

## HR METRICS FOR VALUE OF HUMAN RESOURCES: GAPS AND DIRECTION

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### ABSTRACT

The gap between what the HRIS of an organisation is capable of and what it is being used for presently is broadening. This is an alarming situation for HR department which has posed a challenge before the HR department to understand the factors underlying this gap, find reasons why have these not been able to cope up with the changed scenario and identify what more can be done to bridge this gap. One of the areas where HR department is lagging behind is the HR metrics, its measurement, implementation and alignment with individual as well as business outcomes which has tremendously been facilitated by HRIS development, but yet has not been complemented by the development of relevant, meaningful, employee centric and business strategy oriented HR metrics. The paper thus attempts to draw a vision as to where we are now, where we can be in terms of measurement of HR metrics and how we can best use these metrics to reach the goals of an organisation which it intends to achieve using their competitiveness in human capital resource.

### Keywords

Hr Metrics, Return on Investment, Human Capital Return, Value of Human Resources.

### Abbreviations

Full-Time Employee (FTE), Return on Investment (ROI).

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## Introduction

There are various kinds of people with varied abilities and competencies working in an organisation. At the same time, various kinds of interventions are used to enhance the performance of these human resources of the organisations. It is important for human resource department to understand which human factors differentiate one organisation from another or are leading human indicators for an organisation as the same is significant for an organisation to build the right measures to measure people value to the organisation (Schiemann, 2007). To this end the concept of using and applying HR metrics to an organisation's endeavors has gained strong justification.

Metrics means data or numbers that provide a descriptive detail about given processes or results (Carlson & Kavanagh, n.d.). It is actual reading on a measure at a given time (Schiemann, 2007). Adler & Burdick (2013) defined HR metrics as the standards of measurement which can be used to assess the value, productivity, efficiency, performance, progress and costs of human capital. These metrics provide information as to how HR department contributes to the organisation (Hussain & Murthy, 2013). For example metrics such as percentage of people hired internally for leadership roles and percentage of key roles ready with replacement may indicate time that organisation takes to fill key leadership roles (Missildine, 2014).

Policy makers are giving increasingly more emphasis on HR professionals to prove the value of HR programmes and thus incorporating a shift in their role by making it more strategic. This can be done through measurement of different metrics which can serve as a common business language of numbers and their application for strategic alignment (Gonzales & Kaye, 2008). This signifies that metrics in HR are considered important in the current scenario; however they only play a role of providing information and deviate from their primary use of driving business strategy based on the value of these metrics (Bhatnagar & Pandey, n.d.). The goal of HR metrics is to enable effective communication of achievement of business goals and to provide predictive intelligence that can be applied for business growth by the users of metrics (Adler & Burdick, 2013). The results found in the study conducted by Luketic (2009), revealed that HR department intends to focus hard on the way they hire and retain people, however they are not much inclined to look into the productivity these human resources are yielding, to find ways how can the same

be increased or to keep a check on their own efficient delivery of HR work (Luketic, 2009). Human resource department needs to understand and acknowledge that the business will not grow with hiring and retaining a good number of human resources rather what is more important in the context is what is the quality of people we have hired or trying hard to retain. The professionals in HR department need to rethink - Are these human resources contributing to the success of the business? Is HR department aware and delivering on its role to measure the extent to which these resources value to the organisation? Are the HR metrics being employed by them appropriate to answer this? Are they doing enough or making best utilization of the infrastructure available to them to calculate such metrics? Are they ensuring that the results obtained are utilized for the betterment of human relations, improvement of customer satisfaction and ultimately increasing the financial strength of the organisation? This paper attempts to draw their attention to these questions and encourage finding answers to the same.

## Review of Literature

There is some though not enough research made in the field of HR metrics. More importantly these metrics don't focus much on the value of human resources, benefits they bring to the organisation, value added to these human resources as a result of various interventions which aim to bring out improvement in their skills, knowledge levels, attitudes and behaviour. Most of these studies which have so far been conducted are qualitative in nature and do not involve much use of HR Metrics of advanced nature to validate improvement in these skills, knowledge level, attitudes and behaviours.

Mulhern (2007), opined that though there is a significant development made in the measurement of customer lifetime value which is evident from activity based costing, quantification of exact revenue and costs associated with individual customers to facilitate HR decisions pertaining to sales force allocation and marketing mix, there has not yet been made much of a progress when we talk about measurement of employee value. He argued that the reason underlying this is the fact that employees have so far been seen as a cost component of the organisation and thus every attempt is made by these organisations to minimize the employee cost. It is further proposed that all financial in flows to the organisation be allocated to individual employees as against the cost of maintaining each one of them for different time periods to assess the value of individual

employees which is quite relevant to justify employees efforts in true sense but not practiced because of the complexity involved.

Schiemann (2007), states that depending on the strategy of various organisations, they differ in measures used for measurement of outcomes of people. Though a cost leadership organisation would be interested in measuring efficiency, revenue per employee, an innovative organisation in idea generation and autonomy, a customer centric organisation would be more interested in empowerment and service skills levels.

As classified by Missildine (2004), HR Metrics can be of three types namely HR efficiency which focuses on numbers internal to HR department to track them, HR Effectiveness which can be measured through HR programmes, and lastly business and strategic metrics which represent result of investment in human capital. Though literature reveals that there is some progress made by organisations to measure effectiveness of human resource interventions like training and development programmes conducted by these organisations, most of the evaluation and analysis is qualitative and subjective which hinders the efforts of HR department to apply the results further to business decisions and strategy formulation. A quantitative evaluation of HR interventions like behavioural training and development programmes would serve as an evidence of the contribution that the programme is making to employees development and well as to organisation's growth (Sachdeva, 2014a). Thus HR needs to focus on developing and implementing HR metrics which provide quantitative and objective information so that the bottleneck to alignment of these interventions with individual and organizational outcomes may be overcome.

### **Current Scenario**

Presently productivity metrics, compensation metrics, recruitment metrics, retention metrics, HR efficiency metrics, workforce demographics are the various kinds of Metrics which are used by the HR departments (Human Resources Management Association, 2014).

According to Koenig & Associates Inc. (n.d.), certain common organisational/ strategic metrics used are - Revenue per Employee, Productivity Ratio, People Profit, Employee Pulse/ Satisfaction.

Productivity Metrics primarily include Revenue per FTE, Profit per FTE, Human Capital Return on Investment, Absenteeism Rate (Human Resources Management Association, 2014). Adler & Burdick (2013) have added two more metrics to this list which give a distinct result namely Revenue per Human Capital Expense, Profit per Human Capital Expense.

HR department in most of the organisations calculate HR Metrics such as Turnover, Absenteeism, Overtime per employee, Labour cost per employee, Vacancy rate, Average length of service, Headcount ratio etc. Though External hire rate, External cost per hire, and metrics concerning human resources directly like Human capital return on investment, Succession planning rate, Churn over (Internal movement rate) are in the wish list or to do list of most of the organisations as has been found by Luketic (2009). Also, organisations have not been found keen on measuring HR metrics such as Career path ratio, Learning and development revenue percentage, Management span of control, percentage of female employees by job level, hire ratio by age group, diversity hire ratio. The study thus reveals that most of the metrics which human resources would themselves be interested in, have a bearing on their work environment, culture, motivation are not being much focused upon by the human resource departments as yet.

In recent past balanced scorecard has come up as an HR metric which has been adapted by many of the organisations. Balanced Scorecard incorporates leading indicators of performance to assess customer, process, employee and financial outcomes and thus recognizes the organisations limitations of relying on measurable financial indicators of performance (Carlson & Kavanagh, n.d.). Similar HR metrics need to be developed which are able to quantify the value of human resources with probably more precision.

It is interesting to notice that many organisations are planning to calculate Human Capital ROI; they presently don't calculate that as such for various reasons. Human Capital ROI indicates the amount of profit generated for each dollar of compensation. The formula that may be used to calculate the same is:

$$(\text{Revenue} - (\text{Operating Cost} - \text{Labour Cost})) / \text{Labour Cost}.$$

A value greater than 1 is considered good in this case as original compensation amount invested is also included in the formula (Human Resources Management Association, 2014).

Similarly ROI of human resource interventions like training and development, recruitment and selection activity may be measured using the formula (Sachdeva, 2014b):

$$(\text{Benefits} - \text{Cost}) / \text{Cost} * 100$$

Sachdeva (2014c) argues that organizations often view HR interventions primarily as an indicator of modernization, adaptability and sustenance rather than attempting to find the financial implications of such interventions on organization and their contribution to the financial objectives of the organization.

The synthesis of literature indicates that there is a lot more that can be done in the field. HR department needs to speed up the process to build and nurture its own competencies to further work in this direction and better equip and enable itself to calculate the worth of employees, to further classify and categorize within human resources based on the quantitative information produced by HR Metrics, to use HR Metrics to align individual and organizational outcomes.

### Some Ironical Facts and Findings

- The Society of Human Resource Management conducted a survey which indicates that the total cost of workforce represents approx seventy percent of the operating expense for Fortune 500 companies (Visier, 2012).
- Koenig & Associates Inc. (n.d.), also found similar statistics and stated human resources costs constitute half or more of an organisations total expenditure, yet 57 percent of them don't track the impact of HR on their business and behaviour of people to improve performance.
- Though the infrastructure that supports HR metrics has changed to great extent in last few years, the metrics themselves have not undergone much of a change. Metrics that are currently used generally relate to costs or easy to calculate figures ignoring the benefits aspect of the information. This is one of the reasons why costs are likely to become the deciding factor for major managerial decisions concerning humans (Carlson & Kavanagh, n.d.).
- It is a bad indicator to discover that HR practitioners are well aware that they need to enhance their HR metrics and analytics ability to be able to efficiently address business

strategy issues (Lawler et al., 2004), yet there is no significant development made in this regard till date. It is the call of the hour for HR department to lead by example and increase its value to the organisation by doing nothing else but moving forward to measure all the aspects concerning the value of human resources and thereby be able to make these human resources a strategic partner in the success of the organisation.

## Trends and Developments

- Division of Human Resources partnership with the Saratonga Institute to launch the HR measurement programme is one such development in the field. More partnerships with intent to improve the HR measurement systems would be a great facilitator. HR metrics are in their infancy and it may take years before analytics may be further developed to predict the impact of people strategies on business goals (Gonzales & Kaye, 2008), but what is more important is that this is a high time for the organisations to at least start moving in this direction slowly and steadily.
- A study conducted by Luketic (2009), revealed that there has been a major change in the use of HR metrics since 2008. According to the study organisations with no measurement earlier have started making the progress towards measurement of HR metrics. Also the organisations which were following measurement of HR metrics earlier have been progressively moving towards alignment of the same with business strategy. However, it was strange to find that only 24 % of the respondents acknowledged availability of a dedicated resource in their organisation for providing HR metrics information. To make progress in this area not only a boost is required in terms of efforts and dedication to collect and analyze the data to measure such HR metrics but also organisations need to realise and ensure that resources are available to the users of HR metrics information so that they can easily get the information required, and relate their decision making process from their routine business decisions to long run decisions to these metrics. This may be one of the ways rather requisites to develop a practice among decision makers to seek and use HR metrics and align their decisions relating to human resources with the strategy of business.

## Limitations

- Linking HR strategy to increase in shareholder's value rather than linking it to business goals and outcomes is one of the factors that limit the effectiveness of HR metrics to contribute to the success of business (Hussain & Murthy ,2013). This in itself signifies that HR efforts are directed towards calculation of HR metrics that overlook the value of human resources which contribute towards the achievement of business goals.
- Various metrics are used by finance, marketing, sales and human resource departments to align their activities to the business strategy and thereby relating these activities and the outcomes to the organisational effectiveness. However, unlike finance and marketing department, human resource department often finds it difficult to provide metrics that exhibit a significant relationship between HR practices and organisational effectiveness due to lack of analytic models (Lawler et al., 2004).
- Managers often take computation and reporting metrics sought by HR only as a mandate without much interest in its use or even understanding the precise information required to compute these metrics. There is a need to bring a significant change in this approach that managers carry. Unless the importance of these metrics is realized by them and information there from is used for better decisions, HR metric in itself will not generate any Return on Investment. Rather this would only result in loss of time and effort in gathering and processing the information to obtain the value of these metrics (Carlson & Kavanagh, n.d.).
- HR metrics are used to measure activities instead of measuring results (Adler & Burdick, 2013). Unless we focus on the results made from investment in human capital, and work towards high return on human capital the activities would not be able to contribute to business results. Merely assessing that an activity was good enough and should be repeated in future using qualitative information carries no meaning without knowing to what extent has the same contributed to the organisational outcomes and individual effectiveness by making a fair comparison between the costs incurred and outcomes obtained.
- Most of the metrics are performed using aggregation to yield organisation level metrics and thus are not much of a help to identify, understand and further deal with differences



within an organisation (Carlson & Kavanagh, n.d.). There is a lot of scope to identify differences in abilities, competencies, attitudes, behaviours inherent and developed overtime using various interventions that lessen or broaden the difference in the worth of these human resources to the organisation. Thus apart from aggregate values, metrics should also be applied to individual employees to be able to determine its unique value to the organisation.

## HRIS and HR Metrics

- In recent years, HRIS field has exhibited a remarkable development. These advances have impacted to a great extent the way HR metrics and analytics are used. Faster and advanced computers, use of internet and intranet for better connectivity, collection and distribution of data have not only contributed to lowering the cost of assessment of people and thereby increasing the capacity of the organisation to assess HR processes and their outcomes, it has also ensued that the impact of HR metrics on organisational effectiveness becomes manifolds (Carlson & Kavanagh, n.d.).
- So long as the development in the field of HR metrics does not couple with the HRIS advancement, HR assessment and measurement system cannot be fully functional and be effective in totality. In a study it was found that though HRIS system is found operational in eighty percent of their respondents, yet very few of them were using the metrics and analytics to identify how HR investments lead to business outcomes (Lawler et al., 2004). Human resource department needs to ensure that the organisation spends each penny to make the best use of it and for that it needs to first focus on HR metrics that provide information as to what is the utility that they are able to draw from each employee, intervention and HR practice.

## Recommendations

Majority of HR Metrics in the field of human resource accounting have either aimed at the administrative efficiency of HR department for example time taken by them to process a request or requisition or at the cost side of the its support functions for example cost per hire, or training cost per employee. The benefits side is yet to be explored to facilitate comparison and see if benefits justify the costs incurred and if so to determine the level of business returns and

outcomes. This is why it is argued that Human Capital ROI approach followed by western nations is a good indicator of the success level of HR activities (Bhatnagar & Pandey, n.d.).

Koenig & Associates Inc. (n.d.), suggested that rather than trying to determine the strategy adapted by people in an organisation it will be more fruitful to measure business outcomes and results as the same are associated with business objectives. Further, Missildine (2014), also points out that in order to understand the impact of HR processes and investments on business outcomes these must be directly linked to business outcomes for example, customer satisfaction, sales level, productivity etc (Missildine, 2014).

For HR function to play a strategic role in an organisation, it is important that they work on developing their ability to not only measure how human capital decisions impact business as indicated by metrics like profit per FTE, revenue per FTE but also to assess how business decisions impact human capital which is better indicated by ROI of human capital, career path ratio, succession planning rate, external hire rate etc. (Lawler et al., 2004). It is further suggested that operational effectiveness impact metrics of training programmes and practices should attempt to identify changes brought in the performance levels of business processes such as reduction in defective items, increase in speed, frequency of innovations resultant from HR programmes and practices.

Use of HR Metrics and measures, for instance, in case of determination of ROI of training programmes of an organisation, may differ from one organisation to another depending on their training goals which are typically defined by their respective business and the strategy these organisations follow. Schiemann (2007), pointed out that an organisation with high efficiency low cost would use different success criteria to compare training impact than a customer centric organisation. Training cost per employee may not be a wise metric to be used for an organisation with different brands and thus different training needs compared to an organisation with just one brand and common training needs of all the employees.

While measuring value added in the form of productivity, the percentage improvement in workforce productivity over prior years and currency value of that productivity can be used as one of the metrics to describe workforce productivity (Hussain & Murthy, 2013). However while using averages to ascertain value of human resources, we must not overlook the extreme outliers

or else there is a danger of improper alignment among pay, position and performance (Visier, 2012).

Hussain & Murthy (2013), pointed out a strong correlation between human resource practices including rewards and accountability, flexible administration, recruiting and retention, HR service technology and prudent application of resources. These aspects may thus be further studied with the help of HR metrics and analytics to indicate how strong are these related for a given organisation and how they can leverage on success in one area consequent to success in another area and to what extent they can do so.

## Conclusions

In view of the transition witnessed worldwide by HR departments of all the organisations where human resources are considered as human capital and as is evidenced with huge investment made to maintain and improve their behaviour, attitude and performance, it has become all the more important today to focus on HR metrics that describe human resources in a better way, assess their contribution towards business outcomes as mediated by modification or up gradation of their level of skills and knowledge, attitudes and behaviours brought by various HR interventions. It is through- the development of employee behaviours that facilitate achievement of strategic goals of the organisation, measurement of employee behaviours resulting from various HR activities and interventions aimed at reaching the strategic goal and thereby measurement of organisational outcomes of those behaviours, that HR department can create value to the organisation using HR metrics to depict the same (Hussain & Murthy, 2013).

There is a need to build HR competencies and work towards attaining focus on HR value and strategic alignment and be innovative in the context to be able to catch up with the foreign multinationals (Bhatnagar & Pandey, n.d.). It is quite apparent that the time is not far away when statistics and data analysis will become a prerequisite for most of the HR roles and HR leaders would begin hiring a new kind of HR specialists i.e. people with quantitative analysis (Bolton & Payne, 2013).

All this would help organisations to be more aware of their competitive strength Vis a Vis their competitors, identify their weaknesses and thereby enable them to gain a competitive edge over other organisations.

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