4.1 Introduction

Strategic human resource management (HRM) emerged as a consequence of globalization of economy resulting in increased global competition, the demand for cost optimisation and increasing skill shortages. This led to the recognition that the management of people needs to be a high priority area if organisations are to achieve their business objectives (Mello 2006). Strategic HRM has gained significance as a tool for achieving sustainable competitive advantage. Strategic HRM links strategic planning and HRM in a way that the organisation’s objectives are determined and personnel policies and practices aligned with those objectives (Tompkins 2002). Strategic HRM involves the development of a consistent, aligned collection of practices, programs (strategies), and policies to facilitate the achievement of the organization’s strategic objectives (Mello, 2002). Strategic HRM studies in the global context have shown that implementation of strategic HRM practices have led to improved performance both in financial as well as non-financial terms (Chanda and Shen 2009). United States’ General Accounting Office in their draft ‘Model for Strategic Human Capital Management’ issued in Mar 2002 stated “People are an Agency’s most important organizational asset. An organization’s people define its character, affect its capacity to perform, and represent the knowledge-base of the organization. As such, effective strategic human capital management approaches serve as the cornerstone of any serious change management initiative.”

This chapter reviews the available literature relevant to this research. The review consists of four major parts. The first part reviews some fundamental concepts of strategic human resources management. The second part reviews the concept of performance advantages and relevant theoretical approaches to it. The third part summarises the strategic aspects of HRM practices which are significantly correlated to the performance of the company. The fourth part looks at the strategic HRM studies in the Indian context.

4.2 Strategic HRM: Fundamental Concepts

Boxall and Purcell (2003, pp. 28) in a discussion on strategic choice argue that “it is possible to find strategy in every business because it is embedded in the important choices managers and
staff of the firm make about what to do and how to do it”. Strategy is directed towards maintaining the viability of the organization and/or producing sustained advantage in the markets in which the organization exists. A key issue to be resolved is how Human Resources Management (HRM) plays a part in influencing the direction and shape of the evolving strategy. Furthermore, if HRM is considered an integral part of the process of strategic choice, how does it influence the strategic outcomes? Strategic HRM, as business strategy, might be seen as contributing to strategic choice by either maintaining viability or producing a sustained advantage.

The term ‘strategy’ is used to explain both the processes (e.g., organizational restructuring) and the outcomes (financial and non-financial performance) of chosen long-term directions. It can be either a conscious, planned activity or a series of activities leading to desired objective. Gronfeldt and Strother (2006) define strategy as “a pattern or plan that integrates an organisation’s major goals, policies and action sequences into a cohesive whole“. Go´mez - Mejia et al. (2004) define strategy as the grand plan adopted through employees, to help realise the business mission. Corporate and business level strategies evolve into HR plans (Bratton and Gold 2007) so that HR policies are built from well-designed personnel practices that fit into the corporate business strategy. strategic HRM is concerned with ensuring a strategic ‘alignment’ or ‘fit’ between business and HRM strategies, necessarily involving an evaluation of the likely impacts of both the external and internal organizational environment, the long-term goals of the organization and the ways in which HRM strategy will enable the adaptation of human resources towards realising these goals.

Human resources play a strategic role in formulating policies and practices to support organisational objectives. Based on an analysis of an organisation’s internal and external environments and the strategic objectives, HR objectives and strategies are developed. HR objectives are aligned to the organisational objectives to achieve vertical as well as horizontal alignment. HR functions that are strategically aligned benefit organisations and employees alike by improving commitment, work satisfaction and performance (Cascio 2006). An integrated personnel program with consistent interrelationships ensures policies and practices in one functional area do not work at cross purposes with those in other areas (Fisher et al. 2006).
Strategic HRM emphasizes the need for Human Resource (HR) plans and strategies to be formulated within the context of overall organizational strategies and objectives, and to be responsive to the changing nature of the organization’s external environment. Nankervis et al. (1999) argue that strategic HRM approach checks likely impacts of both the external and internal organisational environments against the long term goals of the organisation and adapts the human resources to meet these goals. This means HR professionals need to expand their competencies to include business, finance, strategy, and management of change processes for them to, according to Professor David Ulrich’s model, “become a partner with ... line managers in strategy execution, become a champion for employees, become an agent of continuous transformation” (Nankervis et al. 1999). Strategic HRM model requires interpretation and adaptation by practitioners to ensure the most suitable fit between HR and business strategies and plans. Thus, the overall themes of strategic HRM are the integration of all HRM functions to broad organizational goals, and responsiveness to the external environment.

When linking HRM with the business strategy, the organisational policies and practices should align with the vision and mission statements. Linking human resources to the strategic vision is crucial to establish linkage between strategic intent to employee behaviours (Gratton 1994). In strategic terms the vision helps the organisation to know where it is heading and why it exists and who the customers are and sets the basic directions and strategies to get there. Strategic HRM needs to be aligned with the vision and mission as part of the organisational strategy (Kenny 2005). Mill more et al. (2007) describe organisation structure as another factor influencing strategy formation, as this depicts the working relationships that affect how strategic HRM is implemented. The organisational structure has inherent features which influence the implementation of strategic HRM, and structural changes may be required to gain the full benefits of strategic HRM.

4.3 Strategic HRM Models

Several models depicting strategic HRM have been suggested by scholars. Some authors have viewed HRM model as soft or hard. Beardwell and Clark (2007) suggest that central to the soft approach to HRM is enhancing employee commitment and communication. According to Nankervis et al. (1999), soft HRM approach seeks the involvement of employees through consultation and empowerment. Hard HRM seeks to manage human resources as a factor of
production like any other factor of production (Storey 1992). Beardwell and Clark (2007) suggested that hard HRM represents objective measures emphasising the strategic role human resources play in achieving organisational goals. Nankervis et al. (1999) further argue that key goal of HRM is to ensure that organisations have the “right numbers, types, and skill mixes of employees at an appropriate time and cost to meet present and future requirements”. This calls for effective strategies for attracting, selecting and keeping employees productive, satisfied and motivated to contribute to the organisation’s progress.

The Michigan Business School model (Fombrun et al. 1984), which aligns to ‘hard’ HRM theory, identified selection, appraisal, development and rewards as the key elements of HR. This approach combines the four traditional functions (recruitment and selection, appraisal, compensation and development) with performance to form the strategic HRM-Cycle (Fischer and Weitbrecht 1995). Pfeffer (1994) has suggested that strategic integration of these elements will lead to improved performance. Critics of the Michigan model claim it is inhuman as employees have no say in decisions and power is in the hands of managers.

The Harvard model recognises the presence of different stakeholders, such as employees, government and the community. The interests of these different stakeholders differ from that of the organisation (Beer et al.; 1984). The Harvard model emphasises the soft side of HRM.

Guest (1989) proposes another model that incorporates the concepts of strategic integration, high commitment, high quality and flexibility in an attempt to ensure a balance between hard and soft HRM. Lundy and Cowling (1996) and Storey (1997) argued that line managers in an organisation are crucial to the effective delivery of HRM policies. The five key activities of HRM—staffing, retention, development, adjustment and managing change demand shared responsibilities between line and HR managers. There is considerable evidence in the literature that employees will be at their best if they are fully committed to the organisation. Armstrong (2000) has suggested that employees high commitment is produced from self-regulation rather than a response from external pressures.

A typical model practiced in the industry views strategic HRM as a process that links strategic planning and human resource management by determining vision-related objectives and aligning HR policies and practices with the objectives. Nankervis et al. (1999) have identified
major themes of strategic HRM in this model. The model shows that HR needs to operate at three levels; the strategic level (HR strategies - involvement in corporate and human resource planning), the operational level (HR planning) and the functional level (HR functions - involvement in activities that ensure employees are in the right place at the right time and for the right cost). The three levels of the model are discussed below.

4.3.1 Strategic level
Three steps to HR strategy formulation and implementation are a) identifying the nature of alignment required with business strategy b) developing and implementing appropriate HR strategies and c) continuous evaluation of the strategy. Cascio (2006) considers the HR strategy as the prioritisation that aligns the human resources policies, and programmes with the strategic business plan. Since strategic HRM approach involves evaluating the likely impacts on the organisation of both the external and internal environments, the organisation’s long-term goals, and the ways in which HRM strategy will help adapt human resources to meet these goals, HRM strategy will differ across organisations. Tompkins (2002) has identified five categories for implementing human resource strategy namely a) cost containment strategy b) performance management strategy c) involvement strategy d) retention strategy d) investment strategy (investing in training and development) and e) cohesion strategy (strategies for establishing a sense of community and social bonds). These various strategies can be applied individually or in combination, depending on situational factors, such as the industry type and the business priorities.

4.3.2 Operational level
Strategic HR planning maps out strategies about the type of employees required for the future and the essential skills and training needed to enable the organisation achieve set goals. The HR planning process considers long, medium and short-term HR strategies and modifies functions, such as recruitment, training, development, career management and employee separation, to match employee demand and supply forecasts such that relevant objectives can be met (Nankervis et al.; 1999).

4.3.3 Functional level
The human resources functions can be grouped into the five major areas of staffing, retention, development, adjustment, and managing change to achieve organisational goals. The functions are
shared by the HR department and line managers. The HR department is responsible for implementing the HR functions, unless of course it is a very small sized organisation where numbers sometimes don't substantiate a dedicated HR department (Noe et al. 2007).

4.4 Strategic HRM and Firm Performance

The strategic HRM since the 1990s has emerged as the predominate paradigm for HR research. During this period the concept of grouping together of human resource practices attracted many researchers. Ferris et al. (1990) in their study of over 2,236 U.S. firms in construction industry observed that HRM functions positively influenced the firm performance. Cutuher-Gershenfeld (1991) concluded that transformational labour-management relations were associated with higher levels of organisational performance. Mac Duffie (1995) in his survey of 62 automotive companies found that HR practices influence firm performance as a bundle rather than as individual standalone HR practice. Huselid, (1995) concluded that high performance work practices are linked with higher financial performance, lower employee turnover and higher productivity. Delaney and Huselid (1996) observed that firm performance was associated with HRM practices such as training and selection. In a subsequent study Huselid, Jackson and Schuler (1997) concluded that there exists a significant correlation between HRM practices and market value of the firm, employee productivity and cash flows (Boxall and Macky 2009).

Effective strategic HRM practices provide competitive advantages and improved performance because it aligns the human resource functions of recruitment, selection, performance appraisal and management, reward and compensation and developing employees to the organisation’s goals (Pfeffer 1994; Lundy and Cowling 1996; Armstrong 2000). Unlike traditional personnel management, where the personnel functions of employee are performed without integration with overall organisational objectives, strategic HRM assumes that all personnel activities are integrated with each other, and at the same time strategically linked with organisational objectives (Nankervis et al. 1999). The main focal areas of strategic HRM include quality, customer service, productivity, employee involvement, workforce flexibility and teamwork. Policies that support mutual goals, respect and responsibility elicit commitment to produce better performance (Armstrong 2003).
Nankervis and colleagues (1999) argue that personnel management relates to the people related functions or activities of recruitment, selection, training, salary administration and industrial relations. People related activities are integrated with each other and with the strategic organisational objectives. A fundamental belief and assumption of HRM is that human resource more than other factors of production, make the difference in organisational growth. To realise the benefits, managers should be encouraged to put people first (Burke 2006) as the management of people is a key factor in bringing about a competitive edge (Lengnick-Hall and Lengnick-Hall 1990). Human resources, through their efforts, knowledge, capabilities, resources, relationships and decisions can place an organisation ahead of its competitors (Prahalad and Hamel 1989). The central principle of HRM is the effective utilisation of employees to achieve organisational objectives. An organisation is said to have competitive advantage over its competitors when its products or services cannot be easily imitated or copied (Bernardin 2007). Beardwell and Claydon (2007) have opined that the value of human resource lies in its ability to develop and exploit rare characteristics, the ability to develop and nurture characteristics that competitors cannot easily copy and the ability to better coordinate the organisation’s policies and practices.

Many authors question the underlying philosophies and practical applications of HRM models. Similar concerns are raised about strategic HRM; its managerial focus, strategic perspectives and ‘realities’ of HR practice have been questioned by several writers (Legge 1995; Guest 1997). Strategic HRM is certainly concerned primarily with contributing to the ‘bottom line’ success of an organization. The strategy concept has developed as an important aspect of management since the dynamics and complexity of the world and business environment have increased. It is evident that the various schools of theory are incomplete.

4.5 HRM Practices and Strategy

Various HRM practices can be broadly classified into five categories, a) recruitment and selection, b) training and development, c) performance management, d) rewards and compensation and e) employee relations. These practices in relation to strategy have been adequately discussed in the literature and are summarized below.
4.5.1 Strategic Recruitment
The essence of strategic recruitment and selection is to ensure that both current and future strategic needs of skills and experience are met so the organisation can adapt to its internal and external environments. Another feature of strategic recruitment and selection is to align and integrate this function with the strategic processes, mission statement and values so these match the attributes demonstrated by potential employees. Having a good fit between the personal attributes of the employees and the organisation’s goals lays the foundation for success in the long term (Millmore and Baker 1996). The strategic recruitment and selection criterion based on the employee attribute is referred to as person-organisation (P-O) fit, which is defined as “the compatibility between specific individual attributes and comparable organisational attributes” (Higgins 2002). A good fit with the P – O selection model supports higher employee satisfaction. According to Cascio (2006; p244), “a close fit between individual strengths and interests and organisational and job characteristics almost guarantees a happy marriage”.

4.5.2 Strategic development
The aim of strategic training and development is to create and implement a career development program that benefits both the organisation and the individual (Nankervis et al. 1999). Training and development involves programmes designed to positively enhance/change current knowledge, skills, attitudes and/or social behaviours to improve future performance at the individual, group or organisational levels. Strategic training and development begins with induction, training and development and continues throughout employment with the organisation. Strategic Human Resource Development (SHRD) aims to ensure that individual experience, attitudes and values are utilised to promote effective performance for the present and future critical operational as well as strategic management tasks (Kiggundu1993; Noe et al. 2007). A pro-active approach to development of employees in line with the strategic needs of the organisation should be adopted for better outcomes Analoui (2007).

4.5.3 Strategic performance management
The process of performance management aims to improve individual’s efficiency and effectiveness by providing a feedback loop. The organisation can utilise the results of the performance appraisal for the entire range of HRM activities (Bohlander and Snell 2007) such as, decisions on employee’s working conditions, promotions, termination and rewards.
Performance management includes outcomes and targets as well as the strategic competencies employees need. Aligning the appraisal and performance management practices with the organisations objectives is what makes it strategic. The process becomes the key to employee development and improved employee performance (Gomez-Mejia et al. 2004).

4.5.4 Strategic rewards
Strategic reward is defined as “the deliberate utilisation of the pay systems as an essential integrating mechanism through which the efforts of various sub-units and individuals are directed towards the achievement of an organisation’s strategic objective” (Gomez-Mejia and Balkin 1992). A reward system is designed to align organisational objectives and individual expectations. Reward systems aligned to achievement of strategic objectives aim to attract, retain and motivate the workforce. Organisations are under an obligation to reward and compensate their employees with pay (Heneman and Judge 2003). The strategic objectives of remuneration are to reward past performance, remain competitive in the labour market, motivate future performance, attract and retain good staff and reduce staff turnover (Leopold, Harris and Watson 2005).

4.5.5 Strategic relations
Pfeffer (1995) observed that employee participation and involvement can positively influence performance as they increase job satisfaction and productivity. Kling (1995) further suggested that employee involvement reduce absenteeism and turnover problems. Banker et al. (1996) suggested that employee involvement in business strategy can be achieved through forming cross-functional teams, participation in decision making process and quality improvement programmes and establishing formal feedback mechanism.

4.6 Strategic HRM Studies in Indian Context
Most research in the strategic HRM has been conducted in Western contexts. Budhwar and Sparrow (1997) and Singh (2003) and more recently Chanda and Shen (2009) are some of the studies in the Indian context relating to the strategic HRM practices and their association with firm performance.

Since the beginning of 1990s, India has gradually liberalised its economy with reforms in the public and private sector, banking and financial sector, and foreign investment policy. Increased
globalisation and liberalisation of economy has had an impact on the HR function of domestic companies to develop their workforce to compete globally. Economic reforms have made a profound impact on the business environment in India and people are recognized as one of the greatest resource that can play a strategic role. Indian companies have responded positively with changes in priority of the HRM function from routine HR activities towards a strategic approach. More recently, India has capitalized on its large pool of educated, English speaking, people to become an important outsourcing destination for multinational corporations. India has also become a major exporter of software as well as financial, research and technological services (Chanda and Shen, 2009). Many scholars and researchers (Budhwar and Sparrow 1997; Krishna and Monappa 1994; Venkata Ratnam 1995) firmly believe that the liberalization of economic policies in India is bringing an increasing level of competition.

With liberation and increased global competition there have been concerns for quality, re-skilling and de-skilling of the work force, cultural changes, mixed workforce, and issues related to workforce rightsizing (Venkata Ratnam 1995). Liberalisation has created HRM issues associated with strategic expansion, diversification, turnaround and internalisation (Ahluwalia 1994; Sodhi 1994). All this has direct implication on how people are managed in Indian firms (Krishna and Monappa 1994). Jain (1991) and Jain and Venkata Ratnam (1994) have argued that this becomes all the more challenging due to diverse socioeconomic background of Indian workforce and the antagonist nature of trade unions makes it difficult to make them work as a team. Technological edge supported by a talent pool has become a crucial factor for survival in the market especially for small scale companies in the IT services sector. Chanda and Shen, (2009) in their study report ‘HRM and Strategic Integration’ maintain that HR managers are now seen often performing the role of motivators for their knowledge workers to adapt to changes in business environment. One of the biggest challenges for the HR managers in the small IT firms has been attracting the talent and retaining them. Attrition levels have been high especially in the IT services sector. There is increased level of poaching and attrition between organizations. In the IT industry, the average attrition rate is 30-35 per cent and could increase to 60 per cent. This is more pronounced in small IT companies. HR managers have to continuously keep on their toes to bridge the gaps created by attrition as well as recruit for the growth. High attrition rates result in a shifting workforce adversely affecting the consistency in performance and keeping
motivation levels high. Thin not only leads to manifold increase in recruiting and training costs but also affects quality and revenue adversely.

Chanda and Shen, have further argued that Indian firms are seen to be over manned and less efficient and place more emphasis on talent acquisition strategies. Management in these firms is adopting measures to reduce costs by rightsizing the workforce and making them efficient. Recruitment has become a major function from an imperative sub-system in HR, particularly in the knowledge industry such as IT. Human resources managers play a vital role in creating assets for the organization in the form of quality manpower. Attracting new talent is a top priority for software companies. Another challenge for HR managers is to put systems in place to make the people a perfect fit for the job. There are number of recruitment and selection practices in Indian organizations for both white and blue collar employees.

There are different ways in which compensation is practiced in Indian organizations such as: (A) seniority or work experience based; (b) performance based (c) skills or competencies based and (d) a combination of the first three practices. There are some findings that suggest Indian firms adopt a skill or competency based approach to reward their employees, as indicated in the emergent Indian literature. However, lifetime employment and seniority-based pay are still very much prevalent in Indian organizations (Venkata Ratnam 1995). Ramaswamy and Schiphorst (2000) have observed that as an outcome of a mixture of Indian cultural values and legal requirements, there are organisations which are still unable to move from compensation based on work experience to performance based compensation packages. It seems that a subtle transition is taking place away from seniority-based towards performance based pay in India especially in the white collar industry.

To overcome the problem of retention and building competitiveness, many organizations give utmost priority to training and skill enhancement programmes. A significant number of managers in organizations are trained in various areas such as performance appraisal, communication, delegation, motivation and team building. These developments point to an increased importance of employee development in Indian organizations (Budhwar 2000). Indian organizations put emphasis on annual career development interviews for the training and development of their employees. Sharma (1992) has observed the presence of in-house training and development
facilities in many Indian organizations. The adoption of formal career plans, annual career development interviews, assessment centres, succession plans and planned job rotation depict the existence of a structured training and development system.

Indian organizations share less information related to both strategy and financial performance with their staff in comparison to managerial staff. There can be a number of explanations for this. First, senior management does not have much faith in subordinates (Sparrow and Budhwar 1997). Second, Indian managers prefer centralized decision making, practice tight control and do not like to delegate authority (Sharma 1984; Tayeb 1987).

Indian research in various sectors (Rao 1994) has shown significant differences in the pattern of HR practices in India. Sharma (1992) highlights the comparison of public and private sector organizations and observes that less money is spent, less training is given and fewer employees are trained in public sector organizations than private ones. According to Singh (2000), some of the studies which have tried to focus on the relationship of HRM to firm performance have shown a low to moderate relationship between human resource practices and business performance. Singh (2004) conducted a study on 82 Indian firms indicating that there is a significant relationship between two HR practices namely, training and compensation and perceived organizational and market performance of the firms.

The literature on internal labour markets highlights the need for HRM practices to be consistent with a systematic and rationalized employment system (Osterman 1994). There is plenty of evidence regarding the existence of structured employment systems in developed Western countries, for example, the United Kingdom (Gospel 1992). However, there is much less research evidence for Indian organizations. Nevertheless, there is evidence regarding the provision of limited benefits and the existence of simple rudimentary pay systems in Indian organizations. Moreover, rules regarding practices such as recruitment, training, promotions and lay off are ad hoc in nature and are subject to easy manipulation by employers (Venkata Ratnam 1995). Further, recent research highlighted that Indian organizations tend to be significantly more hierarchical (Rao 1994). Senior managers in Indian organizations make fewer decisions in conjunction with their subordinates (Tayeb 1987). Although general studies of HRM in India have been conducted, there is limited body of literature on comprehensive
research on HRM practices and their strategic linkage to business performance of the organisation.

The onset of a burgeoning competitive service sector, especially the IT and IT enabled services, compelled a demographic shift in worker educational status and heightened the demands for job relevant skills as well as regional diversity. As a result, there has been a marked shift towards value enhancement of HR in Indian organizations as they become increasingly strategy driven (Chatterjee 2007). It is also observed that HR’s significance is being emphasized as a competitive advantage in industries like Software Services, IT Enabled Services, pharmaceuticals, and biotechnology (Khandekar and Sharma 2005).

4.7 The Gap

Given the striking cultural and institutional differences, whether Western HRM concepts are generally applicable to non-Western economies remains a matter of conjecture and is a growing topic of research in many parts of the world. In India, in a recent study conducted by Chanda and Shen on the HRM strategic integration in a large sample of companies concluded that a fit between HRM and strategic integration is indeed improving organizational performance. Most research in the strategic HRM has been conducted in Western contexts. Little has been done in developing economies such as India. There is limited or no body of literature available with regard to small scale IT services sector. A study of the extent to which strategic HRM practices are implemented in small IT companies will help understanding how these practices are correlated with the business outcomes of the firms. It will, therefore, make a very useful topic of study, one, which has not been attempted before.

4.8 Conclusion

This chapter reviewed the relevant literature. A large number of studies have been conducted on strategic HRM and their alignment with business objectives. However, there are very few such studies available in Indian context. In this backdrop of paucity of research in Indian context especially in the small scale IT industry sector, this study is considered important and pioneering. There are several reasons why an analysis on HRM policies and practices and levels of linkage to operational efficiencies are needed. First, the recent HRD practice in India emphasises the need for increased levels of integration between strategy and people management. Second, most
studies which have analyzed the phenomenon of HRM and business strategy integrations have been undertaken in developed nations. Thirdly, in liberalised global economy, it is essential to remain viable and competitive to survive. Fourthly, HRM practices when implemented with strategic intent tend to keep the employees satisfied by way of involvement, appropriate rewards, performance management and appropriateness of recruitment and development all linked to the strategic vision of the company. Fifthly, the body of literature available in Indian context is almost non-existent. The scarcity of research on integration of HRM with business strategy and its contribution to organizational performance in the context of small scale IT companies in India makes for an important topic for study.