The Practice of Human Capital Reporting Among Australian Financial Institutions

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ABSTRACT

Within the field of intellectual capital), human capital has received significant emphasis. This paper examines the reporting of human capital performance in the Australian banking sector, a context where human capital is important to competitive advantage. Utilising Sveiby's (1997) Intangible Assets Monitor, a content analysis is performed of annual and special purpose reports. The paper finds significant diversity in levels and focus of human capital reporting and significant reporting that exhibited corporate social responsibility-stakeholder concerns. These findings have implications for policy and research in terms of extended performance reporting.

Keywords: intellectual capital, human capital, voluntary disclosure, Australia

INTRODUCTION

In the transition to the information age, the intellectual capital (IC) of organisations, such as competencies, processes and people have become the central sources of current and future wealth (Kaplan & Norton 1996; Petty & Guthrie 2000). Concurrently, businesses are beginning to embrace formalised approaches to manage and report IC, with the ascribed benefits of doing so including business growth, improved financial performance, more effective strategic planning and enhanced productivity (Department of Industry, Science, & Resources, 2001).

Within the IC discipline, human capital has often been singled out as being of prime importance in organisational value creation (Fitz-enz, 2000; Bontis and Fitz-enz, 2002) and a significant influence as a source of innovation (Sveiby, 1997). In light of this, this paper examines how key performance indicator (KPI) reporting discloses the performance of organisations in managing their human capital (as one component of IC). The reason for focusing on KPI reporting specifically is that these quantitative indicators of performance are often considered to be a form of high quality disclosure (Patten, 1995; van der Laan Smith, 2005). The research site is the Australian banking industry, a sector that is both one of the fastest growing segments of the Australian economy (Australian Bureau of Statistics, 2005) and one where human capital is important.

INTELLECTUAL CAPITAL AND HUMAN CAPITAL

There is general consensus that IC can be usefully characterised in terms of a tri-partite model comprising human capital, relational capital and structural capital components (Edvinsson and Malone 1997; Sveiby 1997). Human capital (employee competences) in particular refers to the skill, training and education, and experience and value characteristics of an organisation's workforce. In the process of creating value from IC, the role of human capital is central. Skilled and engaged employees are required to drive innovation and both create and subsequently realise the benefits of favourable customer, supplier and broader external relations. It is for these reasons that the management of human capital has been cited as critical for businesses if they are to compete effectively (Sveiby, 1997). Indeed, within the IC literature, human capital has often been singled out as being of prime importance (Fitz-enz, 2000; Bontis and Fitz-enz, 2002), where "people, not cash, buildings or equipment, are the critical differentiators of business enterprise", (Fitz-enz, 2000, p.1).

Measuring and reporting IC and human capital in particular can be an important means of ensuring that all stakeholders are fully informed of the value creation potential of the business. While a plethora of models for the measurement of IC have been developed, one of the earlier and better-known frameworks is the Intangible Assets Monitor developed by Sveiby (1997). The Intangible Assets Monitor focused on the identification of measures based on four different intangible asset value creation modes: growth, renewal and innovation, efficient utilisation and stability. Based on the relative emphasis of these modes in the firm's strategy, corresponding indicators are chosen across the three IC components of employee competence, internal structure and external structure (Sveiby, 1997). Consistent with the focus on human capital here, only those relating to employee competence are outlined below:

- Growth – Example indicators include number of years in profession, level of education, competence index, competence turnover

- Renewal/Innovation – Example indicators include the number of competence-enhancing customers, diversity, training and education costs
- Efficiency/Utilisation – Example includes the proportion of professionals in the company, value added per employee/professional, profit per employee/professional
- Stability – average age, seniority, relative pay position, turnover rate of professional component of workforce.

While the Intangible Assets Monitor recognises that value can be created in four different ways across the three IC components, at its centrepiece is the notion of people as the organisation's profit generators (Sveiby, 1997). As such, it is particularly relevant to the examination of how human resources are accounted for, and comprises the framework that will be utilised in the empirical section of this study.

RESEARCH SAMPLE AND METHOD

Banks are the largest deposit-taking and financial institutions in Australia. At the end of June 2004 there were 52 banks operating in Australia. Furthermore, as service organisations, they are primarily reliant on their human capital for competitive advantage. Four major banks: the Australia and New Zealand Banking Group (ANZ), Commonwealth Bank of Australia (CBA), National Australia Bank (NAB), and the Westpac Banking Corporation (WBC), account for over half the total assets of all banks (Australian Bureau of Statistics, 2005). Given the size of the four major banks in Australia, these organisations are selected as the research sample.

Content analysis is used as the research methodology for this empirical study. It is widely used to evaluate the nature and extent of disclosure (Guthrie and Parker, 1990; Hackston and Milne, 1996). Content analysis requires the selection of a 'unit of analysis' (Holsti, 1969). The unit of analysis for the empirical research was the non-financial key performance indicator (KPI) in line with prior studies that have used the presence of quantitative information as a proxy for a level of quality in the disclosure (Patten, 1995; van der Laan Smith, 2005). The content analysis was thus limited to the non-financial data available through company annual reports and special purpose reports that contained stakeholder information. Reports for the year ended 2005 were analysed. The results of the coding process are presented in the next section.[1]

RESULTS

Table 1 presents the results of analysing the KPIs reported by the sampled banks in terms of the Intangible Assets Monitor. As indicated, there is variety both in terms of the number of KPIs reported and the proportion that can be related back to the individual value creating dimensions of Sveiby's (1997) intangible assets. Bank A reports the lowest number of KPIs at 6, while Bank D reports the highest at 22. In contrast, however, Bank A reported the highest proportion of KPIs that related to Sveiby's (1997) value creation modes (6/6 or 100%) while Bank D reported the lowest (8/22 or 36%), with Bank B and Bank C reporting intermediate proportions (7/14 or 50% and 6/15 or 40% respectively). Indeed, in relation to KPIs that could not be related directly to the Intangible Assets Monitor, these tended to focus on

[1] Where individual KPIs were considered to be sub-sets of the same performance dimension, they were combined for analytical purposes.

workforce diversity, health/injury and work/life balance. As such, they reflect a more stakeholder-oriented or corporate social responsibility (CSR) perspective where the focus on reporting is not on 'value created from human capital' but on 'value provided to employees as a stakeholder group'.

Comparing across the banks also reveals significant diversity in the KPIs reported against the value creation modes of growth, renewal/innovation, efficiency/utilisation and stability. Bank A focused more on the efficiency/utilisation (50%) and the stability (33%) of its human capital. In contrast, Bank D exhibited more CSR/stakeholder concerns (other KPIs were 64%) and within the IC framework, focused more on stability (23%) and renewal/innovation (14%). In terms of IC focus, Banks B and C were again different, with Bank B emphasising stability (21%) and growth (14%) while Bank C emphasised renewal/innovation (20%) and stability (13%). Relatively less attention was placed on the growth aspect of human capital.

CONCLUSIONS AND IMPLICATIONS

Overall, the findings of the paper indicate diversity in human capital reporting levels, the co-existence of IC and CSR/stakeholder concerns in reporting on human capital, and variation in the value creation focus of organisations when reporting their performance in managing human capital.

While the findings above need to be interpreted with caution given the small sample size and the focused examination of KPI reporting of human capital within banking, they nevertheless have implications for practice and research. Firstly, the question of mandating reporting of extended performance needs to be examined. Currently, IC reporting is predominantly voluntary. Although studies that find performance benefits for better disclosers (for example, Linstock Consultants, 2004; Petty and Cuganesan, 2005) support arguments for voluntary disclosure regimes, the heterogeneity in observed disclosure suggests that greater consistency in reporting practice is required if comparability across organisations is to be attained.

A second issue involves the issue of convergence between IC and CSR concerns. Both were evident in the reporting practices observed and both movements are interested in issues of sustainability, with IC focused more on the sustainability of future economic cash flows through knowledge flows while CSR/stakeholder considerations emphasise questions of the environment, society and broader stakeholder groups. Thus the issue of convergence in reporting needs to be further examined. A final issue for consideration by future research in particular is the alignment between externally reported KPIs, internal measures and incentive systems and the management practices actually enacted within organisations. Future research needs to investigate the linkages between extended performance management, measurement and reporting and the consequences of particular approaches to the task of managing IC, which at best is a problematic task (Cuganesan, 2005).

Table 1 – Coding Results: Sveiby Intangible Assets Monitor

	Bank A	Bank B	Bank C	Bank D
Growth		• B1 - New hires • B2 - New customer facing hires	• C1 – New hires	
Renewal/ Innovation	• A1 – Training programs attended/completed	• B3 - Training programs attended/completed	• C2 - Training programs attended/completed • C3 - Average training and development spend/employee • C4 - Number of feedback/comments and amount implemented	• D1 - Training programs attended/completed • D2 - Employee satisfaction - training and development • D3 - Number and $-value of employees accessing external tertiary training
Efficiency/ Utilisation	• A2 - Product sales per retail staff member • A3 - Total operating income per full-time (equivalent) employee • A4 - Staff expense/Total operating income (%) • A5 - Staff Numbers and Expenses	• B4 - Staff Numbers and Expenses		
Stability	• A6 - Engagement percentile ranking	• B5 - Engagement score • B6 - % of staff with positive perceptions about career opportunities • B7 - Employee turnover	• C5 - Satisfaction/ Engagement[1] • C6 - Average staff turnover	• D4 - Employee commitment • D5 - Employee morale • D6 - Employee satisfaction[2] • D7 - Staff turnover • D8 - Retention of graduates
Number of Other KPIs and Theme		• 7 KPIs focusing on workforce diversity, code of conduct compliance and health/injury.	• 9 KPIs focusing on workforce diversity, work/life balance and health/injury.	• 14 KPIs focusing on workforce diversity, work/life balance, health/injury and access to employee-support facilities provided by the organization.

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