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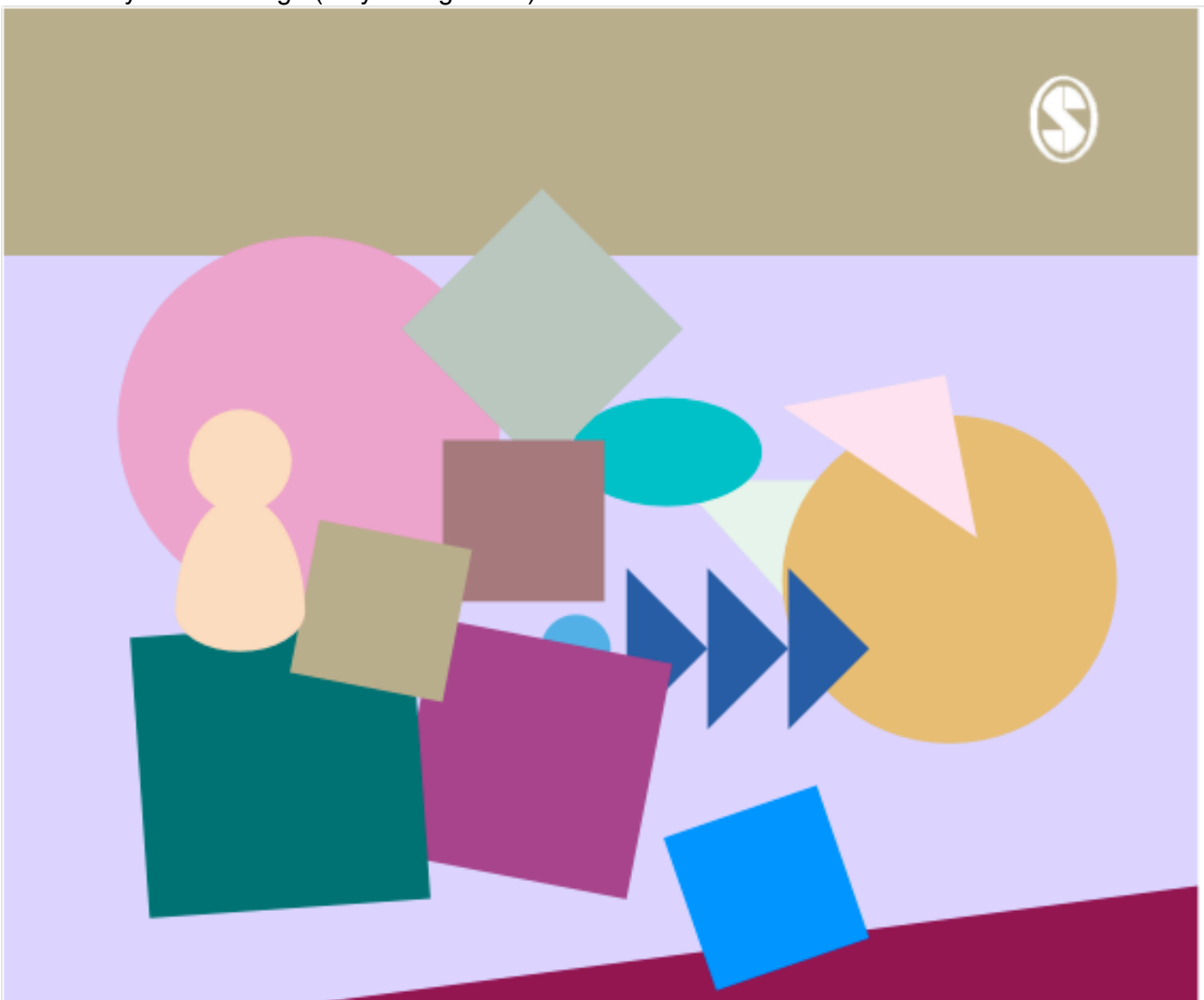

Skills in Business

The role of business strategy, sectoral skills development and skills policy

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INTRODUCTION

> **'Skills have become the global currency of the 21st century.** Without proper investment in skills, people languish on the margins of society, technological progress does not translate into economic growth, and countries can no longer compete in an increasingly knowledge-based global society. But this 'currency' depreciates as the requirements of labour markets evolve and individuals lose the skills they do not use. Skills do not automatically convert into jobs and growth.'
>
> OECD (2012a: 3)

The 2011 OECD *Skills Strategy* captures much of the raison d'être for this book. So what are the reasons that skills may not automatically convert into jobs and growth? One answer lies in two main strands of skills policy, education on the one hand and training on the other, being dominated by what are known as the 'supply side' considerations – the belief that if we improve the supply of skills, economic growth and enhanced competitiveness will follow. The principles that underpin this approach to skills policy are still those of market failure and human capital theory. We argue that while these guiding principles were appropriate for economies in the 20th century, they are now becoming inadequate on their own to understand the role of skills in 21st century economies. Nevertheless, they are still used to inform policy approaches to education and interventions to remedy 'market failures' at the lower reaches of the labour market.

The second answer to the difficulties in converting skills into jobs is our tendency to overlook factors that are influencing the productive system, the ways in which production is organised within businesses, as it is this that drives the creation of jobs as well as the type of skills demanded. Thus, while the OECD statement captures the changing nature of skills demand in the 21st century, it unfortunately tells us nothing about what is driving this demand. It is here that our book makes its major contribution. The late 20th century and early 21st century have witnessed major transformations of the economy creating new demands that conventional supply side policies cannot meet. What we provide is a theory of the business drivers of skills, enabling us to

explain how and why the demand for skills is changing. At the moment our understanding of employers' demand for skills is at best fragmentary and at worst lacking in theoretical coherence. Yet, it is here with respect to employers' behaviour that new forms of government action are needed if countries are to compete effectively in the intensively competitive global markets that we all now face.

The main source of the problem is the fact that we have never defined what 'skills policy' means. We argue that the lack of proper understanding of what skills policy means leads to the confusion that skills policy, especially in the Anglo-Saxon world, is always synonymous with human capital theory, creating the view that investing in skills is what skills policy is all about. It is not. To develop an effective skills policy that is also high skills-oriented and utilising, skills policy needs an understanding of how skills demand is derived within a productive system. Skills policy, viewed from this perspective, is about what might influence the employers' competitive behaviour and their business strategy.

In the next seven chapters of this book, we will explain the sources of our argument, and how we arrive at this conclusion. The following is the structure of the book.

Chapter 1

The book starts by showing how the conventional approach to skills policy among Anglo-Saxon countries, namely to concentrate on improving the supply of skills and to leave it to market forces to ensure that these skills are used to improve economic performance, has become unfit for purpose. The approach worked for a period in the mid to late 20th century but is now running into serious problems. Moreover, comparative analysis reveals that reliance on the market to convert this supply of skills into skilled highly skilled jobs is now becoming a failed strategy. Other countries such as Germany and Singapore have adopted very different strategies and have had more success in delivering higher-skilled jobs with higher incomes for their citizens.

To understand these different outcomes we need to start by examining the factors that drive the demand for skills from employers. These are to be found in the business environment within which employers make their decisions about which type of product they will produce and how they will use the available technology to secure a competitive advantage in the market. These factors range from the availability of opportunities in the national and international markets, the supply of skills from the vocational education and training (VET) system, the cost of labour, how they can use those skills which shaped by the industrial/employee

relations system, the system of economic governance and others. These are all factors over which governments have some influence, and how they use that influence through their approach to skills policy plays an important part in explaining why some countries such as Singapore and Germany have succeeded in enabling companies located there to compete at the leading edge of world markets while countries such as the UK have been less successful.

One of the most important factors shaping these approaches to skills policy is the location of the country in international markets. In the UK with its long history of dominance in global and later Empire markets, the policy was to minimise state intervention and rely on the market to deliver growth. However, this policy failed to sustain a great deal of industrial production resulting in the replacement of those jobs by low-skilled, low-paid jobs in the service sector. In countries such as Germany that had to break into world markets dominated by British and American companies, the state was more active in helping establish a framework within which the social partners, employers and unions collaborated in developing a highly skilled labour force for companies competing in high-value engineering products. In Singapore, after the Second World War, the government had to establish a framework that would ensure that foreign multinational corporations (MNCs) were attracted to the country in order to help them break into world markets. Once having a foothold in global markets, the government's policy ensured that firms moved into high value-added product markets creating high-skilled, high-paid jobs. As will be discussed in Chapters 6 and 7, these 'interventions' are key to forming the institutional logics that govern the way employers see how they compete.

This chapter is devoted to explaining how these broader government policies were instrumental in generating these different outcomes at the organisational level. It is presented in the form of a historical overview, not for the purpose of understanding the history of the countries concerned but to show how the demand for skills is shaped by two specific factors that are usually absent from the current debate, namely the importance of the position occupied by a country in global markets in shaping the approach to skills policy and how the type of industry, or 'production system' as we call it, that dominates the domestic economy shapes the demand for skills.

Chapter 2

Rarely would any skills analysis start from what businesses actually are. This is the starting point of our book before building our strategic skills model. Key to this unusual starting point is to recognise that businesses

are 'purposive entities'. In other words, they exist for a reason, and the reason is seldom about learning or skills – unless you are in the education and training business. But of course learning and skills are all very important to the success of a business and any organisation. So how do we get learning and skills back into the business performance equation? The answer lies in business strategy – the very element that makes a business 'purposive'.

This chapter therefore has two sections. This first identifies the inadequacy of the business strategy research that may include skills but has never formalised the role of skills in any business strategic model. The end result is a simplistic understanding of the relationship between skills and business performance, which at best means that skills are 'unproblematic' in any of the existing strategic models. Skills (higher or lower) are simply a given in a business model. Generally, skills are treated as a cost factor. And at worse, more skills and higher skills is inevitably linked to higher business performance. The assumption is that any available skills will be translated into drivers for business performance. Well, how does it work? The first section of this chapter will show us that research has never answered this question, let alone treated it seriously.

The second section of this chapter will propose a new strategic skills model. The new model makes two major contributions compared with previous efforts. The first contribution is that business strategy is the key concept to influencing the level of skills utilisation. The second contribution is that business strategy consists of two components, product market strategy and competitive strategy, each of which impacts skills in very different ways. The product market strategy determines the type of product or service the company will market and the type of technology it will employ to do so, and the competitive strategy identifies how the firm will seek to a achieve a competitive advantage in the market to secure its future. The product market strategy adopted in turn determines the technical relations (TRs) which shape the level of skill demanded by the employer from its employees. The competitive strategy determines the interpersonal relations (IRs), which shapes how the firm manages and uses the skills of employees. At one extreme the skills of employees can be the most important source of its competitive advantage, as the other the firm can use its technology to reduce the skill required and seek a competitive advantage through the use of low-cost, low-skilled labour. Unlike previous attempts, our strategic skills model allows the business owner a degree of choice in selecting any combination of product market and competitive strategies. Likewise, there is no universal best-approach assumption, other than that different strategic combinations will lead to different levels of skills utilisation and different types of skills demanded.

Chapter 3

This chapter is the first of the two chapters that examine the strategic skills model in depth. In Chapter 3, we focus on how the product market strategy of the firm determines the TRs which shape the *level of skill* it demands from employees. Crucial to the TRs is the type of technology the firm uses to manufacture its products or deliver its services. The product market strategy is shaped by the business opportunities and market environment in which the firm operates, the knowledge of the entrepreneur and type of technology available at any one point in time. History is therefore crucial in determining these relationships and we therefore have to adopt a historical perspective in order to show how these relationships worked out in practice. Once established and proved effective in delivering performance these technical relationships may persist over time.

The chapter distinguishes between different types of TRs. It starts from the early industrial form of mass production, whose TRs were characterised by combining mechanised production with a high division of labour that first occurred in the UK. This was followed by Tayloristic mass production characterised by large organisations using Taylorist forms of management and the moving assembly line that was developed in the USA – what we term the 'mature form' of mass production characterised by the application of new information technology to mass production capable of producing smaller batches which had its origin in Japan. More recently, we have seen the emergence of knowledge-intensive forms of production that started in the USA in Silicon Valley. Each of these forms of production makes different demands on the level of skill required from managers and while-collar employees as well as manual workers and service staff. As the mix of these systems change through time so too do the skill demands on the VET system.

Chapter 4

In Chapter 4, we explore how the competitive strategy adopted by the employers shapes the IRs, the ways in which companies manage and *use the skill* of their employees. Employers using early industrial systems of production usually sought a competitive advantage through their mechanised technologies and an extreme form of the division of labour to create jobs that required little skill, enabling them to recruit unskilled females and young people to produce the low-cost products that delivered the employers' competitive advantage. The skills that mattered were those of the entrepreneur and a handful of managers. In our

strategic skills model, this form of production had huge implications for the competitive strategy and therefore interposal relations of the workplace. In effect, the productive system would be focusing on 'task focused' processes, which tended to make use of very limited ranges of worker skills. This process of 'deskilling' was best represented by the emergence of mass national markets in the USA where employers were able to use Tayloristic forms of the division of labour together with the moving assembly line to deskill other production processes and secure their competitive advantage by lowering the cost of consumer products. However, while deskilling one large section of the productive system, these were complex technologies requiring not only professional managers but also skilled engineers and administrators. These were the staff whose skills were crucial to securing a competitive advantage in the market and where company resources were devoted to developing their skills.

With the advent of mature mass production the source of the company's competitive advantage shifted from reliance on the use of skills by managers, professionals and administrators to those of the core production or service delivery staff. Not only that, but the nature of the skills that were utilised shifted from these required to function in a command and control organisation to those required for the flatter high-performance organisation. In order to keep these skills up to date, their character changed. Management no longer relied on command and control systems of authority but now had to acquire more participative skills in leadership, while other employees required problem solving, communication and teamworking skills. Commitment to the values of the company also starts to become important for most employees. The commitment of employees to the company and the use of these 'new' skills now had to be managed through the use of competence-based systems of learning and skill formation. Therefore, the result of this development 'pushed' the competitive strategy towards the more 'people-focused' type of work processes.

With the development of knowledge-intensive forms of production for both products and services, the use of employee skills become even more central to securing the competitive advantage of the company. Almost all the staff are highly qualified and managers rely on the continuous application of judgement by highly skilled staff to produce the creativity and quality that are crucial to the company's advantage in the market. Here commitment to the values and goals of the company facilitates the exercise of discretionary effort that enhances the overall performance of the organisation. The management of employee commitment, learning and skill formation become central to the qualities expected of managers and team leaders.

Chapter 5

In Chapters 3 and 4, we have assumed that different types of TRs tend to be associated with different types of IRs: Taylorist mass production with the development of management and white-collar skills but low skills for manual operatives, and knowledge-intensive production with high levels of skill use by virtually all employees. This is a relatively static snapshot of what in reality is a continuous process of change, so in this chapter we shift the focus. In this chapter, we focus directly on the process of change as firms continuously seek to adapt to the market through the introduction of change in their business strategy, which in turn affects either the technical or IRs or, as sometimes happens, both dimension at once.

The academic literature has already identified some of the problems encountered in the process of change. Here we are especially concerned with the decision making of owners an senior managers because it is they who are the powerful agents in changing strategy and through that the TRs and IRs dimensions. Yet there is evidence that this group are often resistant to changing their business strategies. At the same time, it is possible that managers and workers may lack the skills to implement the new practices associated with, say high-performance work practices (HPWPs). There is also substantial evidence that even if owners and senior managers want to change their business strategy and introduce change in either TRs (e.g. through introducing new technology) or IRs (e.g. through introducing HPWPs), that this is a very difficult process which can take considerable time with no guarantee of success. So there is a risk element as well as the knowledge that is required in effecting changing business strategy.

To explore these and similar issues in greater depth we examine the case of Glenmorangie, a company that successfully introduced change along the IRs dimension through adapting high-performance management practices to a massproduction technology. Yet many companies may not be so successful, so we move on to examine in detail another company where the attempt to introduce HPWPs to a system of batch production of airframes encountered major problems. This case illustrates the wide range of contextual factors and barriers that firms encounter in their attempts to change management practices and consequently the process of skill formation in the enterprise.

Chapter 6

Having traced the mechanisms through which business strategy drives the process of skill formation in organisations and how contextual factors may hinder or prevent the process, we return in Chapter 6 to our

initial focus on policy approaches. The aim is to apply the lessons we have learnt to questions of national policy. What is abundantly clear is that the crucial area where employers and senior managers make their decisions about business strategy is in the market environment of their particular industry or sector. It is here that they identify the opportunities either in the domestic or international markets and how they should respond. That response is shaped by the interaction of factors at two levels, the national and the sectoral.

At the national level these are factors such as the availability of finance and technologies, the cost and availability of labour, the supply of skills, and the perceived threats to their business from competitors. At the sector level they are affected by the regulations that govern their industry and its products or services (including those that governing the use of labour), the demands from customers in the supply chain to meet industry standards, the availability of skills from the local VET system, the relations with unions and professional bodies that influence how they can use the skills of employers and so on. It is also at the sector level that these factors (what we call the 'institutional logics') interact and shape the decisions of employers about their business strategies and their use of labour. In view of this interaction, it is therefore important that action be made at the two levels. First, a sectoral agenda has to be set at the national level, though some of the early action may have to be facilitated by the government. This means a vision of an industrial strategy that will focus on building those sectors in which the country has, or can build, a competitive advantage in world markets and actions to create an infrastructure that will support this vision.

Crucially, this will involve building institution at the second level, that of the sector or industry that will ensure the implementation of the strategy. We use 'institution' in an environmental sense, which may include regulations and processes that govern the way competitors compete (e.g. more incentive for high value-added productive systems). This means the formation of powerful, employer-led sector bodies that have the capacity to influence the business environment. This means the power to shape the regulations that govern the industry or sector, to shape the institutions that supply the skills and to influence the local employee organisations such as unions that can help reduce the attraction of the low-skilled route. It has to be a body that can influence regulations embedded in the supply chain and provide assistance to employers to pursue a higher value-added, high-skills business strategy. Many of the levers to introduce such a policy approach are already in existence, in many respects it means just coordinating them within the context of a policy that places the encouragement of companies pursuing high value-added strategies and highly skilled, good-quality jobs as a national priority. In this chapter, we conclude by placing such a policy in context and identify/discuss what we can expect from such an approach.

Chapter 7

This is the conclusion chapter. Instead of providing a summary of the analysis, this chapter is used to put forward a set of important and related points that have not been formally mentioned in the previous chapters. Some of the points are crucial in the successful implementation of the strategic skills model and the sectoral approach to skills development. For example, what role does supply side policy play, if demand factors are so important in shaping skills demand and skills utilisation at work? Would our proposed model work in every sector? What do we expect and are we expecting too much from skills? What is the fine balance between high skills utilisation, high-performance working and work intensification?

Also, before the reader begins the book, it might be useful to spell out our argument in the following summary:

1. That the demand for skills is primarily determined by the changes in the productive system and that these demands are constantly changing through time.
2. That societies have developed different ways of responding to these demands in terms of their policy frameworks and that these frameworks adapt to these changes in demand in different ways.
3. That human capital theory has provided just one way of shaping these policy frameworks. It provided a basis for a framework that 'worked' for a limited period of time in the Anglo-Saxon countries, when the modern corporations associated with Taylorist mass production were expanding in the mid-20th century, with their huge bureaucracies that required a constantly growing supply of educated personnel for the new white-collar jobs. Since then, as economies have become dominated by different types of productive system, namely mature forms of mass production and knowledge-intensive production, the demand for skills has shifted pushing issues of skill utilisation to the fore. In this context human capital theory and the notion of market failure that provides its theoretical consistency has become increasingly irrelevant, only capable of generating a skills policy that is based upon augmenting public provision for training and increases in qualifications, and nothing more.
4. What is required in the current context is a skills policy that is focused on influencing the company's productive systems towards the adoption of business strategies based on high value-added forms of production and high skills utilisation in order to provide their competitive advantage. Only then will there be the basis for the demand for high-skilled jobs.

Figure 0.1 summarises the argument by illustrating the changing meaning of skills policy. It shows on the right-hand side that human capital theory uses the concept of market failure to provide some general reasons for what is claimed to be employers' (and individuals') 'under investment' in training (e.g. uncertainty, lack of information, barriers to access capital funds or technology and so on). But all this can provide is policy prescriptions for augmenting public provision for training and increases in qualifications. It is too blunt an instrument to provide any effective policy prescription to encourage the adoption and use of mature mass production and knowledge-intensive forms of production that depend on high levels of skills utilisation. To do that the Anglo-Saxon nations have to explore how skills policy can shape the left-hand side of Figure 0.1, something that other societies have been already been experimenting with.

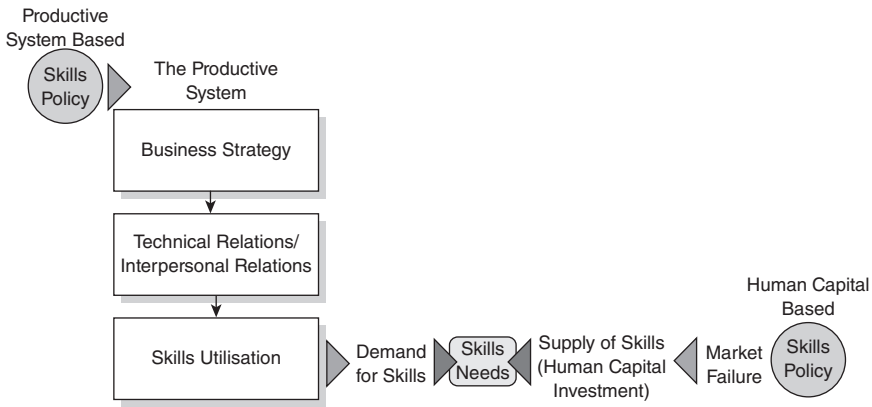

Figure 0.1 The changing nature of skills policy and skills demand

The left hand side of Figure 0.1 illustrates why contemporary skills policy demands an understanding of the productive system. This is because of the key role that business strategy plays in influencing skills demands. The Figure shows that within any productive system, the level and extent of skills deployed are influenced by the relevant business strategy via technical relations (TRs) that determine the demand for skill levels and interpersonal relations (IRs) that determines the ways in which skills are used. It is the interaction of these two dimensions which determines the nature of the workplace in terms of the value it adds to the output, the design of work and work processes and the way that employees and their skills are deployed. As we will show in later chapters, the specific combination of TRs and IRs directly impacts on skills utilisation and therefore skills demand.