

# RELATIONSHIP BETWEEN HUMAN CAPITAL DEVELOPMENT AND ORGANIZATION PERFORMANCE. (EVIDENCE FROM PAKISTAN BANKING SYSTEM)

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**ABSTRACT:** Due to globalization and rapid changes in corporate world the importance of human capital is increased day by day. Latest research indicate that in order to sustain competitive advantage and contentious growth, most of the companies across the globe emphasize on developing new strategies to retain the most valuable human resource. In the current research paper relationship between strategies for the development of organizational human resource factors and organizational performance is measured in the banking system of Pakistan Twin cities (Islamabad and Rawalpindi). Human capital development strategies were measured on the basis of their competencies (employee's knowledge, skills and capabilities), commitment (employee's participation, job satisfaction and empowerment) and strategic HRM practices (training, compensation, participation and sharing of information). Employee's commitment can be defined as psychological attachment and the resulting loyalty of an employee to an organization. It can be best measured by assessing employee's participation in organizational activities, their satisfaction from current job status. While SHRM activities can be better understood by the compensation offered to the employees, training programs evaluation and information sharing mechanism inside the organization. On the other hand organizational performance was measured through the indication of betterment in Financial Performance, goodwill and sustained HR polices. For this purpose adopted Questionnaires with some modification from (the expert in the field of study) was distributed among 400 banking employees. After one week 340 filled questionnaires were received. Finally 300 questionnaires consisted accurate information were analyzed through SPSS V-17 and AMOS for factor loading, SEM analysis and Model fit indices. Results indicate that Skill attribute of employee's competencies contribute 0.61, followed by Knowledge 0.49, and capabilities 0.32. Similarly Employees commitment was strongly associated with empowerment issue and SHRM practices attribute was strongly associated by employee's participation. In the current research examination between human capital indicators and organizational performance based on financial performance, goodwill and supreme HR performance is examined for the first time in single model. Results also confirm that commitment, capabilities and SHRM practices play an important role in reshaping strategies to emphasize on human capital development, that leads to boost organizational performance. Current research suggests that organizations can develop their human capital by providing appropriate training sessions and systematic rewarding opportunity. Organizations must also emphasize on improving their employees knowledge by proper knowledge management polices to cope with the advancement inside and outside organizational environment. Study also indicates that employee's unionization may also be favored but within prescribed limits of organizational policies that will create unity among employees. It will also create better understanding between organizational employees and top level management, which directly result in committed employees, as well as dedicated employees are the true asset for an organization to achieve its objectives with least efforts.

**Keywords:** Human Capital, Organization performance, SHRM Practices, Competencies, Commitment

## INTRODUCTION.

In today's world of globalization human capital is rated as one of the most important segment of organization that provides competitive advantage and increase organizational profit, which ultimately boost organizational performance [42]. Human capital must also be treated as other organizational assets like cash, inventory, factory and machinery, plants etc. Keeping in view the business profitability margin, now most of organizations at national and international level tries to increase the moral, character as well as motivation of their employees. By enhancing the skill, competence, satisfaction and commitment of employees, organizations can achieve its goal and objective easily. According to Barney [9] human capital have four different attributes, which are rare in nature, most valuable and cannot be imitated. Nelson [48] states that "resource theory" is based on the concept that proper allocation of resources particularly (human resource) provide sustainable position in market. Hence one of the important factors of organizations is to

invest a lot on reshaping the capabilities of existing and available human resource to produce competitive pool for future challenges [29,59,51,52] and [70] state that human capital must be kept at the top priority of organizational leaders [21]. All references mentioned above provide evidence to convert human capital practices into financial figures and state that human resource must be treated and presented as an assets on balance sheet. It means that organizational human resource (employees) is also like other assets e.g., cash, Factory, inventory etc. Findings from [51] and [62] indicate that use of capital and technology cannot provide sustainable position to organization, because the concept of these two resources is build on short term logic. Findings of other studies, indicate that appropriate human capital decision can provide the chance to the organization to reach its destiny without any hurdles [66, 17]. Most of the research studies found positive relationship between human capital and organizational performance [72, 54, 33] but still the question arises, that how this relationship is established

[32]. The prime concern about this relation is to investigate about the key factors (attributes) of human capital that makes way for organizational success. In the current study relationship with three important aspects of human resource, with organizational performance will be explored. For this purpose research will investigate the casual relationship between human capital decision and organizational performance. Human capital will be measured on three different dimensions (Competencies, commitment and SHRM practice. Competency based approach related to human capital will be explored on further three dimensions (Knowledge, Skills and capabilities of employees). Employees Commitment will be investigated through (employee's participation, their job satisfaction and participation in organization politics). Third one dimension of Human capital is related to Strategic HRM Practices. Which consist of (training, incentive compensation, and sharing of information). On the other hand organization performance will be measured on betterment in organization performance approaches through (HR decisions, financial position and overall rating of organization).

Current study begin with the need to effectively manage organizational human resource. Because of the change in market on the basis of competition, globalization, employee lay off, variation in market structure and different socio-political circumstances, which leads the organization to compete on the basis of its human capital decisions. Such an unfavorable circumstances challenge organizational top level management to formulate strategies to maintain its position in the market with competitive era. Due to such challenges, HR department of various organizations became a very challenging post for ordinary humans. As a result, it becomes a topic of interest for the academicians and management to find out the possible solution for different problems associated with human capital [17]. Moreover, it plays a significant role in creating wealth for their stakeholders [44, 45]. Different studies proved the positive and significant relationship between human capital and organizational performance [32, 66] but still the question remains, that which particular type of human capital decision are significant to the organizational success and how this relationship will be measured [66, 17]. Therefore the significant role of HR is to investigate that how human capital decision affects organizational performance.

## OBJECTIVES

- To investigate the link/association between commitment based HR practices and human capital decision.
- To investigate the association between strategic HR practices and human capital decision.
- To investigate the relationship between human capital (SHRP, CBHR, BHRP) and organization outcomes (HR based, financial performance and position based performance).

## LITERATURE REVIEW

Human capital can be define as a process of managing people and creating values as well as to systematically evaluate the way people behave in organizations and lead to develop strategies for achieving organizational objective effectively and efficiently. Based on the above definition that national and chartered institute of personnel (UK) highlight human capital as knowledge, skill and learning process of organization employee [70]. Employees competencies is the aggregate of skills, knowledge and capabilities [31] that result in improved organizational performance. Employees' organizational commitment are also important like employees competencies for organization's wellbeing [66,16]. Organizational performance can be better treated if human capital decision are in an appropriate way and give competitive advantage. While low in an appropriate way and give competitive advantage. While Liouville [43] state that human capital decision plays its role directly or indirectly in improving the performance of organizations. The strategic human resource theory concept is based on two important theoretical backgrounds, human capital theory [56, 17] and SR theory [9] the strategic resource theory work on the concept, that it must provide edge to over competence [10]. The competitive edge concept is an important pillar of organization all these authors SHRM is most important factor of production and cannot be replaced easily by another factor of production [17]. According to Huselid [33] theory of human capital indicates that the knowledge and abilities are most important functions having ability of economic value creation for organizations.

Indeed the effectiveness of any organization will be possible outcome of improved organization human capital asset. In today's world of globalization most of the organizations depend upon the employees skills / abilities. That's why reshaping organization employees skill can better constitute in organizational success, thus the HR strategy of the organization is focusing on investing more and more toward the human capital programmer to optimize their workforce. In order to face the challenges of the dynamic world competency as well as capacity building programs becomes order of the day [14, 31]. Moreover, according to follower of human capital theory, human resources return is higher as compare to other investment [29] organization those assets which are invisible (Knowledge, experience attributes attitude, skill, motivation, competencies are the prime factor in producing outs trading result [50, 51].

The relationship between different SHRM attributes (Training, information sharing participation intensive compensation) and organizational performance was explored by Arcand [3] in Tunisia Telecom industry. Results indicate that four important attributes of SHRM are positively associated with organizational performance in term of financial HR an overall organizational performance. At the same time a positive relationship was found between organizational performance and training attributes of SHRM practices. While the therelation ship between incentive compensation and organizational performance was also significant. A positive and significant relationship was found between sharing of information by organizational employees

and organization performance rate, a significant relationship was also found between participation in decision making style and improved organization performance [5,33,35,47,46, 56]. Welbourne [65] found positive relationship between compliancy and commitment based human capital factors and organization.

Based on research objectives and previous research studies following hypothesis are developed for the current study.

**HYPOTHESES**

- H1.** Competencies based practices of employees have positive and significant effect on human capital.
- H2.** Commitment based practices of employees have positive and significant effect on human capital.
- H3.** Strategic HR practices have positive and significant relationship with human capital.
- H4.** Human capital factor have positive relation with organizational performance on the basis of financial results.
- H5.** Human capital has a positive effect on organizational performance on the basis of HR result.
- H6.** Human resource practice has positive effect on overall organizational performance.

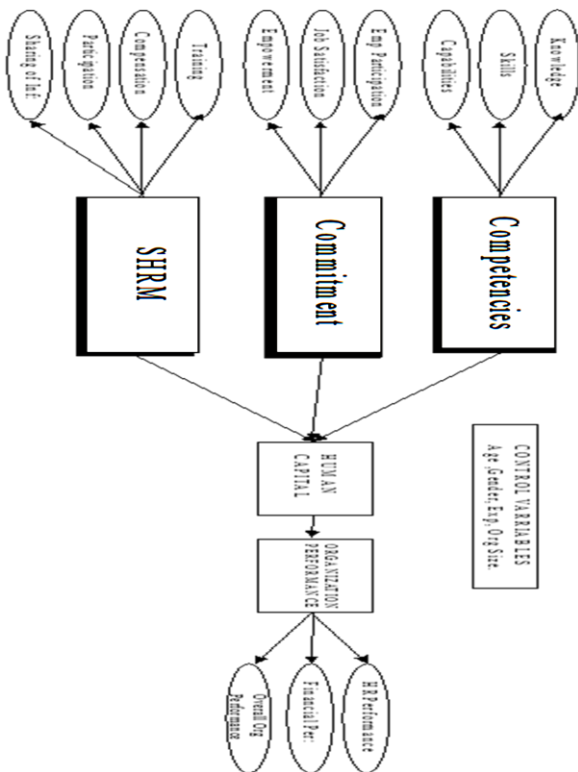
**METHODOLOGY**

The population of the sample is banking sector in twin cities of Pakistan (Islamabad and Rawalpindi) the questionnaires’ for two important component of independent variable, i.e., competences and commitment factor was developed on the basis of previous literature. While questionnaire for SHRM component training practices, information sharing and intensive compensation was adopted form [58, 3, 37, 27, 56, 22]. Simple random sampling techniques we applied to collect the data. Totally 400 questionnaires were distributed among employees of selected bank. All the components of questionnaires were pretested by 20 faculty members and PhD students of HR studies.

A formal letter of permission was also send along the survey questionnaires which clearly indicate that participants can fill the questionnaires with their mutual consent and their name verification will be kept in secret. Secondly Ethical codes of social, business and management studies (SBMS) were followed in collecting information from respondents. In the current research study the independent variables are three (Competency based, commitment based and SHRM based attributes of Human resource practices), while dependent variables are organizational performance. Age, gender, experience and organizational size were controlled variables. All the attributes of dependent and independent variables were measured on 5 point Likert Scale where 1 denote strongly Disagree 2 Disagree, 3 Neutral, 4 Agree and 5 Strongly Agree. After 30 days of questionnaires’ distribution, 340 filled questionnaires were received showing response rate of 85% some of the questionnaires’ consists of missing values, while overall usable questionnaires’ for final analysis were 300. All the data was entered in SPSS Version 20 in appropriate way for furtherer analysis. AMOS Version 20 was also used for factor analysis; structural equation modeling and model fit indices.

**RESULT AND DISCUSSION**

Factor analysis is the process of examining convergence and loading structure of each items in the survey. And in factor analysis communalities is the degree which show how each item is related to each other. Higher the value of communities better will be the results. Here in our research studies the communities are explained in term of extraction in which every factor informs about the items related to all factors. Almost every item have execution value higher than 9 which show that 90% item value have important over the other factor. Smaller value designate that it is not fit with factor solution and should plague from for the analysis.



**Fig 1.1: Proposed Research Model.**

**Table No. 1 Related Component Matrix and their Convergence Value.**

Question Number	Factor 1	Factor 2	Factor 3	Factor 4	Factor 5
Question_1	.901				
Question_2	.899				
Question_3	.923				
Question_4	.911				
Question_5			.521		
Question_6			.499		
Question_7	.832				
Question_8	.901				.522
Question_9		.541		.433	
Question_19	.760		.601		
Question_11				.533	
Question_12		.521			.411
Question_13		.988			

**Table No 2. Related Component Matrix of Survey item and their Convergence Values.**

	Factor 1	Factor 2	Factor 3	Factor 4	Factor 5
Question_14	.491	.980			
Question_15		.911			
Question_16		.865		.457	
Question_17	.521				
Question_18				.424	
Question_19	.511				
Question_20	.544			.424	
Question_21		.711			.662
Question_22		.711			.662
Question_23	.511	.672			
Question_24			.911		
Question_25			.921		
Question_26			.988		
Question_27		.417			
Question_28	.511	.413			
Question_29		.554			

**Table No 3. Related Component Matrix of Survey item and their Convergence Values.**

	Factor 1	Factor 2	Factor 3	Factor 4	Factor 5
Question_30			.699		.421
Question_31	.522		.589		
Question_32				.621	
Question_33		.529			
Question_34		.498			
Question_35	.622			.655	
Question_36		.501		.688	
Question_37	.411	.417	.447	.522	
Question_38					.814

**Table No. 4. Regression Path of SEM/Structural Co efficient of Model.**

Relationship testing via path_30;	Estimates	S.E	CR	P	Labels
H.Cap $\leftarrow$ CPT	0.349**	0.212	7.177	**	Support
H.Cap $\leftarrow$ CMT	0.512**	0.077	12.058	**	Support
H.Cap $\leftarrow$ SHRM	0.414**	0.089	11.012	**	Support
SKLS $\leftarrow$ CPT	0.612**	0.346	4.132	**	Support
KNOW $\leftarrow$ CPT	0.499**	0.444	4.162	**	Support
CAPB $\leftarrow$ CPT	0.302**	0.045	9.002	**	Support
EXPS $\leftarrow$ CMT	0.349**	0.151	4.244	**	Support
EMPL $\leftarrow$ CMT	0.214**	0.221	14.132	**	Support
JSAT $\leftarrow$ CMT	0.219**	0.063	9.403	**	Support

TRAN←SHRM	0.414**	0.193	4.454	**	Support
COMP←SHRM	0.56*	0.196	5.042	*	Support
PART←SHRM	0.616**	0.321	7.098	**	Support
SOI←SHRM	0.273**	0.422	2.531	**	Support
ORGP←H.CAP	0.412**	0.818	8.233	**	Support
HR←ORGP	0.313*	0.612	7.111	*	Support
HPR←ORGP	0.298**	0.444	8.121	**	Support
O.P←ORGP	0.423*	0.714	12.212	*	Support

\* 0.001 shows beta significance at 90CI

\*\* 0.05 shows beta significance at 95CI

Factor loading is the process of showing relation of different variables with every factor in related or unrelated matrices. The main theme of factor loading is to increase the inter relationship of different variables on numeric single factor. During related matrices. First factor analysis show response higher rate of variance present in table Table 2 series. Factor 2 is related with other factor having higher Value (Loading) higher loading mean commonly values higher than 4, third factor have also slight higher values (loading) shown in table 3 so based on the information from these tables factor 1, 2, 3 have higher loading and explanation has become difficult so in the next step structural equation modeling will be used to determine causal relationship between the variables.

The results shown in table 4 indicates the different critical ratios regression estimates and significance value of different variables the result conform that competences of employees

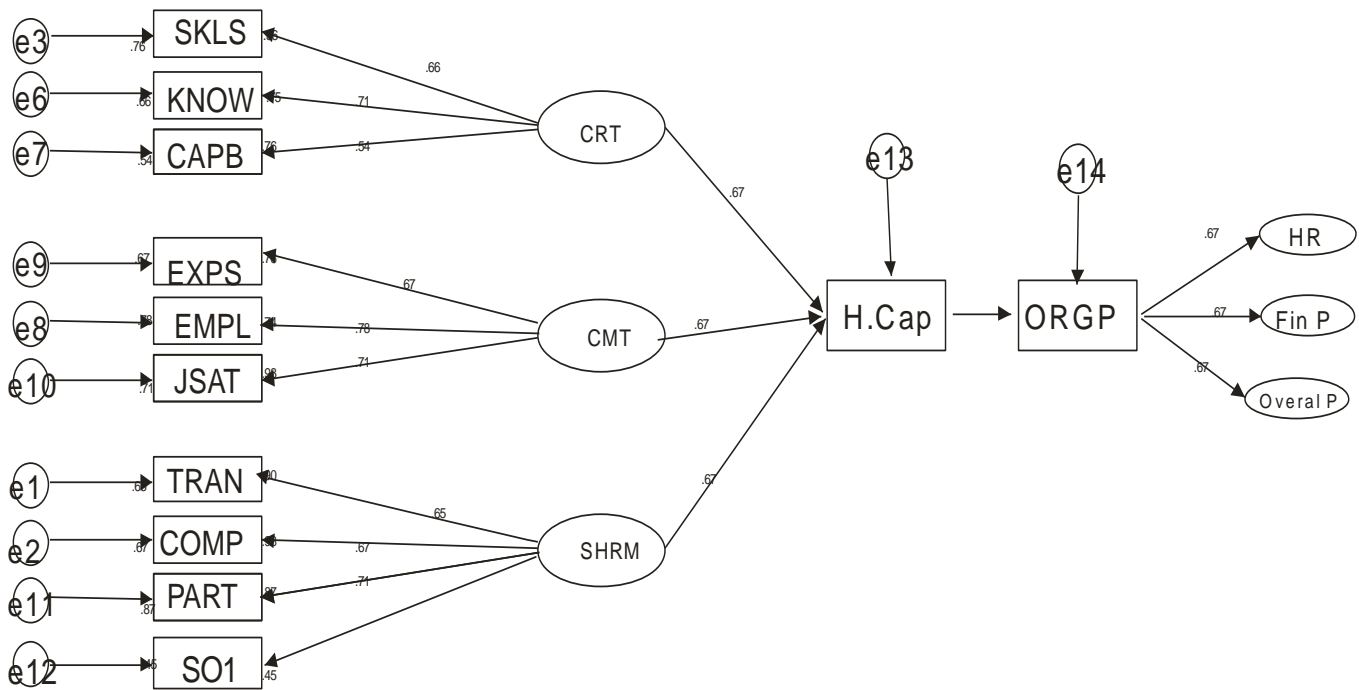
have significant effect on human capital and show 34% amplifications. Similarly beta's values are also significant at 0.005% while critical ratios of 7.117 also conform their significance. Both organization commitment and SHRM practices are significant at 0.051%. In construct HR, financial performance and overall organization performance results indicate that they have significant effect on organization performance and show 31%, 29% and 42% escalation in the enhancement of organization performance. Even in the table it is clearly indicated that competency and sharing of information are positively related to SHRM practice at 0.01% with 41% and 27% escalation. While two other factor of SHRM participation in organization decision network and training have significant impact towards strengthen organization performance with 41% and 61% escalation respectively with beta result significance level of 0.05%.

**Table No 5. Model Fit Indices**

$\chi^2/df$	GFI	AGFI	CFI	NFI	RMSEA
76.0/27	0.952	0.919	0.911	0.932	0.0492

Table No 5 shows model fit indices with different attribute of model by applying SPSS version 20 in table No. 5 it is clearly show that chi square value is less than the acceptable value of (PLO.05) and show model is not fit. But the problem arise because of small sample size. As according to [54] that good and acceptable value for goodness of fit indices (GFI) must be equal or greater to 0.90. In our case CIF value is 0.952 which is greater than 0.90 hence on GFI basis our model is fit.

CFI (Comparative fit indices) value must also be equal or greater to 0.90 [31] and NFI (Norm Fit Indices) must also be in this range. Our results indicate that CFI (0.911) and HFI (0.932) are both in acceptable range. Hence model is good fit on the basis of CFI and NFI value. RMSEA is another factor showing weather the selected parameter are fit in the population variance matrix or not. RMSEA value lower than 0.08 is acceptable and equal to 0.05 is ideal. In our case it is near to 0.05 which is below than (.08) hence model is good fit and acceptable.



**Figure 1.2: Model and hypotheses. Numbers around a path indicate standardized coefficients of the path resulting from the SEM. \* po.05.**

**CONCLUSION AND RECOMMENDATIONS**

The most important factors for the success of organization are to invest on its human resource management skills. Although there is a lot of literature available on the importance of different human skills and its association with organizational performance. But still the question is how this linkage evolved and what are the basic circumstances behind this relationship. Different researchers found the association between single factors of human capital with organizational performance. In the current study an attempt was made to investigate almost all the important attributes of employees in single model. In Pakistan’s prospective so far no single study is conducted to investigate all these factors simultaneously and to check its relationship with organizational performance on the basis of HR as well as financial performance. The results of the current study show that if employee’s performance is reshaped in accordance to its capabilities, the result will be motivated employees. In the current study different attributes of SHRM practices and organizational performance results are significant and in line with the findings of [34, 3]. As competency can be defined as combined attribute of knowledge, skill, ability, motivation, and experience of employees and it is found that for advancement in current knowledge, it can be possible through appropriate training, here the findings of our study are in accordance with [70]. Commitment of employees play significant role in boosting organizational performance. Previous studies show positive relationship between organizational performance, the positive and significant results of current study are consistent with previous studies

[16, 65]. In the light of the findings of current study it is evident that relationship between human capital organizational performance must be taken into consideration as serious strategies. An appropriate method /techniques relevant to employee’s well being may be initiated to boost up this relationship. As Human Resources asset can play its role as an undefeatable component for organizational success. So it is highly recommended that employee’s skills, abilities, competences, learning, commitment, satisfaction, participation, may be placed at top priority for their intrinsic and extrinsic motivation and organization wellbeing.

**RECOMMENDATIONS**

Following are the recommendations from current research study.

1. It is recommended that organizational employees (first line and middle managers) must provide appropriate training and reward system to boost their skills and may act as a catalyst in organizational success.
2. To improve the capabilities and attributes of employees it is recommended that organization must apply appropriate knowledge management practices. That employees may get much knowledge about current challenges, and relevant changes in their role/responsibilities etc.
3. Current human capital may be trained in organization and focus must be on enhancing the capabilities of current employees that will create commitment among employees. As a result organizational performance will be increased dramatically.

4. Employee's unionization can be favored, that employees may raise their voice against any injustice, but with the prescribed limits of the organizational procedures and in accordance with the rules and regulation.
5. Employees must participate in organizational decisions through their representatives. This practice will increase mutual communication and employee's perception about organization ownership. That will lead to committed work force. The current study is conducted in banking sector of twin cities. It must be applied to marketing firms. Healthcare department, educational institution and SME's sector to get enrich information about the underline mechanism.

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