

# Balanced Scorecard

INSIGHT, EXPERIENCE &amp; IDEAS FOR STRATEGY-FOCUSED ORGANIZATIONS

REPORT



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## Managing the Development of Human Capital

by David P. Norton

In the last issue of *BSR*, we introduced the results of the Human Resource Action Working Group, focusing on approaches to describe and measure the impact of human capital on organizational strategy — like the HRAWG's newly developed "Human Capital Readiness Report." Here, we will explore the second outcome of HRAWG: programs to better manage the development of human capital, including the design of HR organization Balanced Scorecards.

It's become our mantra: "the starting point to executing strategy is the ability to describe it." The Human Resource Action Working Group's Human Capital Readiness Report identifies the requirements of human capital that support strategy. Developed jointly by HR and line executives, the report builds a shared understanding of the strategy — a prerequisite for a successful strategy and the foundation on which HR organizations can become true strategic partners.

### ON Balance

#### PART TWO OF A SERIES

However, devising the measures is only the beginning; they must be linked to — and change — the way organizations are managed. This is no small challenge, when you consider that:

- 60% of organizations do not link strategy to budgeting
- 70% of organizations do not link middle management incentives to strategy
- 85% of executive teams spend less than one hour per month discussing strategy
- 95% of the typical workforce do not understand their organization's strategy
- 90% of organizations fail to execute their strategies

HR organizations are no different in these respects than any other organization. Our surveys indicate that 80% of them lack a strategic planning process by which to align their spending programs with enterprise strategy. If 85% of organizational value is indeed based on intangible assets like human capital, these management practices are clearly unacceptable. By developing a strategic program for measuring and managing human capital, HR executives have the opportunity to spearhead the development of better strategic management.

The Balanced Scorecard has proven to be a useful tool for managing an entity as complex as the HR organization. Before constructing one, however, it's important to understand the dual role that the scorecard plays. HR does not stand alone; it's obviously part of the broader organization. It creates value by helping others create value. This is frequently a frustration for HR teams that are under pressure to justify the value of HR investments. That's where the Human Capital Readiness Report comes into play. By improving the readiness of its human capital, HR enhances the ability of the

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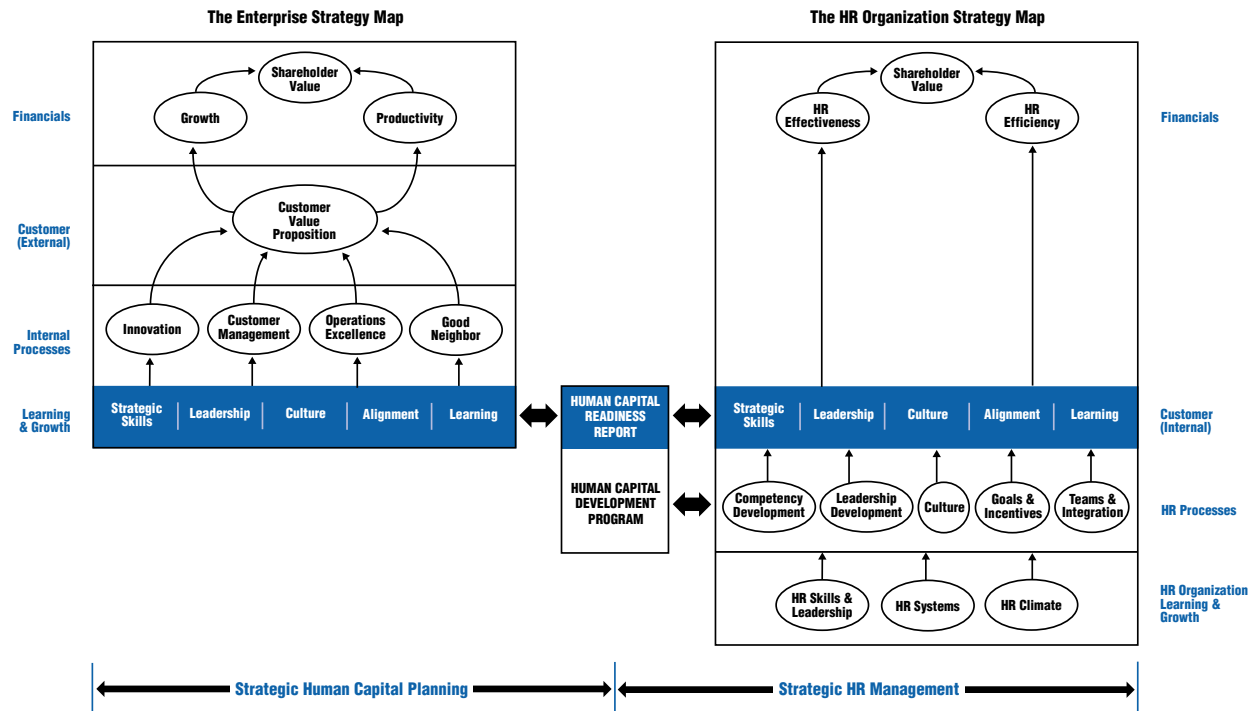
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**Figure 1. Linking the HR Organization to Enterprise Strategy**



organization to execute its strategy. *Figure 1* shows how the Readiness Report provides the basis for building a Human Capital Development Program, which in turn becomes the foundation of the HR strategy and the HR scorecard. These instruments provide the strategic linkage between HR and the enterprise.

competency?). The result of this activity will be a Human Capital Development Program. As illustrated in *Figure 2*, this program ensures alignment between HR investments and the enterprise strategy. In effect, it serves as the contract for services and expected results between HR and the end-user. It also defines a second tier

of measures, associated with HR programs, that are the true “lead indicators” of strategy. In addition, it allows the various departments within HR to share a common, integrated plan for supporting the end-users which is rooted in the strategy of the enterprise.

## Build a Human Capital Development Program

The Human Capital Readiness Report describes the objectives, measures, and targets which must be achieved to support the overall enterprise strategy. The programs required to support these objectives and their targets generally fall within the responsibility of the HR organization. Each functional group within HR (like recruiting) should review these objectives to determine which individual programs will be used to support the plan. HR should work as an integrated team in developing the plan, making tradeoffs about which programs will be most cost effective in supporting the strategy (e.g., should you use training, recruiting, or knowledge sharing to develop a

## Balanced Scorecard Report

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The strategy of Alterra Health Care Corporation, an operator of managed care facilities for the elderly, called for pushing responsibility to the lower levels of the organization. “Every level makes a difference” was the company’s objective. The Human Capital Readiness Report identified a strategic measure, “number of approvals needed,” as the specific indicator. As part of its Leadership Development Program, Alterra designed a mentoring initiative to build the culture of trust and innovation required at all levels. A second element of Alterra’s human capital strategy was to “encourage and reward empowerment” at all levels within the organization. The measure selected was “incentive pay for new ideas.” Two initiatives were identified for priority development: a revised benefits program, with funding for good ideas; and a quality assurance program to train staff in identifying opportunities.

Thus, the Human Capital Development Program provides a roadmap of the support the HR organization will provide to make strategy happen.

## Develop a Balanced Scorecard for the HR Organization

Figure 1 illustrates how Balanced Scorecards of both the enterprise and the HR organization can be linked to achieve perfect organizational alignment. The impact of human capital on enterprise strategy is reflected in the Learning & Growth section of the enterprise scorecard. The Human Capital Readiness Report describes this and the HC Development Program defines the programs that HR will provide to support the strategy. HR must view the enterprise as its customer, and the elements of the HC Development Program as its customer requirements. This, then, becomes the Customer perspective of the HR Balanced Scorecard. Having clearly defined the Customer strategy, the HR organization can then define the internal HR processes required to support the strategy, along with the requisite skills, climate, and information systems. By treating the Human Capital Readiness Report as the HR Customer objective, all of the activities of the HR organization will be in alignment with the strategic priorities of the enterprise.

Figure 3 illustrates the strategy map of the HR organization at Bonneville Power Authority (BPA), a federally-operated power utility in the Pacific Northwest. Note that the Customer section of its scorecard (referred to as “Stakeholders/BPA Workforce”) identifies the four themes from its Human Capital Readiness Report: (1) Leadership, (2) Talented Workers, (3) Motivated Workers, and (4) Positive Work Environment. The Internal Systems and Processes section of the scorecard identifies fourteen initiatives taken to support this strategy. The strategy for “Developing Talented Workers” (Stakeholder Objectives S4 and S5) is supported by five of these Internal HR Process initiatives:

- (I4) Improving the performance management process
- (I8) Encouraging best practice knowledge-sharing
- (I9) Using the merit system more effectively for job placement
- (I10) Establishing cutting-edge employee development
- (I11) Improving the linkage of the recruiting process to meet talent requirements

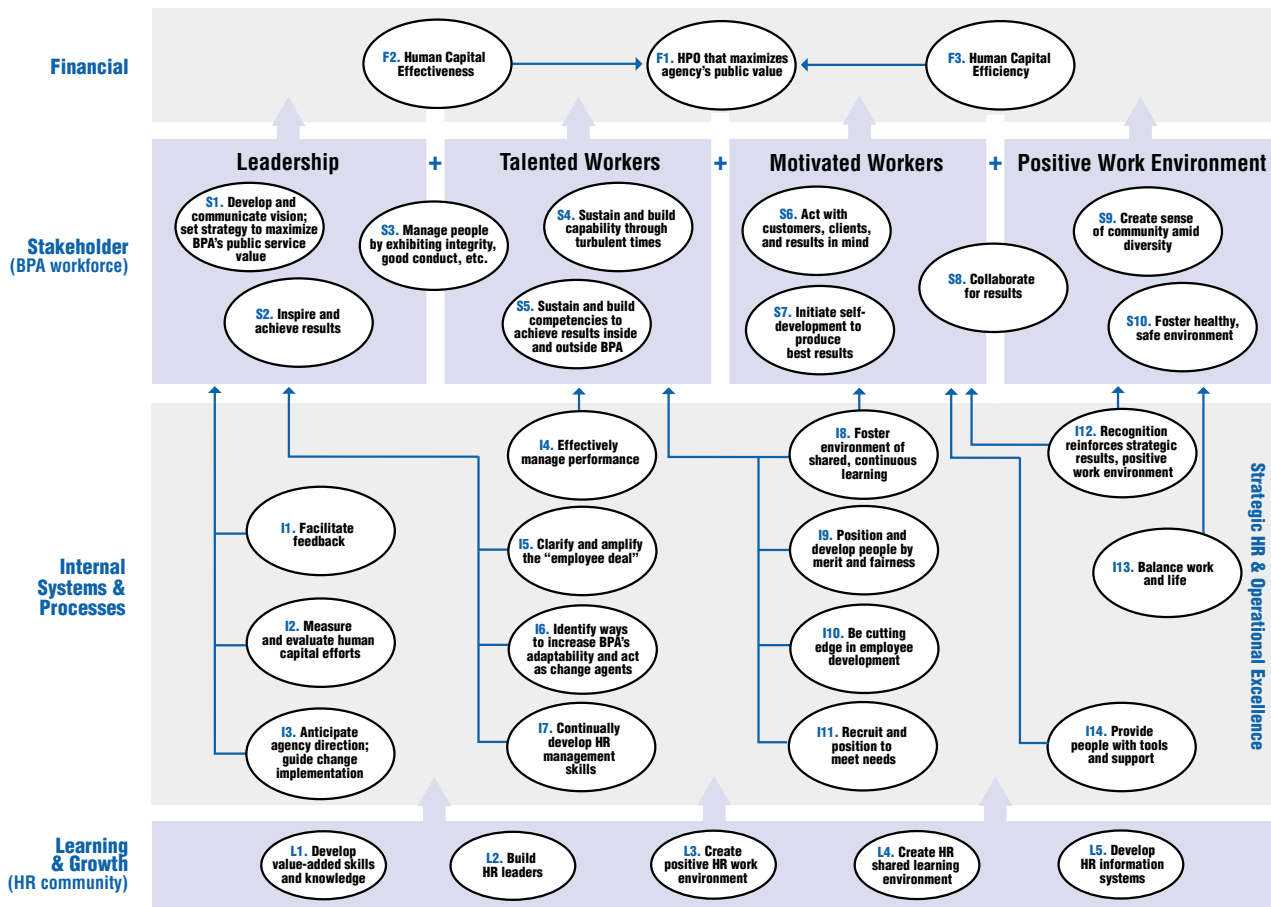
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**Figure 2. A Strategic Program to Develop Human Capital**

Human Capital Readiness Report			Human Capital Development Program		
Human Capital Category/Objective	Measure of Strategic Readiness	Target	HR Programs/ Functions	High Performance Practices (examples)	Measures (examples)
1. <b>Strategic Competencies</b> Understand the competencies needed, the competencies available, and the plan to close the gap.	<ul style="list-style-type: none"> <li>Strategic talent gap</li> <li>Key employee retention</li> </ul>		<ul style="list-style-type: none"> <li>Recruiting &amp; selection</li> <li>Training &amp; development</li> <li>Job/work design</li> </ul>	<ul style="list-style-type: none"> <li>Jobs filled from within</li> <li># Qualified for &gt; 1 job</li> <li># Hours training</li> </ul>	<ul style="list-style-type: none"> <li>Hours of training (strategic focus)</li> <li>Fill rate</li> </ul>
2. <b>Leadership</b> Build a cadre of leaders who can leverage human capital for competitive advantage.	<ul style="list-style-type: none"> <li>Leadership gap</li> <li>Employee survey of leadership effectiveness</li> </ul>		<ul style="list-style-type: none"> <li>Leadership development</li> <li>Succession planning</li> <li>Governance process</li> <li>Strategy management</li> </ul>	<ul style="list-style-type: none"> <li>Leaders are visionary</li> <li>Mission is clear</li> <li>Accountable for strategy</li> </ul>	<ul style="list-style-type: none"> <li>% Internal vs. external hires</li> <li>% Participation in leadership courses</li> </ul>
3. <b>Strategic Awareness/Culture</b> Create an organization that internalizes the shared vision, strategy, and cultural values required to execute.	<ul style="list-style-type: none"> <li>Cultural alignment index</li> </ul>		<ul style="list-style-type: none"> <li>Communications</li> <li>Change management</li> <li>Leadership development</li> </ul>	<ul style="list-style-type: none"> <li>Formal information-sharing program</li> <li>Mentoring program</li> </ul>	<ul style="list-style-type: none"> <li># of Approvals needed</li> <li>Culture assessment</li> </ul>
4. <b>Strategic Alignment/Motivation</b> Create an organization where personal goals and incentives are aligned with strategy and that encourages personal contribution.	<ul style="list-style-type: none"> <li>Goal alignment (%)</li> <li>Incentive alignment (%)</li> </ul>		<ul style="list-style-type: none"> <li>Performance management</li> <li>Compensation &amp; reward</li> <li>Positive work environment</li> </ul>	<ul style="list-style-type: none"> <li>Alignment of HR/business</li> <li>Balanced Scorecard</li> <li>Owning stock</li> <li>Eligible for incentive</li> </ul>	<ul style="list-style-type: none"> <li>Personal goals linked to BSC (%)</li> <li>% Receiving incentive compensation</li> <li>Gain sharing payments</li> </ul>
5. <b>Strategic Integration</b> Create teamwork and culture to encourage the sharing of knowledge and experience needed by the strategy.	<ul style="list-style-type: none"> <li>Sharing across boundaries</li> <li>Best practice</li> <li>Key people</li> <li>Teams</li> <li>Rewards</li> </ul>		<ul style="list-style-type: none"> <li>Knowledge management</li> <li>Organization effectiveness</li> <li>Staff rotation</li> </ul>	<ul style="list-style-type: none"> <li>Key staff retention</li> <li>Cross functional-teams</li> <li>Shared rewards</li> </ul>	<ul style="list-style-type: none"> <li>% Using knowledge-sharing channels</li> </ul>

*The Human Capital Development Program ensures alignment between HR investments and the enterprise strategy.*

**Figure 3. High Performance HR Organizational Strategy Map at Bonneville Power Authority**



The Learning & Growth layer of BPA's HR scorecard identifies the developmental objectives which must be achieved for the HR staff itself. To support this strategy, they will need improved skills, better leadership, an improved work environment, knowledge-sharing, and new HR information systems. Finally, note the Financial layer of BPA's HR scorecard. Since HR is a support organization, its financial objectives are a subset of the broader enterprise strategy. Identifying financial results for an HR organization is further clouded by the fact that effective human capital strategies also require complementary technology, process, and marketing strategies. It is not possible to isolate the financial contribution of human capital. However, it is helpful to use the financial framework to tell a part of the HR story. "HR efficiency" measures should be used to ensure that the HR organization is competitive with alternate

sources of service. Benchmarking against measures like HR administrative expenses (e.g., per employee or as a percentage of sales), or HR cost per transaction (e.g., per recruit) provides useful insights. "HR effectiveness" is determined through the Human Capital Readiness Report. However, macroeconomic measures like "revenue per employee" or "p/e ratio vs. competitors" are frequently used to evaluate the long-term effectiveness of the organization. Because they are such serious lag indicators, they are of little value as tools to manage by. Elevating the strategic readiness of the organization's human capital provides the best indicator of HR effectiveness.

### HR Must Take the Lead

Developing human capital is a strategic priority in the new economy — and it must become more of a science and less of an art. HR organizations are the natural custodians and leaders of such a process, but this will require a

change in traditional roles and behaviors. While these changes are necessary in numerous dimensions, the introduction of a structured process to develop human capital could serve as the "forcing function" to initiate these changes. If structured properly, such a program would allow the HR organization to take the initiative, instead of being reactive to the demands of the enterprise. A comprehensive approach that creates strategic alignment between HR and the enterprise at all levels (strategy, resource allocation, budgeting, reporting) is absolutely essential. The new role of HR should be captured in its own HR Balanced Scorecard. Developing this new management process provides the foundation to make HR a true strategic partner and enable the enterprise to realize the full value of its human capital.

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