

## Strategic Human Resource Management and its Impact on Organizational Performance

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### Abstract

*HRM represents a new concept of and approach to performing personnel functions. It still requires the performance of those personnel functions that have evolved over the years in response to emerging needs. However, instead of treating these functions as separate and distinct, HRM considers them interrelated parts of a management system that must be integrated closely with strategic organizational planning.*

*Human resources are one important source of competitive advantage. Human resource systems can contribute to sustained competitive advantage through facilitating the development of competencies that are firm specific. Strategic human resource management concerns with the creation of a linkage between the overall strategic aims of business and the human resource strategy and implementation. The published research generally reports positive statistical relationships between the greater adoption of HR practices and business performance. The causal linkage between HR and organizational performance will enable the HR managers to design programs that will bring forth better operational results to attain higher organizational performance. In this paper, after emphasizing that the human resources are an important source of competitive advantage, strategic human resource management is defined. Through specific examples from academic research regarding the impact of strategic human resource management practices on organizational performance, the conclusion is that the way an organization manages its human resources has a significant relationship with the organization's performance.*

**Keywords:** *human resources, SHRM impacts, organizational performance, strategic role, competitive advantage*

**JEL Classification:** M3

### 1. Introduction

Economic environment is changing rapidly and this change is characterized by such phenomena as the globalization, changing customer and investor demands, ever-increasing product-market competition. To compete successfully in these environment

organizations continually need to improve their performance by reducing costs, innovating products and processes and improving quality, productivity and speed to market.

The people who make up an organization -human resources- are considered to be one of the most important resources of today's firms. People and how they are managed are becoming more important because many other sources of competitive success are less powerful than they used to. Recognizing that the basis for competitive advantage has changed is essential to develop a different frame of reference for considering issues of human resource management and strategy. Traditional sources of success such as product and process technology, protected markets, economies of scale, etc. can still provide competitive leverage but an organization's human resources are more vital for its sustainability.

Parallel to the understanding those human resources are vital for an organization; human resource management function is also going up in organizational hierarchy. Human resource management aims to ensure that the organization obtains and retains the skilled, committed and well-motivated workforce it needs. This means taking steps to assess and satisfy future people needs and to enhance and develop the inherent capacities of people - their contributions, potential and employability - by providing learning and continuous development opportunities. It involves the operation of recruitment and selection procedures, management development and training activities linked to the needs of the business.

Strategic human resource management (SHRM) represents a relatively new transformation in the field of human resource management. SHRM is concerned with the role human resource management systems play in firm performance, particularly focusing on the alignment of human resources as a means of gaining competitive advantage. Organizations are becoming aware that successful human resource policies and practices may increase performance in different areas such as productivity, quality and financial performance.

## **2. Human resources as a source of competitive advantage**

The concept of competitive advantage was formulated by Michael Porter. Competitive advantage, Porter asserts, arises out of a firm creating value for its customers. Porter emphasized the importance of differentiation, which consists of offering a product or service 'that is perceived industry-wide as being unique', and focus - seeing a particular buyer group or product market 'more effectively or efficiently than competitors who compete more broadly'. He then developed his well-known framework of three generic strategies, -cost leadership, differentiation, focus- that organizations can use to gain competitive advantage. Porter's widely accepted view suggests that the industry - environmental determinants- affects a firm's performance. Resource-based view, on the other hand, asserts that the basis for a competitive advantage of a firm lies primarily in the application of the bundle of valuable resources at the firm's disposal. Competitive advantage, according to this view differs from the environmentally focused strategic management paradigm in that its emphasis is on the links between the internal resources of the firm, its strategy and its performance.

The resource-based view suggests that human resource systems can contribute to sustained competitive advantage through facilitating the development of competencies that

are firm specific. The sustained superior performance of many companies has been attributed to unique capabilities for managing human resources to gain competitive advantage. Conversely, to the extent that HR systems inhibit the mobilization of new competencies and/or destroy existing competencies, they may contribute to organizational vulnerability and competitive disadvantage. In the closing years of the twentieth century, management has come to accept that people, not products, markets, cash, buildings, or equipment, are the critical differentiators of a business enterprise. All the assets of an organization, other than people, are inert. They are passive resources that require human application to generate value. The key to sustaining a Profitable company or a healthy economy is the productivity of the workforce.

What is important to recognize is why success through human resources can be sustained and cannot readily be imitated by competitors. The reason is that the success that comes from managing people effectively is often not as visible or transparent as to its source. Culture, how people are managed, and the effects of this on their behavior and skills are sometimes seen as the "soft" side of business, occasionally dismissed. Even when they are not dismissed, it is often hard to comprehend the dynamics of a particular company and how it operates because the way people are managed often fits together in a system. It is easy to copy one thing but much more difficult to copy numerous things. HRM needs to achieve the following strategic goals in order for the company to gain and sustain competitive advantage:

- to invest in people through the introduction and encouragement of learning processes designed to increase capability and align skills to organizational needs;
- to ensure that the organization identifies the knowledge required to meet its goals and satisfy its customers and takes steps to acquire and develop its intellectual capital;
- to define the behaviors required for organizational success and ensure that these behaviors are encouraged, valued and rewarded;
- to encourage people to engage wholeheartedly in the work they do for the organization;
- to gain the commitment of people to the organization's mission and values.

To achieve these goals it is necessary to understand the linkage between HRM and business strategy.

### **3. The strategic role of human resource management**

The human resource management function has consistently faced a battle in justifying its position in organizations. At good times when there are enough budgets, firms easily justify expenditures on training, staffing, rewards and employee involvement systems, but when faced with financial difficulties, such HR systems get the earliest cutbacks.

The advent of the subfield of strategic human resource management (SHRM), devoted to exploring HR's role in supporting business strategy, provided one opportunity for demonstrating its value to the firm. The birth of the field of strategic human resource management can be dated back to 1984, when Devanna, Fombrun and Tichy extensively explored the link between business strategy and human resources.

HRM discipline has witnessed a great deal of change over the past 25 years. These changes represent two major transformations. The first is the transformation from being the field of personnel management to being the field of human resource management. The second is the transformation from being the field of human resource management to being the field of strategic human resource management. The first transformation incorporated helped the recognition that people are an important asset in organizations and can be managed systematically. The second transformation has built on the proceeding knowledge base of the discipline. This transformation is based upon the recognition that, in addition to coordinating human resource policies and practices with each other, they need to be linked with the needs of the organization. Given that these needs are reflected in the strategies of the firm, this transformation of "human resource management" came to be known as "strategic human resource management".

Strategic human resource management is based upon the recognition that organizations can be more effective if their human resources are managed with human resource policies and practices that deliver the right number of people with the appropriate behaviors, the needed competencies and the necessary level of motivation to the organization.

To put it another way, strategic human resource management is "the creation of linkage or integration between the overall strategic aims of business and the human resource strategy and implementation. In principle, the processes and people within the company are managed in such a way as to foster the aims of the business strategy and create an integrated approach to managing the various human resource functions, such as selection, training and reward so that they complement each other".

Strategic human resource management may bring a number of benefits to the organization:

- Contributing to the goal accomplishment and the survival of the company,
- Supporting and successfully implementing business strategies of the company,
- Creating and maintaining a competitive advantage for the company,
- Improving the responsiveness and innovation potential of the company,
- Increasing the number of feasible strategic options available to the company,
- Participating in strategic planning and influencing the strategic direction of the company as an equally entitled member of top management,
- Improving cooperation between the HRM department and line managers.

SHRM's spreading popularity owes much to the promise of greater organizational effectiveness achievable, through the development of internally consistent bundles of human resource strategies which are properly linked to business strategies.

Researchers in the field of SHRM have increasingly relied on the resource-based view of the firm to explain the role of human resource practices in firm performance. Resource based view of strategy is that the strategic capability of a firm depends on its resource capability, especially its distinctive resources. Indeed, theoretical research on SHRM has suggested that systems of HR practices may lead to higher firm performance and be sources of sustained competitive advantage because these systems of practices are often unique, causally ambiguous, and difficult to imitate. HR practices can enhance firm performance when they are internally aligned with one another to manage employees in a

manner that leads to competitive advantage. HR practices can create value for a firm when the individual practices are aligned to develop critical resources or competencies.

#### 4. How SHRM impacts on organizational performance

Many organizations face a volatile market situation. In order to create and sustain competitive advantage in this type of environment, organizations must continually improve their business performance. Increasingly, organizations are recognizing the potential of their human resources as a source of sustained competitive advantage. Linked to this, more and more organizations are relying on measurement approaches, such as workforce scorecards, in order to gain insight into how the human resources in their organization add value.

The increasing interest in measurement is further stimulated by a growing number of studies that show a positive relationship between human resource management and organizational performance. The relationship between HRM and firm performance has been a hotly debated topic over the last two decades, with the great bulk of the primary scientific research coming from the USA and, to a lesser extent, the United Kingdom. Both organizations and academics are striving to prove that HRM has a positive impact on bottom line productivity. The published research generally reports positive statistical relationships between the greater adoption of HR practices and business performance.

In a world in which financial results are measured, a failure to measure human resource policy and practice implementation dooms this to second-class status, oversight, neglect, and potential failure. The feedback from the measurements is essential to refine and further develop implementation ideas as well as to learn how well the practices are actually achieving their intended results.

The assumption underpinning the practice of HRM is that people are the organization's key resource and organizational performance largely depends on them. If, therefore, an appropriate range of HR policies and processes is developed and implemented effectively, then HR will make a substantial impact on firm performance. Much of the research over the last two decades has attempted to answer two basic questions: 'Do HR practices make a positive impact on organizational performance?'; 'If so, how is the impact achieved?' The second question is the more important one. It is not enough to justify HRM by proving that it is a good thing. What counts is what can be done to ensure that it is a good thing.

Although there are various stakeholders in an organization, the chief strategic goal of any business is higher financial performance or maximization of wealth for the shareholders. Financial performance of an organization depends to a large extent on effective operational performance. The operational performance of an organization is a function of people, process and technology. For effective interaction of people with technology and process, the people in the organization have to be competent enough, with the required knowledge, skill and abilities. Competence of the individual is an important factor that decides operational effectiveness in terms of providing quality products and services within a short time. HRM practices such as selection, training, work environment and performance appraisal may enhance the competence of employees for higher performance.

Obviously, human resources rarely has a direct effect on firm performance. This is particularly true when the business logic of HR's effect requires that human resources drive firm performance through its contribution to effective strategy execution. HR professionals (and line managers) need to recognize that effective strategy execution is the basis of shareholder value and that effective strategy execution is a system of intermediate outcomes. Thinking like a strategy manager means recognizing the importance of the causal relationships between HR decisions and these intermediate outcomes that ultimately drive strategic success in organizations. The practice areas covered by HR strategies that impact on performance are summarized in Table 1.

Table 1.

**HR Impacts Organizational Performance**

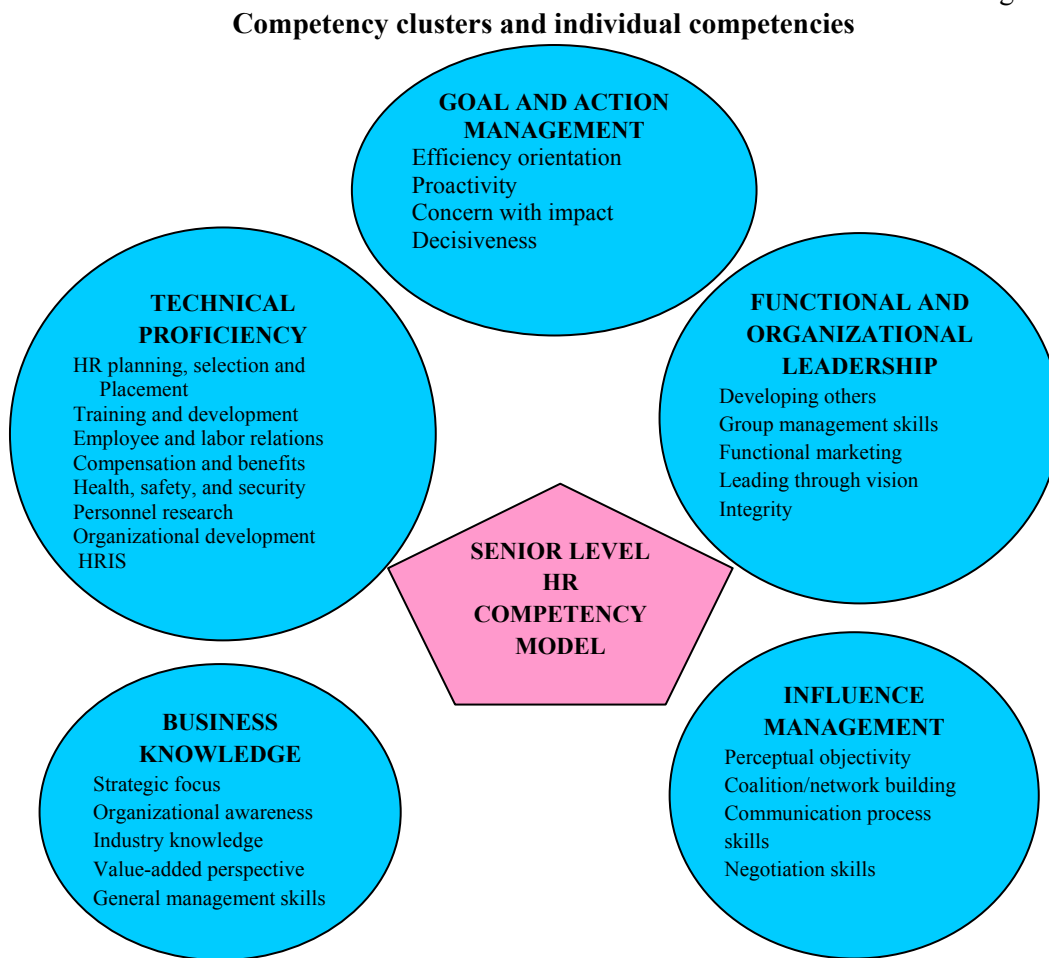
<b>HR practice area</b>	<b>How It impacts</b>
Attracting, developing and retaining high-quality people	Matches people to the strategic and operational needs of the organization. Provides for the acquisition, development and retention of talented employees who can deliver superior performance, productivity, flexibility, innovation and high levels of personal customer service and who 'fit' the culture and the strategic requirements of the organization.
Talent management	Wins 'war for talent' by ensuring that the talented and well-motivated people required by the organization to meet present and future needs are available.
Working environment -core values, leadership, work- life balance, managing diversity, secure employment	Develops 'the big idea', i.e. a clear vision and a set of integrated values. Makes the organization 'a Great place to work'.
Job and work design	Provides individuals with stimulating and interesting work and gives them the autonomy and flexibility to perform their jobs well. Enhances job satisfaction and flexibility, which encourages high performance and productivity
Learning and development	Enlarges the skill base and develops the levels of competence required in the workforce. Encourages discretionary learning, which happens when individuals actively seek to acquire the knowledge and skills that promote the organization's objectives. Develops a climate of learning - a growth medium in which self-managed learning as well as coaching, mentoring and training flourish.
Managing knowledge and intellectual capital	Focuses on both organizational and individual learning and on providing learning opportunities and opportunities to share knowledge in a systematic way. Ensures that vital stocks of knowledge are retained and deals with improving the flow of knowledge, information and learning within the organization.
Increasing motivation, commitment and role engagement	Encourages people to identify themselves with and act upon the core values of the organization and willingly to contribute to the achievement of organizational goals. Develops a climate of cooperation and trust, clarifying the psychological contract.
High-performance management	Develops a performance culture that encourages high performance in such areas as productivity, quality, levels of customer service, growth, profits and, ultimately, the delivery of increased shareholder value. Empowers employees to exhibit the discretionary behaviors most closely associated with higher business performance such as risk taking, innovation, knowledge sharing and establishing trust between managers and subordinates.
Reward management	Develops motivation, commitment, job engagement and discretionary behavior by valuing and rewarding people in accordance with their contribution.

(Source: Michael Armstrong (2006). *Strategic Human Resource Management: A Guide to Action*. Kogan Page. London. p. 77-78)



Figure 1. Represent the competency clusters and individual competencies

Figure 1.



## 5. Conclusion

Since it is clearly understood from academic research that human resources are a source of sustained competitive advantage, while, traditionally, the costs associated with the development of HR strategy have been regarded as an operating expense, these costs would be better considered as an investment in capital assets.

The way an organization manages its HR has a significant relationship with the organization's results, a revelation that supports the resource-based view, where business competitiveness is related, at least in part, to the investments in company specific assets. Although the published research generally reports positive statistical relationships between

the greater adoption of HR practices and business performance, it should also be kept in mind that many other factors besides HR practices could influence organizational performance. Also, it is possible that there are complex relationships between HR practices and other resources of the firm.

The causal linkage between HR and organizational performance will enable the HR managers to design programs that will bring forth better operational results to attain higher organizational performance. The focus of the HR management should be to understand organizational performance processes and design HR practices that influence process and outcome variables.

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