

**THE IMPACT OF STRATEGIC INTEGRATION AND
DEVOLVEMENT OF HR PRACTICES ON FIRM
PERFORMANCE: SOME EVIDENCE FROM AUSTRALIA**

Kai K Andersen, Brian K Cooper & Cherrie Jiu-hua Zhu

*Working Paper 53/05
August 2005*

**DEPARTMENT OF MANAGEMENT
WORKING PAPER SERIES
ISSN 1327-5216**



Abstract

Since its emergence, strategic human resource management (SHRM) has been the focus of debate over whether it exists in reality or is merely rhetoric. SHRM is often measured by the integration of the HR function in the strategic management process, the devolvement of HR practices to line managers, and the impact of these practices on firm performance. Based on a survey of senior, line and HR managers from 66 Australian publicly listed firms, this paper examines the extent to which SHRM is practised and its impact on firms' financial performance. The research findings indicate that strategic integration and devolvement of HRM are practised to a moderate extent in the organizations, and the degree of alignment of HRM with business objectives and strategies had a positive relationship with firm performance. Furthermore, the amount of line management training in HR practices acted as a moderator by strengthening the relationship between devolvement and firm performance. The results indicate that SHRM practised in Australian firms could be improved if organizations increased training and support of line managers in the devolvement of HR practices.

THE IMPACT OF STRATEGIC INTEGRATION AND DEVOLVEMENT OF HR PRACTICES ON FIRM PERFORMANCE: SOME EVIDENCE FROM AUSTRALIA

Human resource management (HRM), once claimed as 'a contemporary manifestation of the American dream' (Guest 1990), has been developed and is widely practised in Western countries (e.g., Brewster and Hgewish 1994). However, critiques have been raised regarding its value creation, i.e., whether HRM can contribute directly to the implementation of the strategic objectives of firms and improve performance (e.g., Hope-Hailey et al. 1997). As a consequence, strategic HRM (SHRM) emerged in the early 1990s with more emphasis on an integrative and value-driven approach to HRM. SHRM focuses on several issues, including the fit between human resource (HR) practices and organizational strategic goals, the integration of HRM in organizational strategic management, the involvement of the HR function in senior management teams, the devolvement of HR practices to line managers, and the value that is added to organizational performance by HRM (Bowen and Ostroff 2004; Ulrich 1998).

Although supported by both theoretical work such as the resource-based view (e.g., Wright, Dunford and Snell 2001) and some empirical evidence (e.g., Becker and Gerhart 1996; Wright, Gardner and Moynihan 2003), SHRM still needs to prove its worth, i.e., its contribution in a measurable way to organizational performance (Budhwar and Khatri 2001; Fisher and Dowling 1999; Schuler and Jackson 1999). Despite the efforts into SHRM research, there is debate as to whether organizations actually practise SHRM, whether line managers have a role in transforming the HR function to be more strategic, and whether it adds value to the bottom line (Martell and Carroll 1995). In this paper, based on a preliminary investigation conducted in Australia, we examine the extent to which strategic integration and devolvement of HRM are practised in a sample of publicly listed firms and the impact strategic integration and devolvement of HRM practices have on a firm's financial performance.

STRATEGIC HUMAN RESOURCE MANAGEMENT: INTEGRATION AND DEVOLVEMENT

The term SHRM evolved over the late 1980s and the early 1990s with an increased emphasis on a proactive, integrative and value-driven approach to human resource management (e.g., Butler, Ferris, and Napier 1991, Schuler 1992). SHRM views human resources as assets for investment, and the management of human resources as strategic rather than reactive, prescriptive and administrative (Budhwar 2000a; Buyens and De Vos 2001). It is defined as the extent to which HRM is considered during the formulation and implementation of corporate/business strategies (Brewster and Larsen 1992) or as "the pattern of planned human resource deployments and activities intended to enable an organization to achieve its goals" (Wright and McMahan 1999: 52).

Integration of HRM with Corporate Strategies and Management

Integration refers to the involvement of HRM in the formulation and implementation of organizational strategies and the alignment of HRM with the strategic needs of an organization (e.g., Buyens and De Vos 1999; Schuler and Jackson 1999). There is evidence that integration tends to result in enhanced competence, congruence and cost effectiveness (Black and Boal 1994; Teece, Pisano and Shuen 1997). Researchers also argue that in order for HR to be a strategic partner HR managers should be involved in strategic decision-making alongside other senior managers, providing greater opportunity to align HR goals, strategies, philosophies and practices with corporate objectives and the implementation of business strategy (Ulrich 1997a; Buyens and De Vos 1999). This involvement would include the membership of HR managers in the most senior management team in the organization (see Budhwar 2000b, Teo 2000, 2002), which provides the opportunity for HRM to represent its concerns and influence business strategy from the outset of decision-making. To achieve strategic integration and alignment of HRM with business strategies, a documented HRM strategy would also be useful (see Budhwar 2000b; Teo 2000, 2002) as it can make more concrete the role and authority of HR managers in corporate

decision-making, and helps the organization to develop an HRM vision and objectives and to monitor performance.

Much of the research for evidence of the link between SHRM and firm performance has focused on intermediary performance indicators such as absenteeism, commitment, customer satisfaction and innovation (e.g. Pfeffer 1994; Chew and Chong 1999; Bowen, Galang and Pillai 2002). There is a need for research to focus on bottom-line indicators (Richard and Johnson 2001) such as return on equity and profitability as HRM is under pressure from CEOs, CFOs and senior managers to quantify added value to the bottom-line when HR managers join the senior management team (Buyens and De Vos 1999; Sullivan 2003). We thus propose three hypotheses:

H1a: There will be a positive relationship between strategic HRM alignment and firm financial performance.

H1b: There will be a positive relationship between senior management committee membership of HRM and firm financial performance.

H1c: There will be a positive relationship between a documented HRM strategy and firm financial performance.

Devolvement of HR practices to Line Managers

To make HR managers more available for participation in strategic decision-making processes, it is argued that the responsibility of routine execution and administration of HR practices should be delegated to line managers as they have direct and frequent contact with employees and a capacity to understand, motivate, control, and respond quickly to employees (Ulrich 1997b; Budhwar and Khatri 2001). This delegation or devolvement of HR practices is defined as the involvement of line managers in the execution and administration of HR practices (Brewster 1999; Budhwar 2000a, 2000b), such as performance assessment, recruitment, selection and training of employees. In addition to providing increased opportunities for involvement of the HR function in strategic decision-making, devolvement may have more direct effects on firm performance. This devolvement may also increase contact between HRM and line managers to assist HR managers in understanding front-line business problems (Sullivan 2003), and increase the ability of HR to contribute ideas for change at a corporate level (Laabs 1992).

However, for the benefits of devolvement to be realised line managers will possess appropriate skills to execute HR practices competently and effectively, to a benchmarked standard advocated by HR managers (Hope-Hailey et al., 1997; Hall and Torrington 1998; Budhwar 2000b). It means that the senior HR manager needs to be a strategic partner with line managers, providing training, resources, incentive and a communication channel to ensure these HR practices are carried out in accordance with HRM policy (Budhwar 2000b; Budhwar and Khatri 2001; Teo 2002). Hence, the amount of line management training in executing HR practices is likely to act as a moderator by positively strengthening any relationship between devolvement and firm performance. Thus Hypothesis 2 proposes:

H2: There will be a positive interaction between line management training in HR practices and devolvement on firm financial performance.

METHOD

Sample and Procedure

The data reported here are based on a stratified random sample of publicly listed firms from the Australian Stock Exchange (ASX) database. A population of 961 firms was available from the ASX database as of May 2003. Due to cost limitations in surveying the entire population, a stratified random sample ($N = 231$) by industry sector was selected. Anonymous questionnaires were mailed to the senior human resource manager in each firm, accompanied by a covering letter and reply paid envelope. Follow-up phone calls were made two weeks after the initial mail out in an

effort to increase the response rate and to verify that the company had a HR department or function. These follow-up calls identified 15 firms that did not have a formal HR function, leaving 216 eligible respondents. Of this, we received 66 completed questionnaires, a response rate of 31%. Despite the relatively small sample size, this is a typical response rate for mail surveys to managers (Baruch 1999).

In terms of managerial seniority, most respondents reported being either senior (44%) or middle (30%) managers. The majority of managers (61%) were based in the firms' HRM Department. Mean firm size, as measured by the number of full-time equivalent (FTE) employees was 3,096 (due to severe positive skewness, this variable was transformed in subsequent analyses). In respect of industry, organizations in the manufacturing sector accounted for 24% of the sample. The services industry sector accounted for another 23% of the sample (this included organizations in financial services, retail stores, food preparation and entertainment), with a further 20% in resources (mining and exploration) and 33% in 'other' industries, including a wide variety of miscellaneous industries from power distribution to information technology.

Measures

Strategic HRM alignment with business objectives and strategies was measured by 10 items, each rated on a 5-point scale ranging from (1) 'not at all' to (5) 'to a great extent'. Items developed from the literature (e.g., Budhwar 2000b; Teo 2002) were: (1) HR practices help achieve business objectives, (2) HR practices are used to implement business strategies, (3) HRM involvement in business decision-making, (4) HRM strategy is formulated based on business strategy, (5) HRM involved in coordination of the business, accessibility of HR information, (6) alignment between business and HRM strategies, (7) senior HR manager is a strategic partner for line managers, (8) HRM involvement in development of employee programs, (9) HRM involvement in development of work procedures, and (10) HR is part of the organization mission statement. Principal components analysis of the 10 items indicated a single factor thus providing support for the unidimensionality of the scale. Internal consistency reliability of this measure was excellent, with a Cronbach's alpha coefficient of .94. The 10 items were averaged to form a composite measure, with higher scores indicating greater strategic alignment.

We also asked whether the firm had a documented HRM strategy (coded 0 = no, 1 = yes) and if the senior HR manager was a member of the senior management committee (coded 0 = no, 1 = yes).

Line management devolvement. This variable was measured by asking respondents to indicate the involvement of line managers in the execution of five HR practices. These practices were chosen based on a previous research design (see Budhwar, 2000b), and based on their administrative type natures. Items were worded to emphasize the execution of HR practices: 'recruits new people', 'selects applicants', 'trains employees', 'executes performance assessments' and 'designs job roles'. Firms that indicated the involvement of line managers in one HR practice scored a 1, two practices scored a 2, and so on, up to 5. The range of the line management devolvement index is thus 0 to 5.

Line management training in HR practices. This variable was measured by asking respondents to indicate the proportion of line managers trained in the firm to execute HR practices. The percentage of line management training was scored on a scale from (1) 'less than 10%' to (10) 'more than 90%'.

Firm financial performance. Following the work of O'Shannassy (2004), four items were used to measure financial performance: (1) return on equity (ROE), (2) return on assets (ROA), (3) market growth, and (4) profitability. Ratings of each performance indicator were made relative to the industry's average on a 5-point scale from (1) 'very poor' to 5 'very good'. This is a perceptual measure relative to the financial performance of competitors. Perceptual measures have been found to correlate moderately to strongly with more objective measures of firm performance

(Delaney and Huselid 1996). Internal consistency of this measure was excellent, with a Cronbach's alpha coefficient of .90. The four items were averaged to form a composite measure, with higher scores indicating greater financial performance.

Control variables. In our multiple regression analyses, we controlled for contextual influences on firm performance, namely, the effects of firm size (total FTE employment) and industry sector (Huselid, 1995). It has been argued that HRM could be more conducive in services industries, since labour-intensive industries such as manufacturing can often substitute people with automated technology (Schuler and Jackson 1999). We therefore included a service sector dummy variable (1 = service sector industry, 0 = other) in our analyses.

RESULTS

Extent of Strategic HR integration and Devolvement

The mean score for the strategic alignment measure was 3.27 out of a possible high score of 5, suggesting a moderate extent of strategic alignment between HRM and organizational business objectives. Of the firms, 65% had a documented HRM strategy. Higher levels of committee membership were found with 83% of firms reporting that their most senior HR manager was a formal member of the most senior management team.

To assess the tendency of organizations to devolve HR practices to line managers, two criteria were used, namely, the involvement and training of line managers in HR practices. Based on a possible range of 0-5 practices, the results revealed that line managers executed a mean of 2.65 HR practices, slightly higher than the number executed by HR personnel (2.26), middle managers (2.21), and senior managers (1.78). In terms of the second criterion for devolvement (i.e. training provided for line managers to execute HR practices), the findings were mixed. The mean response (4.91 out of 10) indicated a moderate level of training offered by organizations to their line managers in the execution of HR practices.

Impact of Strategic HR Integration and Devolvement on Financial performance

We then conducted a multiple linear regression analysis using firm financial performance as the dependent variable. Firm financial performance was regressed on to the variables of strategic HRM alignment, committee membership, presence of documented HR strategy, line management devolvement, line management training, and the product term representing the interaction between line management training and devolvement. Firm size and the service sector dummy variable were also included. Colinearity diagnostics using the Tolerance Test indicated that the regression coefficients were not degraded by multicollinearity. Pairwise deletion was used for missing data. There were no consequential departures from normality, linearity and homoscedasticity. To generate a standardized regression model when an interaction term is present, all variables were converted to z-scores prior to analysis (Tabachnick and Fidell 2001).

Table 1 presents the results of the multiple regression analysis. Overall, the regression model accounted for 24% (adjusted R^2) of the variation in firm financial performance. Two variables were statistically significant in the prediction of firm performance. There was a moderately strong positive relationship between strategic HRM alignment and firm financial performance, controlling for other variables ($\beta = .48, p < .01$). This finding supports H1a. As predicted, the interaction term was statistically significant and in the expected direction ($\beta = .30, p < .05$). This finding provides support for H2 that the amount of line management training in HR practices acts as a moderator by strengthening the relationship of devolvement and firm financial performance.

Table 1 also shows that committee membership and presence of documented HR strategy failed to show any statistically significant relationship with firm performance. These results indicate that both H1b (i.e., there will be a positive relationship between senior management committee

membership of HRM and firm financial performance) and H1c (i.e., there will be a positive relationship between a documented HRM strategy and firm financial performance) were not sufficiently supported by the present data.

Insert Table 1 about here

DISCUSSION

This preliminary study contributes to our understanding of the relationship between the variables of strategic HRM integration, devolvement and firm performance. We should acknowledge some limitations of this preliminary investigation upfront. Generalizability is limited by the relatively small sample size and possibility of non-response bias. The data are cross-sectional and a longitudinal design would have helped to strengthen casual inferences. Future studies could obtain measures from different sources, including more objective indicators of firm performance and the use of multiple organizational informants to strengthen validity (Wright, Gardner, Gerhart, and Delery 2001).

The results of this study indicate that HRM was integrated into the organizations' core business operations, although such strategic alignment was only at a moderate level. From the perspective of committee membership, senior management integration appeared to be high (83%). That is, the majority of organizations provided the most senior HR manager with a formal position on the most senior management team. The majority of organizations surveyed had a formally documented HRM strategy (65%). In comparison, Budhwar (2000b) reported that in the U.K. manufacturing sector only 44% of firms reported to have a HRM strategy and 55% had HR managers with committee membership.

In contrast, the empirical evidence regarding devolvement reflected a mixed story. While line managers were involved in the execution of HR practices, on average the level of training for line managers to perform these practices was moderate, which indicates that the transfer of HRM knowledge was likely to be somewhat limited. Insufficient training offered to line managers greatly undermines the capacity of line managers to perform HR activities effectively. Quality of administration and execution is placed at risk and it is more likely that HR managers will be required to fix on-floor problems, i.e. to be a 'fire-fighter' rather than a strategic partner. The mismatch between the involvement of line managers in HR practices, and the training of line managers in HR practices has been a concern highlighted by other researchers (e.g. Buyens and De Vos 1999). However, the results of this study provide support for our Hypothesis 2 that the relationship of devolvement and firm financial performance can be strengthened if firms engage in *more* line management training in executing HR practices.

As predicted, there was a positive relationship between strategic HRM alignment and financial performance, controlling for other variables. Thus, we have received support for our Hypothesis 1a (i.e., there will be a positive relationship between strategic HRM alignment and firm financial performance). This indicates that alignment of HR strategy and practices particularly through involvement in the development and implementation of organizational strategies is a predictor of firm performance. This finding is consistent with previous research that has found weak-to-moderate relationships between SHRM and organization performance such as ROE, productivity, absenteeism, and the achievement of strategic visions, employee commitment, absenteeism, and innovation (e.g. Appleby and Mavin 2000; Buyens and De Vos 1999; Chew and Chong 1999; Richard and Johnson 2001). There was insufficient evidence to indicate a relationship between other SHRM predictors (e.g., presence of documented HRM strategy, senior management committee membership) and financial performance, which means Hypothesis 1b and Hypothesis 1c were not supported.

In conclusion, the results of this preliminary research have indicated a moderate level of SHRM practised within Australian organizations. The study found evidence for a positive relationship between the degree of strategic alignment of HRM with business strategies and financial performance. This research has contributed to the field of strategic human resource management by providing evidence for the value-added SHRM through integration of the HR function within the organization's key strategies and operations. The implications from this study together with other research studies are that managers should integrate their HR function to the firm's business strategy and operation, and that the training offered to line managers should be increased to achieve the objectives of devolvement. The other implication is that future research is required to continue work towards measuring the added value of SHRM. This means in addition to examining the impact of SHRM on financial performance as we did in this paper, we may also need to include its impact on the firm's social performance such as enhancing employee well-being and customer satisfaction.

REFERENCES

- Appleby, A. and Mavin, S. 2000. Innovation not imitation: Human resource strategy and the impact on world-class status. *Total Quality Management, Abingdon*, 11(No. 4-6): 554-61.
- Baruch, Y. 1999. Response rate in academic studies – a comparative analysis, *Human Relations*, 52(4): 421-438.
- Becker, B. and Gerhart, B. 1996. The impact of human resource management on organizational performance: progress and prospects. *Academy of Management Journal*, 39: 779-801.
- Black, J. A. and Boal, K.B. 1994. Strategic resources: Traits and configurations and paths to sustainable competitive advantage. *Strategic Management Journal*, 15: 131-148
- Bowen, D. C., Galang, c. and Pillai, R. 2002. The role of human resource management: An exploratory study of cross-country variance. *Asia Pacific Journal of Human Resources*, 40(1).
- Bowen, D. E. and Ostroff, C. 2004. Understanding HRM-firm performance linkages: the role of the 'strength' of the HRM system. *Academy of Management Review*, 29(2): 203-221
- Brewster, C. 1999. Strategic human resource management: The value of different paradigms. *Management International Review*, 39: 45-60.
- Brewster, C. and Hgewisch, A. (Eds), 1994. *Policy and practice in European Human Resources Management*, London: Routledge
- Brewster, C. and Larsen, H. H. 1992.. Human Resource Management in Europe: Evidence from Ten Countries. *The International Journal of Human Resource Management*, 3: 409-433.
- Budhwar, P. 2000a. A reappraisal of HRM models in Britain. *Journal of General Management*, 26(2): 72-91.
- Budhwar, P. 2000b. Strategic integration and devolvement of human resource management in the UK manufacturing sector. *British Journal of Management*, 11(4): 285-302.
- Budhwar, P. and Khatri, N. 2001. HRM in context: Applicability of HRM models in India. *International Journal of Cross Cultural Management*, 1(3): 333-356.
- Butler, J. E., Ferris, G. R. and Napier, N. K. 1991. *Strategy and Human Resources Management*. Cincinnati, OH., South-Western.
- Buyens, D. and De Vos, A. 1999. The added value of the HR department. In Chris Brewster and Hilary Harris (Eds) *International HRM: Contemporary Issues in Europe (pp31-47)*. London and New York: Routledge.
- Buyens, D. and De Vos, A. 2001. Perception of the value of the HR function. *Human Resource Management Journal*, 11(3): 70-89.
- Chew, I. and Chong, P. 1999. Effects of strategic human resource management on strategic vision. *International Journal of Human Resource Management*, 10(6): 1031-45.
- Delaney, J. T., and Huselid, M. A. 1996. The impact of human resource management practices on perceptions of organizational performance. *Academy of Management Journal*, 39: 949-969.
- Fisher, C. and Dowling, P. J. 1999. Support for an HR approach in Australia: The perspective of senior HR managers. *Asia Pacific Journal of Human Resources*, 37(1): 1-19
- Guest, D. 1990. HRM and the American Dream, *Journal of Management Studies*, 27(2), 377-397
- Hall, L. and Torrington, D. 1998. Letting go or holding on -The devolution of operational Personnel Activities. *Human Resource Management Journal*, 8: 41-55.
- Hope-Hailey, V., Gratton, L. McGovern, P. Stiles, P. and Truss, C. 1997. A chameleon function? HRM in the '90s. *Human Resource Management Journal*, 7(3): 5-19.

- Huselid, M. A. 1995. The impact of human resource management practices on turnover, productivity, and corporate financial performance. *Academy of Management Journal*, 38: 635-672.
- Laabs, J. 1992. HR adds value to Board of Directors. *Personnel Journal* 71(11): 12-21.
- Martell, K. and Carroll, S. J. 1995. How strategic is HRM? *Human Resource Management*, 34(2): 253-267.
- O'Shannassy, T. 2004. Strategic thinking and strategic planning to optimize organization performance. Paper presented at the 18th Annual Conference of the Australian and New Zealand Academy of Management, Dunedin, New Zealand.
- Pfeffer, J. 1994. *Competitive Advantage through People*, Boston: Harvard Business School Press.
- Richard, O. C. and Johnson, N. B. 2001. Strategic human resource management effectiveness and firm performance. *International Journal of Human Resource Management*, 12(2): 299-310.
- Schuler, R. and Jackson, S. Eds. 1999. *Linking Competitive Strategies with Human Resource Management Practices*. Strategic Human Resource Management, Blackwell Publishers.
- Schuler, R. S. 1992, Linking the people with the strategic needs of the business. *Organizational Dynamics* Summer: 18-32
- Sullivan, J. 2003. Knocking down the silos. *Human Resources*: 16-18.
- Tabachnick, B.G., and Fidell, L.S. 2001. *Using multivariate statistics (4th ed.)*. Sydney, Allyn and Bacon.
- Teece, D. J., Pisano, G. and Shuen, A. 1997, Dynamic capabilities in strategic management. *Strategic Management Journal*, 18(7), 509-534
- Teo, S. 2000, Evidence of strategic HRM linkages in eleven Australian corporatized public sector organizations. *Public Personnel Management*, 29(4): 557-575
- Teo, S. 2002. Effectiveness of a corporate HR department in an Australian public sector entity during commercialisation and corporatization. *International Journal of Human Resource Management*, 13(1): 89-105.
- Ulrich, D. 1997a. *Human Resource Champions: The Next Agenda for Adding Value and Delivering Results*. Boston, MA, Harvard Business School.
- Ulrich, D. 1997b. Measuring human resources: an overview of practice and prescription for results. *Human Resource Management*, 36(3): 302-320.
- Ulrich, D. 1998, *Delivering Results: A New Mandate for Human Resource Professionals*, Boston, MA: Harvard Business Review.
- Wright, P. M., Dunford, B. B. and Snell, S. A. 2001, Human Resources and the resource based view of the firm. *Journal of Management*, 27: 701-721.
- Wright, P.M., Gardner, T.M., Gerhart, B., and Delery, J.E. 2001, Measurement error in research on human resources and firm performance: Additional data and suggestions for future research. *Personnel Psychology*, 54: 875-901.
- Wright, P. M., Gardner, T. M. and Moynihan, L.M. 2003, The impact of HR practices on the performance of business units. *Human Resources Management Journal*, 13(3): 21-36.
- Wright, P. M. and McMahan, G. C. 1999. Theoretical Perspectives for SHRM in Schuler, R. S. and Jackson, S. E. (Eds) *Strategic Human Resource Management*, Oxford: Blackwell Publishers Ltd.

Table 1: Multiple regression analysis of independent variables on firm financial performance

	Standardized regression coefficient
Strategic HRM alignment	.48**
Documented HRM strategy	.27
Committee membership	-.22
Line management devolvement	-.07
Line management training	-.34*
Line management training X devolvement	.30*
Firm size	.04
Service industry	.24
Adjusted R ² (explained variance)	.24

* p < .05. ** p < .01.