which mix of HR practices and investments constitute an HPWS in a particular firm and sector. The current literature in the area is obsessed with this question, but it is typically approached in a static manner. There is a second, more dynamic level on which HR strategy should also play a role. This level is concerned with shaping the managerial and broader context in which HPWSs are conceived, evolved and defended.

Acknowledgements

I am grateful to two anonymous reviewers for helpful suggestions.

Notes

1 For example, 'machine uptime' in the steel industry and 'sewing throughput time' in the apparel manufacturing industry.

2 For the sake of the theoretical argument and for ease of discussion, firms are assumed to be single business units. In reality, firms are often more complex. They may be competing in various industries and strategic groups.

REFERENCES

Appelbaum, E. and Batt, R. (1994). *The New American Workplace*, Ithaca, New York: ILR Press.

Appelbaum, E., Bailey, T. and Berg, P. (2000). *Manufacturing Advantage: Why High-Performance Systems Pay Off*, Ithaca: ILR Press.

Arthur, J. (1994). 'Effects of human resource systems on manufacturing performance and turnover'. *Academy of Management Journal*, 37: 3, 670-87.

Barney, J. (1991). 'Firm resources and sustained competitive advantage'. *Journal of Management*, 17: 1, 99-120.

Batt, R. (2000). 'Strategic segmentation in front-line services: matching customers, employees and human resource systems'. *International Journal of Human Resource Management*, 11: 3, 540-61.

Bogner, W. and Thomas, H. (1996). 'From skills to competences: the "play-out" of resource bundles across bundles' in *Dynamics of Competence-Based Competition*. R. Sanchez, A. Heene and H. Thomas (eds). Oxford: Elsevier.

Boxall, P. (1996). 'The strategic HRM debate and the resource-based view of the firm'. *Human Resource Management Journal*, 6: 3, 59-75.

Boxall, P. (1998). 'Achieving competitive advantage through human resource strategy: towards a theory of industry dynamics'. *Human Resource Management Review*, 8: 3, 265-288.

Boxall, P. and Purcell, J. (2000). 'Strategic human resource management: where have we come from and where should we be going?' *International Journal of Management Reviews*, 2: 2, 183-203.

Boxall, P. and Purcell, J. (2003). *Strategy and Human Resource Management*, Basingstoke and New York: Palgrave Macmillan.

Boxall, P. and Steeneveld, M. (1999). 'Human resource strategy and competitive advantage: a longitudinal study of engineering consultancies'. *Journal of Management Studies*, 36: 4, 443-63.

Carroll, G.R. and Hannan, M.T. (eds) (1995). *Organizations in Industry: Strategy, Structure and Selection*, New York and Oxford: Oxford University Press.

Child, J. (1972). 'Organisational structure, environment and performance: the role of strategic choice'. *Sociology* 6: 3, 1-22.

Child, J. (1997). 'Strategic choice in the analysis of action, structure, organizations and environment: retrospect and prospect'. *Organization Studies*, 18: 1, 43-76.

Coff. R. (1997). 'Human assets and management dilemmas: coping with hazards on the road to resource-based theory'. *Academy of Management Review*, 22: 2, 374-402.

Coff, R. (1999). 'When competitive advantage doesn't lead to performance: the resource-based view and stakeholder bargaining power'. *Organization Science*, 10: 2, 119-33.

Doorewaard, H. and Meihuizen, H. (2000). 'Strategic performance options in professional service organisations'. *Human Resource Management Journal*, 10: 2, 39-57.

Eaton, S. (2000). 'Beyond unloving care: linking human resource management and patient care quality in nursing homes'. *International Journal of Human Resource Management*, 11: 3, 591-616.

Fiegenbaum, A. and Thomas, H. (1993). 'Industry and strategic group dynamics: competitive strategy in the insurance industry'. *Journal of Management Studies*, 30: 1, 69-105.

Frenkel, S. (2000). 'Introduction: service work and its implications for HRM'. *International Journal of Human Resource Management*, 11: 3, 469-76.

Frenkel, S., Korczynski, M., Shire, K. and Tam, M. (1999). *On the Front Line: Organization of Work in the Information Economy*, Ithaca: ILR Press.

Godard, J. (2001a). 'Beyond the high-performance paradigm? An analysis of variation in Canadian managerial perceptions of reform programme effectiveness'. *British Journal of Industrial Relations*, 39: 1, 25-52.

Godard, J. (2001b). 'High-performance and the transformation of work? The implications of alternative work practices for the experience and outcomes of work'. *Industrial and Labor Relations Review*, 54: 4, 776-805.

Gorman, P., Thomas, H. and Sanchez, R. (1996). 'Industry dynamics in competence-based competition' in *Dynamics of Competence-Based Competition*. R. Sanchez, A. Heene and H. Thomas (eds). Oxford: Elsevier.

Greenwood, R., Hinings, C. and Brown, J. (1990). '"P2-form" strategic management: corporate practices in professional partnerships'. *Academy of Management Journal*, 33: 4, 725-55.

Haynes, P. and Fryer, G. (1999). 'Changing patterns of HRM and employment relations in New Zealand: the large hotel industry'. *Asia Pacific Journal of Human Resources*, 37: 2, 33-43.

Haynes, P. and Fryer, G. (2000). 'Human resources, service quality and performance: a case study'. *International Journal of Contemporary Hospitality Management*, 12: 4, 240-48.

Herzenberg, S., Alic, J. and Wial, H. (1998). *New Rules for a New Economy: Employment and Opportunity in Postindustrial America*, Ithaca: ILR Press.

Hunter, L. (2000). 'What determines job quality in nursing homes?' *Industrial and Labor Relations Review*, 53: 3, 463-81.

Ichniowski, C., Kochan, T., Levine, D., Olson, C. and Strauss, G. (1996). 'What works at work: overview and assessment'. *Industrial Relations*, 35: 3, 299-333.

Ichniowski, C., Shaw, K. and Prennushi, G. (1997). 'The effects of human resource management practices on productivity: a study of steel finishing lines'. *American Economic Review*, 87: 3, 291-313.

Jones, S. and Ville, S. (1996). 'Efficient transactors or rent-seeking monopolists? The rationale for early chartered trading companies'. *Journal of Economic History*, 56: 4, 898-915.

Kamoche, K. (1996). 'Strategic human resource management within a resource-capability view of the firm'. *Journal of Management Studies*, 33: 2, 213-33.

Kamoche, K. and Mueller, F. (1998). 'Human resource management and the appropriation-learning perspective'. *Human Relations*, 51: 8, 1033-1060.

Keltner, B., Finegold, D., Mason, G. and Wagner, K. (1999). 'Market segmentation strategies and service sector productivity'. *California Management Review*, 41: 4, 84-102.

Lashley, C. (1998). 'Matching the management of human resources to service operations'. *International Journal of Contemporary Hospitality Management*, 10: 1, 24-33.

Leonard, D. (1998). *Wellsprings of Knowledge: Building and Sustaining the Sources of Innovation*, Boston: Harvard Business School Press.

MacDuffie, J.P. (1995). 'Human resource bundles and manufacturing performance: organizational logic and flexible production systems in the world auto industry'. *Industrial and Labor Relations Review*, 48: 2, 197-221.

Miller, D. (1992). 'Generic strategies; classification, combination and context'. *Advances in Strategic Management*, 8, 391-408.

Mueller, F. (1996). 'Human resources as strategic assets; an evolutionary resource-based theory'. *Journal of Management Studies*, 33: 6, 757-785.

Osterman, P. (1994). 'How common is workplace transformation and who adopts it?' *Industrial and Labor Relations Review*, 47: 2, 173-188.

Osterman, P. (2000). 'Work reorganization in an era of restructuring: trends in diffusion and effects on employee welfare'. *Industrial and Labor Relations Review*, 53: 2, 179-196.

Peccei, R. and Rosenthal, P. (2001). 'Delivering customer-oriented behaviour through empowerment: an empirical test of HRM assumptions'. *Journal of Management Studies*, 38: 6, 831-57.

Penrose, E. (1959). *The Theory of the Growth of the Firm*, Oxford: Blackwell.

Peteraf, M. and Shanley, M. (1997). 'Getting to know you: a theory of strategic group identity'. *Strategic Management Journal*, 18: S, 165-186.

Porter, M. (1985). *Competitive Advantage: Creating and Sustaining Superior Performance*, New York: Free Press.

Purcell, J. (1999). 'High commitment management and the link with contingent workers: implications for strategic human resource management' in *Research in Personnel and Human Resources Management (Supplement 4: Strategic Human Resources Management in the Twenty-First Century)*. P. Wright, L. Dyer, J. Boudreau and G. Milkovich (eds). Stamford, CT and London: JAI Press.

Ramsay, H., Scholarios, D. and Harley, B. (2000). 'Employees and high-performance work systems: testing inside the black box'. *British Journal of Industrial Relations*, 38: 4, 501-31.

Reed, R. and DeFillippi, R. (1990). 'Causal ambiguity, barriers to imitation, and sustainable competitive advantage'. *Academy of Management Review*, 15: 1, 88-102.

Rispoli, M. (1996). 'Competitive analysis and competence-based strategies in the hotel industry' in *Dynamics of Competence-Based Competition*. R. Sanchez, A. Heene and H. Thomas (eds). Oxford: Elsevier.

Simon, H.A. (1947). *Administrative Behavior*, New York: Free Press.

Starbuck, W. (1992). 'Learning by knowledge-intensive firms'. *Journal of Management Studies*, 29: 6, 713-40.
Starbuck, W. (1993). 'Keeping a butterfly and an elephant in a house of cards: the elements of exceptional success'. *Journal of Management Studies*, 30: 6, 885-921.
Tallman, S. and Atchison, D. (1996). 'Competence-based competition and the evolution of strategic configurations' in *Dynamics of Competence-Based Competition*. R. Sanchez, A. Heene and H. Thomas (eds). Oxford: Elsevier.
West, G. and DeCastro, J. (2001). 'The Achilles heel of firm strategy: resource weaknesses and distinctive inadequacies'. *Journal of Management Studies*, 38: 3, 417-42.
Wright, P., McMahan, G. and McWilliams, A. (1994). 'Human resources and sustained competitive advantage: a resource-based perspective'. *International Journal of Human Resource Management*, 5: 2, 301-326.
Youndt, M., Snell, S., Dean, J. and Lepak, D. (1996). 'Human resource management, manufacturing strategy and firm performance'. *Academy of Management Journal*, 39: 4, 836-66.