*The Human Equation
of Service Quality*

Why Is This So Hard
The Business Case for Managing People Well
The Seven Strategies of Excellent Companies
Passion and Persistence Over Time

As important as strategy is, the key element of success is *implementation*—making the strategy operational.

The implementation of the day-to-day procedures that make the strategy work is a "nuts and bolts" function that is considerably less "interesting" than developing strategy. However, implementation ultimately has more bearing on long-term success.

In turn, the key element of effective implementation is often the people within the organization. How can a firm maximize the use of its people?

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Successful Implementation:

What is the sign of successful
implementation?
How does a company achieve this?

Any service business is successful only to the extent that it provides value to its customers. The key to customer satisfaction is the attitudes, skill, and motivations of the company's people, for these individuals have direct contact with customers and leave them satisfied—or not.

Managers of successful companies focus on the human equation, providing an environment that enhances the quality of its employees. People practices are the single most important factor in attracting, serving, and retaining customers in a service business.

The Financial Value of the Effective Employee

While improved employee management does not guarantee success by itself, extensive research suggests it is a major factor. For example: high-performance management practices can increase profits, quality, and productivity by 40%.

An award-winning study by Mark Huselid developed two scales: employee skills and organization structures; and employee motivation. The study then evaluated the correlation between these factors and market success (after controlling for other variables). Companies that improved their people policies by one standard deviation had the following results:

- 7% decrease in turnover
- $27,044 increased sales per employee
- $18,461 higher market value and $3,814 higher profits

The overall result on average was an $18,000 increase in stock market value—per employee.

A more comprehensive follow-up study found that the one-standard-deviation improvement in personnel management resulted in an increase in shareholder wealth of $41,000 per employee—a 14% market premium.

Further evidence has been found in the success of initial public offerings (IPO). Theresa Welbourne and Alice Andrews developed two scales (firm's value of human resources and its reward system); a formal measure of these practices then compared the results to survival rate. They found the following greater chance of survival between firms in each scale's top and bottom standard deviation for each scale:

- Human resource value = 20%
- Reward system = 42%

Developing an Effective
Workforce

Personnel management achieves such success only when it meets three standards:

1. Employees have knowledge that the managers do not.

2. The employees are encouraged and motivated to apply this knowledge as they see fit.

3. The firm's strategy acknowledges and incorporates the principle of employee discretion.

How does incorporating such practices lead to improved performance?

1. Employees work harder; they are more invested because of their increased control over how they do their jobs.

2. They work smarter, because they are encouraged to fully use their skills and obtain training.

3. Employees' increased responsibility can reduce supervisory costs as well as the impaired production that can result from employee/management conflicts.

In service industries, these changes enhance the performance of those who have the most direct contact with the customers.

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Employees' Importance
In theService Industry

Because their success is based on customer satisfaction, companies in the service industry must maintain effective personnel management practices. The nature of the business is the direct contact between employee and customer. Often, customers see the employee as *being* the service. In seniors' housing, for example, residents may not be able to effectively judge the quality of a blood pressure test, but they can and do judge the attitude of the employee performing the test.

Again, formal studies support this view. They have found, for example, a relationship among employee attitudes, customer attitudes, and profits. A study of bank branches found that when employees report that the branch focused on service, customers reported receiving higher quality service.

Customers recognize and respond to a service orientation among employees.

Studies of other service industries have produced the same results: effective personnel management leads to employees' higher performance, which, in turn, results in higher profits.

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So Why Doesn't
Everyone Do This?

The preceding discussion of employee management makes sense intuitively and is thoroughly supported by research. However, only 16% of American firms have at least one innovative practice in each of the following human resources areas:

- Flexible job design
- Worker training
- Pay-for-performance compensation
- Employment security

This study of 3300 businesses concluded:

- Only 25% compared policies with other organizations.
- Only 37% has adopted a formal quality-improvement program.
- 13% involved non-managerial workers in self-managed teams.
- Just 18% practiced job rotation.

One reason for the failure to change is that doing so requires a major commitment. In addition to the usual reluctance towards change, giving workers more authority and opportunity requires trust and confidence that they will use that authority well. Many organizations and managers lack that trust and confidence. Further, many management/supervisory philosophies and approaches are based on the implicit assumption that employees can't be trusted and the only way to keep them working is to keep looking over their shoulders. Such philosophies are the exact opposite of those personnel management approaches that have been most successful in motivating employees to provide high-quality service. These practices are called "high-performance" or "high-commitment" management practices.

6. Reduced status distinctions and barriers, including dress, language, office arrangements, and wage differences across levels

7. Extensive sharing of financial and performance information throughout the organization

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Seven Aspects of Effective Employee Relations

The remainder of this module will describe seven specific practices that produce the profit enhancement that well-managed companies have enjoyed:

1. Employment security

2. Selective hiring of new personnel

3. Self-managed teams and decentralization of decision-making as the basic principles of organizational change

4. Comparatively high compensation contingent on organizational performance

5. Extensive training

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Seven Aspects of Effective Employee Relations:

1. Employment Security

In spite of today's culture of layoffs and downsizing, employees with employment security are more productive in their jobs. In many settings, the most productive and innovative workers can, ironically, work their way out of a job.

Additional benefits of employment security:

- Avoiding layoffs prevents skilled employees from going to competitors and reduces hiring costs.
- Companies hire more carefully, because they intend for the individual to be a long-term employee.

- Companies are more likely to invest in training if they know employees will be with them for many years.
- Employees work harder, having a greater investment if they expect to be with the company for many years; they develop a long-term view of the company and its growth.
- Employees develop greater trust in co-workers and management.
- The policy attracts high-quality employees.
- Keeping employees during a slow period ensures they are still with the company when business picks up; other companies are likely to get into bidding wars for employees less talented than the ones they laid off.

All of these benefits have been verified through empirical research.

We emphasize that an employment security environment does not mean that employees are retained no matter what. Those who do not meet standards cannot continue with the company. However, downsizing and other arbitrary reductions have a long-term adverse effect on the company and employees.

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Seven Aspects of Effective
Employee Relations:

2. Selective Hiring

Getting the right people is obviously the starting point for effective personnel management. Six practices can significantly increase the likelihood of hiring employees who will provide the productivity and innovation the company seeks.

- Obtain numerous applicants per opening through such measures as extensive advertising and encouraging employees to discuss openings with colleagues.

- Screen employees for their ability to fit into the organization; hire for attitude, and other traits that cannot be obtained through training or experience.

- Before selecting applicants to interview, clearly identify the traits you are looking for, such as creativity, ability to work with others, and commitment. Doing so encourages interviewers to focus on the traits most needed in that position.

- Use multiple interviews and other tests to obtain information about the employee, build commitment, and reflect the company's emphasis on hiring the right person.

- For the same reason, arrange for senior personnel to interview the candidate whenever possible.

- After hiring the employee(s), formally review the recruiting process to identify potential improvements or practices that should be incorporated into the process. Ask, "How good is our screening problems? How do we objectively measure this process?"

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Seven Aspects of Effective
Employee Relations:
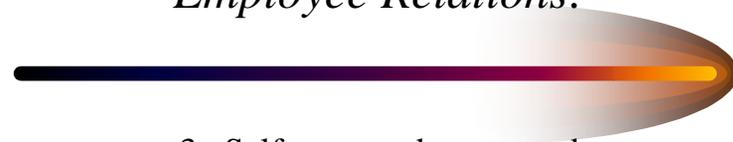
3. Self-managed teams and
decentralized decision-making

Numerous studies have found that the autonomy and discretion enjoyed by workers in self-managed teams increases job satisfaction, and, in turn, work quality. Fewer than 10% of workers on teams would like to switch back to traditional roles, while 75% of those in such roles would prefer to be on a team.

Some reasons self-managed teams are effective:

- Employees respond more to their peers than to management-based supervision; involvement with each other enhances initiative and responsibility.

- Employees feed off of each other's ideas, finding better solutions together than they could individually.

- Using teams significantly reduces costs related to supervision and management, since there is less need for this function and the expensive people who perform it.

Even when organizations can't realistically employ the self-managed team approach, they can still apply the principle of decentralized decision-making. For example, involving nursing assistants as equal partners in decision-making is extremely helpful in improving employee satisfaction.

As noted earlier, application of these principles requires management to trust the workers. Switching from traditional hierarchical control to decentralization requires faith that the workers care about the organization and their performance and will not take advantage of the reduced supervision.

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Seven Aspects of Effective Employee Relations:

4. Relatively high compensation based partially on organizational performance

A company can't expect above-average work from a work force paid at or below average levels. Salary levels send a message to the workforce—either they are truly valued or they are not. Talk is cheap; many organizations claim that people are their most important asset even as they *behave* differently. Tying employees' compensation to the success of the company, division, or team ("contingent compensation") can be in the form of gain sharing, profit sharing, stock ownership, pay-for-skill, or individual or team incentives.

However, contingent compensation must be in the context of the overall culture described in these pages. Even when motivated, inadequately skilled employees or those with little autonomy cannot perform effectively.

Other benefits of contingent compensation:

- It addresses the fairness issue of employees receiving some benefit from the success they helped create.

- People are more motivated because they know they will personally benefit from their work.

- Employment security is enhanced, since employees are encouraged to be as productive as possible rather than putting in time until they retire.

- The compensation encourages peer pressure to perform, since each worker's pay depends on other workers' performance.

The conclusion: High pay can enhance economic success if used properly.

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Seven Aspects of Effective
Employee Relations:
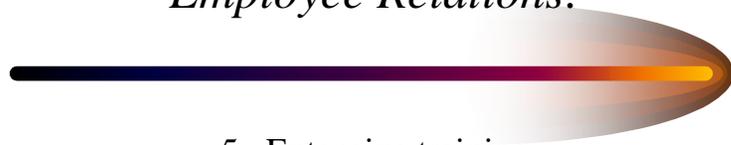
5. Extensive training

A company that promotes worker autonomy must provide extensive training, for a skilled and motivated workforce is central to the concept of self-managed groups. Many companies, however, view training as a luxury to be used only during highly profitable times, particularly since it is difficult to assess its direct financial value. Still, training is an essential investment in the workforce and thus in its future—as well as providing a competitive advantage over firms that do not value it.

Training must be properly focused, however, General training (overall competence, corporate culture, etc.) is needed more than specialist training that focuses on narrow skills. For example, there is virtually no training for nurse's aides on social skills, when in fact this may be their most important skill. Residents respond to this skill, which has the greatest impact on their loyalty and delight.

For a company's training investment to pay off, it must maintain an employment security program. Training workers then laying them off benefits only the firms that hire them later.

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*Seven Aspects of Effective
Employee Relations:*

6. Reduced status differences

To be as effective as possible, the approaches we've described must be associated with the message to employees that they are important to the company and valued. Doing so typically involves two types of approaches:

- Symbolic, by structuring workspace, establishing policies that enhance employees' status and comfort, etc. For example, titles can significantly affect workers' view of their own value and respect from others.

- Substantive, primarily by reducing the organization's wage inequality. For example, some companies have a

policy that the highest-level manager's compensation will be no more than *X* times that of the lowest-paid worker.

Particularly effective is tying managers' pay into the same profit-sharing (or other) plan that determine other workers' compensation.

Organizations can also reduce status differences by having a single dining areas for all employees, getting rid of management parking areas, differences in dress, and eliminating other practices and perks that distance management and staff.

The result of such efforts is open communication between management and teams, further enhancing the benefits of joint problem solving.

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Seven Aspects of Effective
Employee Relations:

7. Sharing performance, strategy, and
financial information

Sharing information with employees has three benefits:

- Emphasizing to the employees that they are trusted

- Giving employees the broad picture, enabling them to understand how their performance promotes overall company success; however, employees must receive training in how best to apply that information.

- Enabling employees to tailor their own work in accordance with the organization's cost control initiatives.

Unfortunately, many companies are reluctant to freely share information:

- Doing so shifts some of the power from management to employees.

- Fearing that information will leak to competitors—neglecting the fact that the competition usually knows this information already.

Employees who have a limited understanding of their company's overall strategy and standing (including financial status) simply cannot be as effective in contributing to its goals. Conversely, sharing information and training them in its use enables people at all levels to make better decisions.

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Getting There from Here

A company can't implement these procedures in a piecemeal fashion, but must integrate them into an overall company philosophy regarding the role of its employees in its strategy and operations. Using a systematic approach and applying a change in company values will make fullest use of these techniques and their potential.

Further, implementing these personnel approaches takes time, largely because of the associated changes in the corporate culture. While results will be apparent almost immediately, the company is unlikely to achieve full benefits for several years.

These practices, therefore, like so many other organizational changes, require the development of, commitment to, and implementation of a long-term vision.

Ultimately, top management, especially the CEO, must *live* this belief system or it will fail. People quickly know if this is just another fad or attempt to make money for top management at the employees' expense.

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