

Financial Intelligence from The Human Resources Point: A Conceptual Framework

İnsan Kaynakları Açısından Finansal Zeka: Kavramsal Bir Çerçeve

Tamer KEÇECİOĞLU¹, Muzaffer HIÇYILMAZ²

ABSTRACT

Human resources functions is in a physiological trauma as it has been moving away from administrative duties to focusing on strategic management roles. Underlying this trauma is the desire of the professional human resources managers to gain more respect and recognition within their organizations as strategic partners with others from this stand. The common denominator of recognition and respect is being equipped with financial intelligence. To understand the contribution of human resources to the financial performance of the company, and to interpret this rightly with human resources point of views is also a reality which is stressed by the shareholders. In this work, first, the literature on the subject is studied, then a definition of financial intelligence from the view of the human resources managers who wants to be a partner is attempted to be made and the significance of human capital is tried to be analyzed by looking at some ratios.

Keywords: Human resources, financial intelligence

ÖZET

İnsan kaynakları fonksiyonları yönetsel görevlerden stratejik iş girişimlerine doğru gelişen bir odaklanma eksenindeki kayma nedeni ile psikolojik bir travma yaşamaktadır. Travmanın olası nedenlerinin altında insan kaynakları profesyonellerinin örgütleri içerisinde stratejik iş ortakları olarak artan ölçüde saygı ve tanınma isteği yatmaktadır. Saygı ve tanınmanın ortak paydası finansal zeka ile donatılmış bakış açıdır. İnsan kaynaklarının sundukları ve sonuçlarının şirketlerin finansal sonuçlarına yönelik etkisi insan lensi ile doğru biçimde yorumlamak bu ortak paydanın altını doldurmanın yanında paydaşlar tarafından dayatılan bir zorunluluk haline gelmiştir. Bu çalışmada ilk olarak bu konuda yazılmış literatür taranmış, iş ortağı olmak isteyen insan kaynakları yöneticisi açısından finansal zekanın tanımlanması, insan sermayesinin önemi, sayıların gücü ve örnekler verilerek anlatılmıştır.

Anahtar Kelimeler: İnsan kaynakları, finansal zeka.

1. INTRODUCTION

Do human resources (managers) need to possess financial intelligence because of their contribution to work and financial results of the company? Many studies have been made in order to determine the relationship between human resources applications and work results (Devanna, Fombrun, Tichy, 1981; Dyer, 1984, 1985; Fombrun, Tichy and Devanna, 1984). Susan Nkoma attempted to test how much investment companies should made in human resources planning process and the contribution to company results of such investment (Nkomo, 1986, 1987). Randall Schuler and Susan Jackson attempted to analyse how human resources management showed differences under various strategies by a cross-company study (Jackson, Schuler ve Rivera, 1989; Schuler and Jackson, 1987; Schuler, 1983). Relationships between investment in human resources and education (Russell, Terborg and Powers, 1985), selection and choice for work (Terpstra and Rozell, 1983), evaluation

of performance (Borman, 1990) and wages (Gerhart and Milkowich, 1992) were tried to be determined. Ulrich (1997) tried to show how investment in human resources contributed to the market values of the companies and their financial results, and in consequence to company performance. Bhattacharya and Wright (2004) proposed to the firms that human resource (management) is an asset that contributes value and competition advantage as well as patterning to develop a logic that goes with the uncertaintyaccompinizing human resources management. Historically, the human resource department was tactical in nature. Its job was to ensure that hiring and firing were done properly, that labor laws were followed. Over the past decade, however HR has begun to transform itself. Schneider (2006), states that "your driver is to increase human productivity by human resources management and strategies and then to change the DNA's of human resources".

¹ Assist. Prof., Ege University, Faculty of Economics and Administrative Sciences, Department of Business Administration, tamer.kececioglu@ege.edu.tr

² Lecturer, EgeUniversity, Faculty of Economics and Administrative Sciences, Department of Economics.

Weiss (2004) argued that in the process of putting forward the capabilities of human capital at present, it is also believed to indicate the required future capabilities of human capital metrics, but not sufficient attention is being given to the importance of such metrics. Bassi and McMurrer(2007)observed the maturity levels in human capital studies and tried to establish a relationship between corporate share profits and the maturity levels in financial companies. Harding and Rouse (2007) showed that mergers and acquisitions generally fail because of the matters of corporate cultural differences, and there occurs a need of working in cooperation with financial and human issues together.

Murphy and Zandvakili (2000) argue that the relations between customers and employees should be established, and contribution to sales and increase in profits should be understood and this work should be done continuously. Schiemann (2005) developed a new paradigm under the concept of human justice in stressing the maximization of return of human capital and specifically the work strategy of the workforce, capabilities, skills, knowledge and all other resources.

Human resources managers with financial intelligence should be aware of the power of ratios, return on investment and deal with metrics. In order to better analyse, he (she) must be able to read balance sheets, income and cash flow statements, and must establish the relationship between the financial statements and human factors. In their work , which has been analyzing how analytical competition would be shaped in the future, Davenport and Harris (2007:184) stress the prediction of the future, referenced points in analytical competition, re-examination of work strategies and their continuous tests as well as that their support to sustainable distinct capabilities by focusing on both the human and technological factors. More important, such work should aim the ways to better performing than the competitors.

2. RELATIONSHIP BETWEEN FINANCIAL INTELLIGENCE AND HUMAN CAPITAL

It is important to know how to measure the financial successes of the employees and how these will affect the overall performance of the organization. To understand this approach is what we call "financial intelligence". This concept is specially significant for those who claim to be human management professionals such as advisers, business leaders who intend to become business partners as well as in order to have employee loyalty and to make them part

able in business success. Success in today's business world is possible only with organizational strategies and the realization of personal objectives. The concept of progressing a unity covers being a part of the organization and realization of where the organization has moved, and his (hers) contribution and his (hers) show in these efforts. Why is profit not the same cash coming in? Some reasons are pretty obvious: cash may be coming in firm loans or firm investors, and that cash isn't going to show up on the income statement at all. Financial intelligence gives a significant responsibility to the future human resources managers and is also important for gaining respectability for such managers and giving them a states for undertaking the role of strategic data lists. Unfortunately, the behavior (standing) of today's behavior of human resources managers towards finance is blurred. Uncertainty prevails in the financial aspect of a business and sales explanation of financial results. There exist problems in understanding human factor and the financial aspect of the organization together. To talk financially and to talk about contribution to organizational strategy should be under the same framework. We can break this degree that human resources management should be concerned only with the human factor by financial intelligence. Human resources management should have a good understanding of the basics of financial measurements, their analysis and the interrelationship of the financial results with the competitive environment, changing customer requirements and the overall economy. All of these constitute financial intelligence. Human resources management analyses the job, it does with the financial consequences of such work. It is important to answer the question whether the human resources management work tenders measurable value to customers and shareholders. A study carried out in 2006 by the Center for Effective Organization of the University of Southern California found that 9% of human resources managers were all to see the connection between human capital, management and organizational performance (Lawler et.al., 2006:21-22). From the point of human capital management, business profitability lies in the production of goods and services that satisfy customer requirements better than the rivals. This also renders sustainable profitability (Pralhad and Hamel, 1990). In the concept of human capital a narrowing down and deepening takes place. This tendency is closely linked with strategic direction. Strategy is the system which contributes mostly to better performance of the employees. The creation of more

value added to shareholders relative to competitors constitutes the foundation of the systems, and this should be taken as the starting point of financial intelligence- its comprehension proof and interpretation. Overall, if a manager's job is to boost profitability, he or she can a positive effect on the balance sheet, just because profits increase equity. The pioneering study on the relationship between company performance and human resources application was carried out by Becker and Huselid (1998). They found out that human resources principles, which firms have been using, could help the firms for acquiring the highest market share per employee- thus, this shows the importance of human resources management on the market value of the company. Financial metrics help developing human resources more efficiently (Boudreau and Ramstad, 2006 and Lawler et.al.,2004). Human resource management in need of metrics and their analytical viabilities become pioneers in making human resources management a strategic partner. It is, therefore important that financial intelligence exists in making decisions about human. Boudreau ve Ramstad (2006) stressed the importance of four factors: logic, analysis, measurement and process. Measuring systems which have been developed has largely answered the question. Why do firms spend effort on the question of "effectiveness?" (for example, effects of different capability goals on organizational betterment).

Studies done has shown that in the measurement of effectiveness motives and analysis one handly used, less than 40% of organizations use measurements of effectiveness and effects (Lawler, 2006:72). The measurement of financial effects of human resources management activities is especially important for financial intelligence-this involves putting together human resource management costs and their analysis. Financial intelligence is very important in determining strategies concerning human resources management. Human resource management should be able to read and understand company's revenues, balance sheets and cash flows. In recent years a change is observed in the tactical and strategic approaches of human resource management. Specifically professionals in human resources management have deepened their experience in organizational development and ability management that go together with their strategies (Beatty, et.al., 2003).

Human resources management is required to partake in related discussion and decision and to understand the business. These requirements carry the knowledge of the business, management of change,

establishment of relations and management of partnership observations on and a critique of company strategies; and their correspondence with the financial picture offers great opportunities to managers with financial intelligence. In the past, development sustainability of competitive advantage were based on high cost and products. However, customers should be offered more persuasive arguments than these in order the company to survive. The best work on this is the book written by Jim Collins (2001). The book explains how some companies maintain their success for long periods of time. Such firms' common denominator is human and perfection in organizational capabilities. This perfection is achieved by human capital. Some reasons why human resource managements should have financial intelligence are most commonly a major part of operational expenses on human capital; increases in the name value of companies in recent years (Bryan, 2007); the observation that especially in labour-intensive concerns, some little improvement in labor productivity returning as great financial gains (Barber, et.al., 2005:56).

The differentiating variable in sustainable work performance is the correct management of the human resources. The betterment of this potential and its measurement, which is a must for competitive advantage, constitutes the base of financial intelligence.

3. POWER OF RATIOS

There exist many ratios that help human resources managers to make decision on various matters. Having acquired the knowledge concerning the business, these ratios must be used to assess their effects on the business and they must be interpreted correctly: revenue per employee, total expenditures on per employee, wages as a percentage of revenue, costs of extra benefits to employess as a percentage of expenditures; percentage of such extra benefits in the total personal expenditures and training per hour for each employee. All these ratios can be calculated from the income statements. To establish a trend, it is also useful to look at the sales in time for instance. Within a region or in every individual sales, outlet percentages of total sales and percentages of sales on a product basis should be followed. Such percentages give much more knowledge to managers than sole raw figures. These percentages concern sales after the human resources managers' information and enable to follow up the expenses incurred for sales purposes and for investment in workforce. The managers should be able to interpret how human matters could increase or decrease the

sales and how they should be interpreted and what measures should be the talents. The full-time equivalent (fte), which is used frequently in ratios, represent the total effect hours of the employees. Various employment forms, such as full-time, seasonal, temporary and trainee schemes, thus converted into a single unit and consistency is secured. This is also important to observe the productivity of the workforce and its effectiveness in a comparative frame. It is useful to determine the number of workforce within the institution. How the workforce should be related to the working capacity is a basic indicator for the performance of human resources. It is used to measure always productivity in time and also the productivity of departments. It is essential that an understanding of financial tables is a must and it is the beginning of the way to financial intelligence.

Two ratios, labour cost/fte and revenue/fte which constitute the structural costs of the organization, gives labour cost/revenue ratio. According to Pricewaterhouse Coopers, this ratio was 22.1 percent in the years 2009-2010 (PricewaterhouseCoopers, 2009:10). This percentage rears for each dolar revenue 22 cents is spent on labour cost. This ratio, of course, change from sector to sector, for example it is about 40 cents for hospitals and professional services, and less than 10 cents in insurance industry. Financial intelligence is concerned with the financial aspects of the business and how financial decisions are taken. Return on investment on human capital is the package revenue/labour cost, non-labour costs/labour costs. In the calculation of the returns on educational training programs and on investment in new recruits the real issue faced is the measurement of such returns, for example , how do we measure the return on a sales or teamwork programme? Human resources managers are not in a good position to show the gains of such activities to the firm. Therefore, before a decision is taken on the measurement of fte per dolar revenue which measures the productivity of labour, we have to look at the metrics on company loyalty, leadership quality and effectiveness. This matrix is called SHRM "organizational data" (SHRM, 2008).

As part of the organization, human resources management is responsible for keeping the balance between labour force productivity and structural costs. Wemay determine the effectiveness of human capital strategy by measuring betterments and changes in key positions during the year (Hall, 2008:59). Other researchers argued that as long as the return on investment (on human capital) is not measured, any assessment as to its value is not possible. He also

argued that benefit/cost ratios or assessment of returns on such investment are mere approaches and therefore, its measurement is a real difficulty. According to another author, the evaluation is useless if return on investment should be developed. There is only one approach for evaluating return on investment. Besides, this approach is useful both evaluating recruitment-selection processes and job security-health initiatives (Phillips, 1996:57). Although there exits many short giving, it is still considered to be the best measuring tool for human resource management because of the simplicity of its use and its understandability (Berman et.al., 2008:194).

The most important issue in nowadays is whether to contract out human resources management tasks completely or partially. Such a decision increased contractor's cost to \$97 per employee and advice and contract cost per employee to \$124 (PricewaterhouseCoopers, 2010:3). With this development, a new employment form has taken "disposable worker" (Business Week, 2010). In "disposable worker" form of employment, wages are low, no side benefits exist, there exists no security of job, and health and retirement benefits. Thus, a new understanding has come into being for firms in periods of slack business which has changed the equation. And this shows us that a new approach should be needed in the view of ratios mentioned above. First, knowing your company's cash situation will help you understand what is going on now, where the business is headed, and what senior management's priorities are likely in be. At this point, we also observe that many human resource management tasks are being compared and as a result, the number of employees served by human resources personnel are increased. These technological changes may render the system of contracting-out easier. However, the risks involved may not be negligible. It may lower the quality of services, it may have less control over the human resources functions, and finally, the costs may be higher than expected. There is a strong relationship between contracting-out the value that the firm wishes to create and the corporate culture. The metrics used in these programmes should be competible with the markets, they should be standartized and should not be in conflict with the prevailing metrics. Ratios of full-time work and structural metrics, payments and functional labour costs are the most significant metrics. Human resources management with financial intelligence should focus both on the effectiveness of their services and on the productivity within the organization. Management should take note of the

returns on investment on employees, and the performance related to betterment of pay on such investment. In the effectiveness of human resources services such subject as the quality in recruitment, learning and developing, reward schemes and labour force planning should be taken account of. A valuation of such programs and their success in labour performance objectives must be done.

The overall evaluation of human resources management cannot be done in a acumen but it should also look at how these affect the investment strategies and organizational performance. Efforts to measure the effects of human resources management reflect financial intelligence. When contracting-out measurement business, human resources management should focus on how to achieve the companies' objectives. How would the workforce create value and how their effectiveness is measured? Finance professional and investors should be knowledgeable about human capital metrics as it is significant for firm's value. Becker, Huselid and Ulrich (2001:23) put forward that in reading how human resource metrics on performance and process measures should be viewed as it can be done, one should focus on costs and value-creation. In order to understand the relationship between human capital and organizational success, we need a frame based on logic and business principles (Cascio and Boudreau, 2008:2). The focus on the role of human resources management sub-departments affects the decision and actions of these professional as well as indicating what roles they would like to have in the future.

4. CONCLUSION

To establish a relationship between the human aspects of business organizations and financial intelligence is difficult but also a necessity. The contribution of human resources management is possible by the measurement of the results from their work. Specifically, company's balanced scorecards and human resources balanced scorecards should be a whole. It is an increasing necessity to pursue financial results with human resource management outputs. Human resources balanced score cards is a mechanism to describe and measure of how organizations create values. It is important that metrics in balanced scorecards should be special to the organization and they should be continuously followed up and they should have elements to direct strategies. As strategies change such metrics and their contents should be renewed. Specifically related to financial intelligence and comparable other department (organization)

requires such organizational magnitudes or date: total revenue, fte/revenue ratio, fte/net income before tax/fte, number of human resources personnel per employee in the firm; number of human resources personnel per operational expenditure; annual sales increases, total expenditures as a percentage of sales, premiums aimed at high management, percentage of premiums to be paid to high performing employees and positions of substitutable personnel should all be followed up.

There exists a positive relationship between the time that goes in getting out of stagnation and the acquirement of new skills. A longitude passed of difficulty seems to exist between demografic changes, management of the Y generation and keeping them in the company. Specifically in developed countries ability pays in the form of premiums and bonuses fall, labour and health expenses remain at high levels. Performance premiums paid falls as percentage of wages/salaries costs. The pace of labour turnover is closely related to human resources planning and cash-flow balances. Specifically, in periods of coming out of stagnation the turnover in the personnel who are in key strategic positions seems to increase on a voluntary basis. It is observed that those who have high performance change their organization in more numbers and more frequently. It is also observed that from the point of view of formal substitute personnel 1.6 persons are considered for each key position(Pricewaterhouse Coopers, The Cataloge Review, Executive Summary of Results from 2009/2010, US Human Capital Effectiveness Report, November, 2009: 3-4). Employers should be aware of the significance of the human capital in financial success and should establish a positive approach to work requisities and future trends.

Organizations require high-quality people to be in the right places in the future. To keep these high-performing personnel help enhance the market and name value of the company, but may entail additional financial costs. By focusing on maximization of productivity of each personnel, old and new, may avoid unnecessary turn-out, and this saving in added to company's profit. Another important aspect is filling the vacant positions in the company.

Another important ratio is the direct human resources costs to total number of workers. Direct human resources costs include wages and side benefits, contracting-out, purchases of advisory service agreements and establishment of systems but not the costs of education/training and security of work

expenses. The return on investment in human capital consistsof the profit on per dolar investment in human resources. This ratio, according to Pricewaterhouse Coopers, was 2.38 in 2006, 2.62 in 2007, 3.41 in 2008 and 3.41 in 2009 (The Saratoga Review, 2009:6). The cost of new recruitment will increase as economics get out recession. Performance management and its important output as bonuses and other stimulases in total labour expenses must also be taken account. A stimuluses to be meaningful must be a significant magnitude of the total wages (up to 40-60%). This may be a good way of keeping able personnel within organization.

A good balance should be established between the budgetary losses due to loss of able employees and financial possibilities of the firm. The human resources managers of the future should be well versed in numerics, should understand what lies underneath these figures as to the human aspects and should be well equipped to analyse these numbers. For human resources managers, numbers may be soulless, the art is to learn their secret language and give them life.

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