

Human Capital – A Driving Force for Business Growth

David Lamotte – Director, ILO Office for the Pacific Island Countries¹

Welcome and appreciation

Thank you for the opportunity to be present with you at this important annual event. I spoke at your event last year and I am pleasantly surprised to be invited again to address your congress.

Presentation outline

My presentation today is titled “Human Capital – A Driving Force for Business Growth”. In speaking to this topic, I intend to address

- What is the ILO and why the concerned for the development of human capital and business growth
- Look more specifically at what is Human Capital, how it is acquired and why it is considered important for business growth
- Provide some reflections on human capital development in Fiji and conclude with some strategies that you might consider in your workplaces to develop human capital

What is the ILO and why we are concerned for the development of human capital and business growth

The International Labour Organisation (ILO) was founded in 1919, primarily in response to humanitarian concern over the condition of workers who were being exploited with no consideration for their health, their family lives or their professional and social advancement. Today the ILO is a United Nations agency dealing with labour and employment issues, particularly International Labour standards and decent work for all women and men.

¹ Acknowledgements: The author wishes to thank the contributions from Michael Elkin and Nikolai Rogovsky.

The ILO is the only tripartite U.N. agency with government, employer, and worker representatives. This tripartite structure makes the ILO a unique forum in which the governments and the social partners of the economy of its 185 member States can freely and openly debate and elaborate labour standards and policies.

The ILO's concern for building human capital is essentially because countries at all development levels have found that adequate education and skills increases their ability to innovate and adopt new technologies. They make the difference between inclusive growth and growth that leaves large segments of society behind. A workforce that has been appropriately trained and is able to continue learning boosts investor confidence and thus job growth.

In recognition of the importance of the need to build skills and talent, the ILO developed the Human Resources Development Recommendation, 2004 (No. 195) that provides guidance on the content of effective skills policies and systems. The Recommendation 195 is built on a number of core principles that reflect the ILO's values, including:

- that education, training and lifelong learning contribute significantly to promoting the interests of people, enterprises, the economy and society as a whole;
- that lifelong learning contributes to personal development, access to culture and active citizenship;
- that the government, and representative organizations of employers and workers have roles to play and commitments to fulfil in support of lifelong learning;
- that many developing countries should be assisted to design, fund and implement education and training policies for economic and employment growth, and the eradication of poverty; and
- that the realization of decent work for workers everywhere is a primary objective of the International Labour Organization.

The Recommendation recognizes the important role of the government in the development and implementation of education, and training policies, and the increasing role of enterprises in enhancing investment in training. It also stresses the importance of individuals making use of the education, training and lifelong learning opportunities offered.

However, what is the relationship between business growth and human capital?

Businesses are very important. All across the world people are in search of jobs. Jobs, so they can raise their families and send their children to school. Jobs, that provide access to social protection for them and their families. Moreover, jobs in which they are respected can organize and have a voice. What they want is decent work. Business play a key role in creating productive

and decent work that helps meet the economic and social aspirations of people and their communities. Whether small, medium or large, enterprises are a major source of growth and employment in all countries. Enterprises and the entrepreneurs who run them play a crucial role in creating jobs and reducing poverty.

Drawing on the latest thinking on sustainable development, private sector promotion and good corporate citizenship, the ILO's International Labour Conference in 2007 addressed the imperatives of sustainable development, fair globalization and the role of enterprises. In its Conclusions, it set out a programme for and provided guidance on the promotion of sustainable enterprises. In respect to the Education, training and lifelong learning it says:

Human talent is the single most important productive factor in today's economy. Focusing on the development of a skilled workforce and the expansion of human capabilities through high-quality systems of education, training and lifelong learning is important for helping workers to find good jobs and enterprises to find the skilled workers they need. Financial support should also be made available to enhance access of poor workers to training and skills upgrading. In this way, society can achieve the twin goals of economic success and social progress.

So there is a broad understanding that businesses need to start and grow in order to create quality jobs and that building of human capital is an important contributing factor. This idea was reinforced at the 2008 International Labour Conference, the ILO's tripartite constituency of governments, employers and workers adopted a set of conclusions focussing on how investing in education and skills – building the human capital - for women and men to help economies achieve dynamic growth with quality jobs is a pressing priority throughout the globe.

What is Human capital, why it is increasingly important and how it is acquired?

To most people, capital means money in the bank or a business's stock or goods. These are all forms of capital in the sense that they are assets that yield income and other useful outputs over long periods. However, such tangible forms of capital are not the only type of capital. One of the most important ideas in labour economics is to think of the set of marketable skills of workers as a form of capital in which workers make a variety of investments. This perspective is important in understanding both investment incentives, and the structure of wages and earnings.

Loosely speaking, human capital corresponds to any stock of knowledge or characteristics the worker has (either innate or acquired) that contributes to his or her productivity. Thus, human capital is the stock of competencies, knowledge, social and personality attributes, including creativity, embodied in the ability to produce economic value.

How is the human capital acquired and owned?

Human capital is an intangible asset - it is not owned by the firm that employs it and is generally not fungible. Specifically, individuals arrive at 9am and leave at 5pm (in the conventional office model) taking most of their knowledge and relationships with them. Despite the lack of formal ownership, this paper aims to highlight that enterprises can and do gain from high levels of training.

How and when individuals acquire their human capital is particularly important and relevant to this discussion. Typically, researches identify five sources of human capital, namely:

- **Innate ability:** workers can have different amounts of skills/human capital because of innate differences.
- **Schooling:** this has been the focus of much research, since it is the most easily observable component of human capital investments.
- **School quality and non-schooling investments**
- **Training:** this is the component of human capital that workers acquire after schooling, often associated with some set of skills useful for a particular industry or useful with a particular set of technologies.
- **Pre-labour market influences:** there is increasing recognition of the influence of family's peer-groups on the knowledge, skills, health, values, and habits of their children. Family and friends effect educational attainment, marital stability, propensities to smoke and to get to work on time, and many other dimensions of their children's lives.

Why is Human Capital an increasingly important issue?

The quantity and quality of human capital is essential to the operation of just about any type of public or private enterprise. Employing individuals who have the necessary expertise, judgment, and ability to function within their assigned roles allows the business to operate at maximum efficiency. This, in turn, increases the potential of earning a profit, and remaining successful for many years. A failure to identify individuals with the necessary combination of skills, experience, and education can undermine the efforts of even the most well organized company.

Globalization and the changing context of trade are having a profound impact on the way enterprises operate. Information and Communication Technology (ICT), nanotechnology, new computerised machinery and higher-speed communications, are just a few of the developments that are revolutionising business processes and management strategies. One effect of these advances has been an increase in short product cycles, essential in an environment where products that would previously have served for a decade can become the victims of fashion or of new innovations within months².

All of the above changes generate a demand for new knowledge and innovation, and for the skills that enable enterprises to benefit from continuous technological advances. Education and training are key responses to this demand, as well as being a responsible workplace practice that enhances the workplace experience and widens the opportunities available to workers.

Today, human capital may be the most critical source of competitive advantage. The phrase ‘our people are our greatest asset’ may have become a tired cliché but studies consistently shown that:

- one of the major problems that managers have is finding good people and keeping them; and
- that most managers fear that their employees are ill-equipped in terms of skills needed to complete their responsibilities.

Whose responsibility is it to build the human capital?

Building human capital is clearly a complex challenge requiring actions at three levels:

1. Firstly, the **government** which has an important role to play in ensuring that policies and institutions succeed in linking skills to productivity, employment, and development. For this effort three main objectives are important, namely
 - matching supply to current demand for skills;
 - helping workers and enterprises adjust to change; and
 - anticipating and delivering skills needed in the future in order to sustain a dynamic development process.

For any government this is a policy coordination challenge involving labour, education and other ministries, social partners, training providers, and employment services to work together to anticipate occupation and skill needs and target training towards

² ILO (2008) Skills for improved productivity, employment growth and development.. Report V, International Labour Conference, 97th Session, Fifth item on the agenda.

meeting them.

The Ministry of Strategic Planning, National Development and Statistics have adopted the National Strategic Human Resource Plan 2011- 2015 as a guide to the fullest and most productive use of Fiji's human resource. I understand that Honourable Minister for Labour and Industrial Relations will be address governments policies and programmes in this regard.

2. Secondly, **enterprises** have role in providing workplace-based learning and training programmes that developing enterprise specific competencies.
3. Thirdly, **individuals** also have a responsibility for their own development through further education, training and lifelong learning opportunities.

Reflections on the Fiji Situation and how your enterprise can contribute to the development of human capital

There is widespread recognition that over the last three decades in Fiji there has been a significant loss of human capital. This loss has often been referred to as "brain drain" or "human capital flight" which occurs when the most talented individuals (those with the most human capital) depart for education or opportunity to wealthier countries.

This is not a phenomena specific to Fiji or the Pacific. In many countries, educated individuals often migrate from poor countries to rich countries seeking opportunity. This movement has positive effects for both countries: capital-rich countries gain an influx in labour, and labour rich countries receive capital when migrants remit money home. The loss of labour in the old country can also increase the wage rate for those who do not emigrate, while the additional labour lowers wages in the new country. When workers migrate, their early care and education generally benefit the country where they move to work. In addition, when they have health problems or retire, their care and retirement pension will typically be paid in the new country.

The number of departing Fijian workers increased before independence in 1970 and between then and the mid-1980s, an average of between 200-300 people left the country each month. Their numbers increased before independence in 1970 and between then and the mid-1980s, an average of between 200-300 people left the country each month.

Since 1987, these numbers have doubled and even tripled. This haemorrhage of human capital was majorly due to the military coups and political upheavals. Today it might be fair to argue that

Fiji is at the crossroads because recent studies have shown that the lack of human capital is a significant constraint to business investment and growth. For example;

- The report on ‘*Obstacles to Economic Growth in Six Pacific Island Countries*’ (2006) states that the factors that limit the determinants of growth are lack of savings and unskilled labour.³
- The *Islands Business Magazine* (2007) reports that the growth in Pacific is constrained by under-investment in infrastructure as well as human capital.
- The South Pacific Business Development Report (2010) draws attention to the current situation of business growth in the South Pacific stating that the several constraints to development are poor macroeconomic performance, lack of diversification, lack of skilful human resource, ineffective policies and frequent natural disasters.
- The paper on *Economic Growth in the Pacific Island States* (2011) emphasizes that developing countries must re-look into building capacity through human resources training and institution building.⁴
- The paper on ‘*Binding Constraints to Economics Growth in the Pacific Islands*’ (2012) explains that for Pacific economies to benefit from long term development plans, it is necessary that they invest in infrastructure and human capital.⁵

What can you do as managers and human resources professionals to build human capital in your workforce

As you are, enterprise owners and managers let me conclude this presentation by turning my attention to what you can do to contribute to the development of human capital in your workplaces.

Question 1: Does your enterprise have fair and transparent recruitment practices?

Recruiting people with the needed basic competencies is a first and important step – here I refer to innate and acquired competencies. Research reveals that bad recruitment practices can have a range of negative consequences. In particular, it can lead to discrimination, brand damage, missed talent, bad appointments, increased dissatisfaction, and unnecessary business costs.

Despite these negative consequences, recruitment practices are often a low business priority. It seems that many companies (though not all⁶) only really look closely at their recruitment

³ Ron Duncan and Haruo Nakagawa, *Obstacles to Economic Growth in Six Pacific Island Countries*, 2006.

⁴ Prasad Biman, *Economic Growth in Pacific Island States: Addressing the Critical Issues*, Feb 2011.

⁵ Duncan R., Codippily H., Duituturaga E., and Bulatale R., *Binding Constraints to Economics Growth in the Pacific Islands: Some Comparative Insights*, the Pacific Islands Development Program, April 2012.

practices when unemployment is low and recruitment is difficult, whereas research points to the importance of integrating Human resource management into strategic planning. Other studies have found that recruitment and selection strategic integration is positively related to market share, sales growth, profit growth, employee productivity and employee satisfaction⁶

Question 2: Does your enterprise offer workplace training?

Investments in training provide good business returns. Studies have shown that enterprises that combine innovations with targeted training are more likely to report growth in output, jobs and labour productivity compared to firms that do not engage in workplace training. Training can contribute to product and process innovations, and firms that innovate in products and services, have been found to grow faster and are more likely to expand their employment than non-innovative ones, regardless of industry, size or other characteristics⁶

Where enterprises do provide training, the form it takes will be affected by the firm's size and resources. Whilst large enterprises may have the resources to create or buy in training, small and medium enterprises (SMEs) may not. In this case, some commonly reported alternatives include:

- Formal on-the-job training or apprenticeships that combine this with public course attendance;
- Informal skill swaps between employees. Giving employees opportunities to pass on skills and teach others about their roles can, in itself, be a motivator and provide a break from day-to-day monotony.
- Forming inter-firm training clusters;
- Seeking to benefit from training provided through value chains (e.g. by multinational enterprises)

In situation like we have in Fiji where there is an outward migration of skilled labour or even poaching of trained employees to save having to pay for training, you sometimes hear business owners and managers complain that why should they train their staff. But the risk of losing trained employees does not mean the investment is wasted, as shown by the large number of successful companies continuing to invest in employee development programmes. One important reason is that it helps them with their recruiting, teamwork and motivation of staff. Training is a route to more interesting tasks and can feel like a 'pat on the back' from the employer.

⁶ Shulzhenko, E. (2012) Human Resource Management and Labour Relations in Post-Transitional Russia Discussion Paper SP III 2012–303.

Question 3: Does your enterprise have policies and practices that encourage and reward employees who invest their own time and resources in taking *further education and training*?

Human capital is an intangible asset - it is not owned by the firm. Individuals do benefit from taking further education and training courses. Enterprises can provide incentives to individuals to engage in learning – particularly those for whom costs have been a barrier to participation. Typical initiatives reducing the direct costs to individuals, compensating for earnings lost during learning; and sharing risks.

Question 4: Does your enterprise invest in management and supervisory training and promote modern management practices?

Good competent skilled workers sometimes are promoted to superiors and managers. The competencies required to fulfil these new roles is often very different from those that got them promoted in the first place. Studies have consistently shown that too many firms, particularly small and medium enterprises, believe that management support services are too expensive and not value-adding. However, studies also show that modern management practices can create long-term resilience for enterprises.

In a paper of this nature, it is not possible to describe all of the many management approaches. However, three examples - Kaizen, Lean Manufacturing and Total Quality Management (TQM) – are provided. These practices are highlighted because they have been adopted widely in enterprises around the world and researchers suggest that they are effective in helping managers to develop responsible workplace practices and competitive edge. All of them place worker-management dialogue at the centre of improvement and efficiency efforts.

Question 5: Does your workplace have policies and practices to retain human capital and reduce staff turnover?

Life events, personal decisions, a change in personal resources, health and a variety of work-life balance can provoke departures that an enterprise can have little influence over. Research also shows that staff turnover is affected by economic circumstances: employees tend to hold on to their positions during an economic downturn and to leave once the economy recovers.

Sometimes, it can be argued that staff turnover bring business benefits, such as new energy, ideas/talent and reduced wage costs of new employees with less time served. However, despite

these benefits, there is broad agreement that high staff turnover represents a significant cost to enterprises and that unusually high turnover is associated with poor enterprise performance.

Enterprises can use a variety of practices that entice existing employees to stay within the enterprise. In most cases, it is a relatively higher wage but there are also other incentives such as annual bonuses, retirement fund contributions, health insurance and opportunities for further training and career advancement. Such incentive can be justified because enterprises invest significant resources in hiring, training and retaining of key employees.

A wide range of research findings confirm that high turnover is, generally, an indication of problems in the enterprise, in terms of wages, industrial relations, working conditions and/or other welfare facilities. Given the high cost of staff turnover and its impact on running a business, a well thought-out program designed to retain employees could easily pay for itself in a very short period.

Question 6: Does your enterprise participate in government board and committees setting education and training policy and management of institutions?

The pace of change of the world of work, set by innovation, technology and markets, is high. Keeping up with this pace of change is a continuing challenge for policy makers and learning institutions. The active participation of employers' and of workers' representatives in Government vocational education and training institutions is essential to bridging this gulf.

Concluding comments

Building human capital is a pre-requisite for business growth and the growth of an economy. The quality and availability human capital, fuels innovation, investment, technological change, enterprise development, economic diversification and competitiveness that economies need to accelerate the creation of more but also better jobs and thereby improve social cohesion.

The building of human capital is a share responsibility involving, the **government** through its education and training policies and institutions; the **individual** through how they take advantage of available training and learning opportunities; and the **enterprise** who can and do gain from high levels of training.

I hope that my presentation today suggests some practical ways in which you as human resource managers can contribute to the acquisition of human capital that contributes to the success and growth of your business and the broader Fiji economy and society.