

## **Series: Human Capital Management**

Session 2: Introduction to Human Capital Management - Linkage of Management Strategy and Human Resource Strategy

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### **1. Introduction.**

The "Human Capital Management Series" presents the basic concept of human capital management, and systematically suggests points that companies should address before implementing it. In the first article, we will discuss the background of the need for human capital management, the difference between conventional management styles and human capital management, and the "Study Group Report on Sustainable Corporate Value Enhancement and Human Capital - The Ito Report for Human Resources" (after this referred to as the "Ito report") released in September 2020 by the Ministry of Economy, Trade and Industry (METI). The Ito report explains the elements of the 3P/5F model and the characteristics of the human capital strategy that should be implemented.

In the second session, the need for each of the perspectives and elements organized in the 3P/5F model will be explained as well as how they differ from conventional views and details. This article explains the first element of human capital management: the linkage between management and human resource strategies.

### **2. Linking Management and Human Resources Strategies**

The critical phrase "linking management and human resource strategies" may not be considered new by many. It is true that in most companies the design and improvement of personnel systems, the total cost of personnel management, the promotion, demotion and evaluation of personnel, and the planning for new graduates and mid-career hires are all decisions made by management; it is no mistake that management and human resources are routinely linked. Precisely, the Ito report emphasizes the importance of the linkage between management and human resource strategies. Since the 2010s, the term VUCA has been used to describe the present business environment. VUCA is an acronym for Volatility, Uncertainty, Complexity, and Ambiguity. It has been defined as a circumstance in which the surrounding environment changes rapidly, and the future is

difficult to predict. In the era of VUCA, companies must make drastic changes to their strategies. Therefore, it is rare to find a company with a business strategy that provides the same value to customers and markets through the same business infrastructure. Most companies incorporate discontinuous changes such as new business models, new businesses, and transformations of management bases into their management strategies. Human resource strategies have been oriented toward efficient, collective human resource management optimized for each company based on the assumption of a stable business environment.

Thus, a gap exists between management strategy, which emphasizes responsiveness to change, and human resource strategy, which is based on the past business environment. Consequently, new business strategies corresponding to the business environment are not implemented because the necessary human resources are not allocated appropriately. In light of this situation, the Ito report recommends that future human resource strategies should flexibly secure and develop the human resources needed to execute the management philosophy and the management and business strategies.

### **3. Linkage of management and human resource strategies - Image of practice**

Now, we will explain how to link management and human resources strategies.

The Ito report states that the management team should take the initiative to promote the following four issues: (1) clarification of the corporate philosophy and purpose, (2) clarification of goals in the management strategy, (3) identification of the human resource agenda important to the management strategy, and (4) establishment of quantitative KPIs for the future image.

First, we will explain (1) the clarification of the corporate philosophy and its purpose. There are various definitions of purpose; one of the typical definitions is the visualization of the company's "raison d'etre" in society. Compared to vision, mission, values, and purpose, it is characterized by the fact that it is expressed in terms of altruism and how to approach social issues. As a company, centripetal forces are indispensable for demonstrating organizational strength in the coming years. However, in light of the discontinuous business environment and the diversification of human resources, work styles, and values, it is no longer realistic to form a centripetal force through lifetime employment. This is expected to be the centripetal force attracting diverse human resources in the coming era.

Next, the sequence of steps is explained: (2) clarification of goals to be achieved in management strategy, (3) identification of the human resource agenda relevant to management strategy, and (4) establishment of quantitative KPIs for the future state to be aimed at.

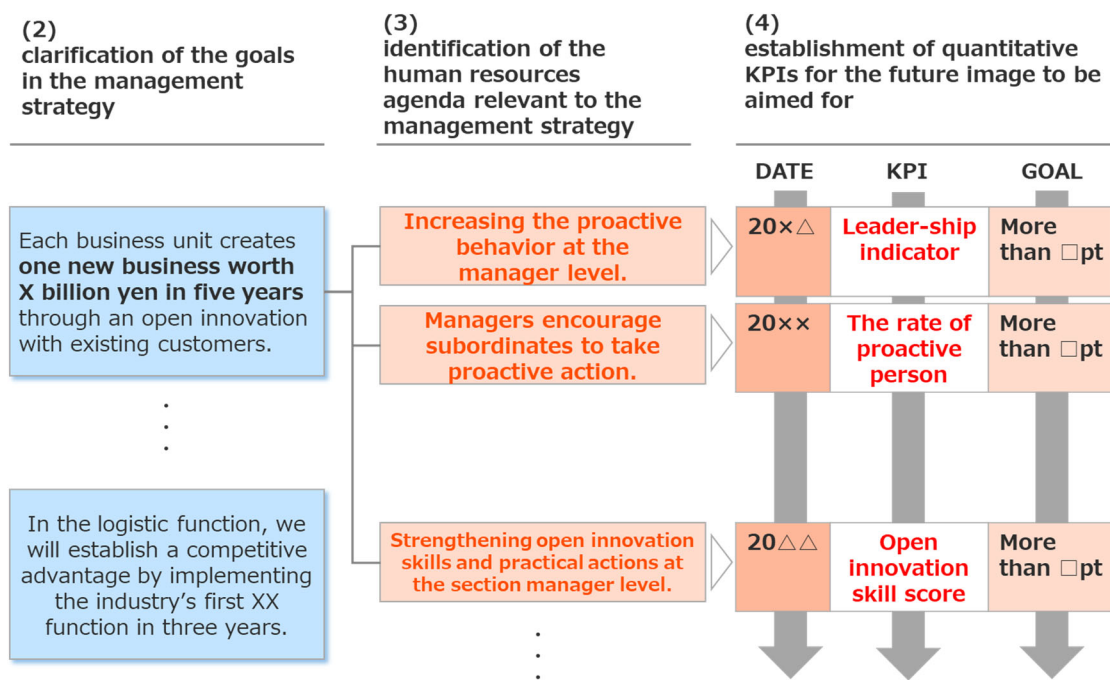
The key to implementing this point is to be aware that the management strategy must be extended to the human resource image when formulating the management strategy and to set specific goals such as "what" and "to what extent" is to be achieved by "when" at least. In situations where management and human resource strategies are not linked, it is often interpreted that the problem lies solely on the human resource strategy. However, the problem often lies in the management strategy. If the management strategy is completed at the policy level, such as "promoting business transformation through DX," and the specific strategy development is unclear, it is impossible to analogize the necessary management resources.

Next, (3) the identification of the human resource agenda is important for management strategies. In this section, the issues of what kind of human resources are needed and to what extent must be set as specific agenda items and permanently placed on the agenda of the board of directors meeting. Although human resources are essential for business strategy execution, management teams rarely discuss it. In recent years, there has been a growing movement to make the board of directors "a forum for discussion and decision-making," as exemplified by the call for a corporate governance code. By setting human capital, which determines the success or failure of management, on the agenda of the board of directors and management meetings, management must formulate and manage human resource strategies.

Finally, (4) quantitative KPIs related to the future state to be aimed at are established. The point is to set indicators that anyone can see as to "when" and "to what extent" they should be achieved in line with the agenda. The critical point is to set KPIs as milestones in terms of whether progress is being made in securing and training human resources, rather than just financial and result indicators such as personnel costs, as has been the case in the past. It is necessary to establish a common communication infrastructure that can observe and discuss how to deal with a situation based on a shared understanding of how well human resources are secured and nurtured.

Thus far, we have focused on the level of detail required, from (2) the clarification of goals to be achieved in the management strategy to (4) the establishment of quantitative KPIs related to the future state to be aimed at. We hope it is now clear that the key to linking management and human resource strategies is the active involvement of the management team and thorough indexing. Although the description level differs from company to company, please refer to the following for a concrete image of the "linkage of management strategy and human resource strategy."

**Figure 1: Specific images of the linkage between management strategy and human resource strategy**



Source: The Japan Research Institute, Limited.