HOW TO SET UP GREAT HR FUNCTIONS: CONNECT, PRIORITIZE, IMPACT
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CREATING PEOPLE ADVANTAGE 2014-2015

HOW TO SET UP GREAT HR FUNCTIONS: CONNECT, PRIORITIZE, IMPACT

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BUSINESS LEADERS TODAY ARE faced with an extremely dynamic business environment, characterized by technological innovation, blurring boundaries among industries, shifts in customer behavior, scarcity of talent, and huge variations in growth across regions. HR functions need to help companies meet these challenges as true strategic partners. To fulfill this mandate, however, HR leaders need a clear view of their current capabilities, their priorities over the next three to five years, and the best way to tailor efforts to improve.

This report, the eighth in The Boston Consulting Group’s Creating People Advantage series, explores key trends in people management by considering ten broad HR topics and 27 subtopics. We looked at each subtopic’s future importance, companies’ current capabilities with regard to the subtopics, the levels of effort invested in them, and how urgently each subtopic needed action. We also explored the link between people management capabilities and economic performance.

In this year’s survey, 3,507 respondents from 101 countries participated, representing industries including industrial goods, consumer goods, and the public sector. In addition, we interviewed 64 HR and non-HR executives at leading companies around the world. The following are among the most compelling findings:

- **HR capabilities correlate with economic performance.** Companies that have strong capabilities in HR topics—such as talent and leadership; engagement, behavior, and culture management; and HR strategy, planning, and analytics—show significantly better financial performance than companies that are weaker in those areas.

- **Analytics and key performance indicators (KPIs) give HR a seat at the table.** There is a strong correlation between the use of KPIs and the strategic role of HR. HR leaders who want a role in strategic discussions with the business must be able to quantify workforce performance. This goes beyond “input” metrics, such as cost and head count, toward more sophisticated “output” indicators, such as productivity.
• **KPIs should link to strategic actions.** Even high-performing organizations, which are generally more data driven, do not use their KPIs systematically to formulate strategic actions. A clear prioritization and selection of KPIs and tools is needed to achieve best-in-class results.

• **Globally, the leadership and talent management topics are the ones in the most urgent need of action.** Across industries and regions, most respondents identified leadership, talent management, behavior and culture, HR and people strategy, employee engagement, and strategic workforce planning as the topics that are most urgently in need of action by their organization.

• **HR departments need to be more consistent in their investment decisions.** Many organizations need to invest their efforts in HR topics more strategically to build capabilities. Among the three HR topics rated as most important (out of a total of ten), companies showed merely average capabilities, and they were not specifically targeting their investments to improve those areas.

• **HR needs to listen more to internal clients.** Non-HR respondents reported a strong need for action with regard to approximately 40 percent of HR topics, particularly in core HR capabilities, such as staff capabilities and communication.

Fundamentally, the report identifies three hallmarks of great HR functions:

• They **connect** by partnering with stakeholders inside and outside of the company to improve operational and financial performance.

• They **prioritize** by using data-driven insights to identify and focus on the most urgent HR priorities.

• They create an **impact** by using KPIs and steering tools to support the organization and its strategic goals.

The report also includes case studies of specific HR best practices from Deutsche Lufthansa AG, PepsiCo, and Transnet.
The Boston Consulting Group (BCG) has published an annual Creating People Advantage report—partnering, in alternating years, with the World Federation of People Management Associations (WFPMA) and the European Association for People Management (EAPM)—since 2007. In this year’s report, BCG and the WFPMA conducted a survey of human resources professionals and other business leaders around the world. The report summarizes the survey’s findings, provides a comprehensive snapshot of people management priorities and capabilities, and explores their link to companies’ operational and financial performance.

This report serves as an overview, with highlights of key findings. Follow-up reports will provide more detailed findings and in-depth analyses on specific topics.

Survey Methodology
More than 3,500 respondents from 101 countries participated in our online survey in 2014. (See Exhibit 1.) We also conducted 64 in-depth interviews with HR and non-HR executives at leading companies in a variety of regions. (For more about the survey methodology, see Appendix I; for a list of executive interviewees, see Appendix II.)

To identify HR priorities, we analyzed ten broad HR topics, which were further broken out into 27 subtopics. (See Exhibit 2.) For example, the topic of training and development includes three subtopics: training and learning, career models and competencies, and assignment management. This categorization allowed us to look at big-picture trends and to drill down into specific analyses. We asked the survey respondents to rank each of the 27 HR subtopics by its future importance, their companies’ current capabilities in the subtopic, and the levels of effort invested in the subtopic.

Exhibit 2 shows the ten HR topics ranked by respondents’ assessment of future importance. The 27 subtopics are color-coded according to the levels of effort invested. Interestingly, while levels of effort broadly link to future importance, there are notable exceptions. For example, leadership, talent management, and strategic workforce planning are among the highest priorities, yet they received only average levels of investment. Clearly, companies must be more consistent in their investment decisions.

In addition, we combined future importance and current capabilities into a single metric—defined as urgency for action—and ranked all 27 subtopics by this dimension.¹ The subtopics most urgently in need of action across all industries were leadership, talent management, behavior and culture, HR and people strategy, employee engagement, and strategic workforce planning. (See Exhibit 3.)

(For more on leadership, see the sidebar “PepsiCo Offers Its Executives a Master Class in Strategy.”)
EXHIBIT 1 | More than 3,500 Respondents from 101 Countries Participated in Our Survey

EXHIBIT 2 | The Analysis Includes 10 Broad HR Topics and 27 Subtopics

Note: Only countries with more than ten responses are shown; of the total, 84 respondents did not specify a country. There were 3,507 respondents in total.
Non-HR Respondents Say That Capabilities Need to Improve

Both HR and non-HR respondents identified the same HR subtopics, such as talent management and leadership, as priorities—that is, the areas with the lowest current capabilities and the highest future importance. However, there were significant differences in the perceptions of their companies’ people management capabilities. (See Exhibit 4.)

Virtually across the board, HR respondents rated capabilities more highly than non-HR respondents. They also did not consider any areas to be in urgent need of action. By contrast, non-HR respondents categorized nearly half of the 27 subtopics as urgently needing action. This was especially true for talent management and leadership, two highly important subtopics for which non-HR respondents think their organizations show low capabilities.

PEPSICO OFFERS ITS EXECUTIVES A MASTER CLASS IN STRATEGY

PepsiCo has developed a well-deserved reputation as a high-performing company that invests in leadership training and development. To build on this, the company recently implemented a strategy master class.

The program was designed around 15 PepsiCo-specific case studies of major strategic decisions over the past 20 years, such as significant acquisitions or an expansion into developing markets. Through these case studies, the training provides a comprehensive foundation for strategy composed of several aspects. First is a uniform set of strategy fundamentals, including consistent definitions, building blocks, and guidance questions. Second is a set of tools to help executives learn how best to lead themselves, lead others, and lead the business. Third—and most important—is a set of five tactics that executives can use to successfully take on new strategic challenges:

- **Frame.** Clearly assess the problem, including the company’s aspiration, objectives, and scope.
- **Diagnose.** Look at the current situation as well as at future scenarios, including external trends and forces, the company’s competitive position and performance, and the relative attractiveness of different options.
- **Design.** Generate a solution that aligns with the company’s portfolio strategy, business strategy, and business model strategy and clarify where to play and how to win.
- **Test.** Stress-test the strategy to ensure that it is coherent, robust, and ready to execute.
- **Execute.** Implement the new strategy, clarifying initiatives, owners, resources, success metrics, and a mechanism for capturing lessons learned.

The training is being rolled out in two stages, starting with a two-day, in-person seminar for senior leaders, led by one of PepsiCo’s C-level executives. A broader segment of PepsiCo executives will then receive a four-hour e-learning version of the class hosted on PepsiCo’s internal education platform. Although the program is still being implemented, the benefits are already clear: PepsiCo’s senior leaders will soon gain additional insights and training that will help drive the company’s continued success in a dynamic global market.

**Connect.** Great HR functions have a strong relationship with their internal clients and thus understand the organization’s most urgent needs and strategic goals. This connection allows them to address the day-to-day realities of business units and to meet long-term considerations, such as the supply and quality of employees.
Creating People Advantage 2014-2015

(For more on talent management, see the sidebar “Decoding 200,000 Global Talent Profiles.”) Also, HR respondents attributed a higher importance to all subtopics—almost 10 percent on average—than did non-HR respondents, and they rated their capabilities as consistently higher.

Equally distressing, the strongest misalignment was in the area of HR staff capabilities, HR communication, works councils and union management, and HR processes. (See Exhibit 5.) HR and non-HR respondents agreed on the level of capabilities in the subtopics employer branding, generation management, and assignment management.

In many organizations, the HR function is perceived as not meeting the expectations of its internal clients. To address this misalignment, HR departments must better align with business units throughout the enterprise, to increase the impact of HR and generate stronger business performance.

**Note**

1. Urgency is determined by calculating the difference between future importance and current capabilities, and then multiplying that difference by future importance.

EXHIBIT 3 | Leadership, Talent Management, and Behavior and Culture Are Most Urgently in Need of Action

<table>
<thead>
<tr>
<th>HR subtopics according to urgency rank¹</th>
<th>HR subtopics according to urgency rank¹</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Leadership</td>
<td>11 Employer branding</td>
</tr>
<tr>
<td>2 Talent management</td>
<td>12 Social media</td>
</tr>
<tr>
<td>3 Behavior and culture</td>
<td>13 Rewards and recognition</td>
</tr>
<tr>
<td>4 HR and people strategy</td>
<td>14 Other HR and workforce analytics</td>
</tr>
<tr>
<td>5 Employee engagement</td>
<td>15 HR staff capabilities</td>
</tr>
<tr>
<td>6 Strategic workforce planning</td>
<td>16 On-boarding</td>
</tr>
<tr>
<td>7 Career models and competencies</td>
<td>17 Generation management</td>
</tr>
<tr>
<td>8 HR communication</td>
<td>18 HR services and systems</td>
</tr>
<tr>
<td>9 Performance management</td>
<td>19 Recruiting processes</td>
</tr>
<tr>
<td>10 Training and learning</td>
<td>20 Recruiting strategy</td>
</tr>
<tr>
<td></td>
<td>21 HR organization and governance</td>
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<tr>
<td></td>
<td>22 HR processes</td>
</tr>
<tr>
<td></td>
<td>23 Labor costs and restructuring</td>
</tr>
<tr>
<td></td>
<td>24 Diversity management</td>
</tr>
<tr>
<td></td>
<td>25 Assignment management</td>
</tr>
<tr>
<td></td>
<td>26 HR internationalization</td>
</tr>
<tr>
<td></td>
<td>27 Works councils and union management</td>
</tr>
</tbody>
</table>

Note: There were 3,507 respondents.
¹ Urgency is determined by calculating the difference between future importance and current capabilities, and then multiplying that difference by future importance.
EXHIBIT 4 | HR Respondents Rate Their Capabilities Higher Than Non-HR Respondents Do


1The sample size for HR respondents was 2,909.
2The sample size for non-HR respondents was 331.
Over the past several years, talent management has been consistently rated as one of the HR subtopics in the greatest need of action. Companies are scrambling to develop strategies, programs, and measures to recruit, develop, and retain their top talent and keep them motivated at the same time—not an easy task.

In Decoding Global Talent: 200,000 Survey Responses on Global Mobility and Employment Preferences (BCG report, October 2014), we explored this issue in depth. We partnered with The Network—an association of more than 50 job boards worldwide, with more than 200 million visitors per month on all its websites—to conduct an online survey. The survey included 33 questions about talent mobility and job preferences, 13 of which looked at demographic factors, such as age, work experience, gender, education, industry, salary, and occupation. The result is a unique database that offers strategic insights for developing people strategies.

For example, the report shows worldwide trends in talent mobility across countries, age groups, and positions, among other factors. Global mobility is widespread, with 64 percent of job seekers willing to work abroad. The U.S. is the favorite work destination, followed by the UK and Canada. Germany is the fourth most popular country to work in and the top non-English-speaking market in the group.

One of the survey’s more striking findings has to do with what people say makes them happy on the job: increasingly, workers are starting to put more emphasis on cultural aspects and less on financial compensation. Out of 26 job elements, the single most important one for all people globally is appreciation for their work. (See the exhibit below for the top ten elements.) Good relationships at the office—whether with colleagues or superiors—are critically important and come in second and fourth, respectively. A good work-life balance is the third most important job factor. The implications for companies, economies, and individuals are significant and varied; addressing them will be key for future success.

The full report is available at www.bcgperspectives.com.

### The Cultural Aspects of Work Are More Important to Employees Than Are the Financial Aspects

"How important are the following job elements to you?"

<table>
<thead>
<tr>
<th>Rank</th>
<th>Job Element</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Appreciation for your work</td>
</tr>
<tr>
<td>2</td>
<td>Good relationships with colleagues</td>
</tr>
<tr>
<td>3</td>
<td>Good work-life balance</td>
</tr>
<tr>
<td>4</td>
<td>Good relationships with superiors</td>
</tr>
<tr>
<td>5</td>
<td>Company’s financial stability</td>
</tr>
<tr>
<td>6</td>
<td>Learning and career development</td>
</tr>
<tr>
<td>7</td>
<td>Job security</td>
</tr>
<tr>
<td>8</td>
<td>Attractive fixed salary</td>
</tr>
<tr>
<td>9</td>
<td>Interesting job content</td>
</tr>
<tr>
<td>10</td>
<td>Company values</td>
</tr>
</tbody>
</table>


Note: Respondents could choose from 26 job elements; this list includes only the top ten.
EXHIBIT 5 | HR Respondents Report Higher Capabilities Than Non-HR Respondents Across All Subtopics

- HR staff capabilities
- HR communication
- Works councils and union management
- HR processes
- Recruiting processes
- Other HR and workforce analytics
- Recruiting strategy
- HR organization and governance
- HR internationalization
- Leadership
- Labor costs and restructuring
- Performance management
- HR services and systems
- On-boarding
- Training and learning
- Talent management
- HR and people strategy
- Strategic workforce planning
- Rewards and recognition
- Social media
- Employee engagement
- Career models and competencies
- Behavior and culture
- Diversity management
- Employer branding
- Generation management
- Assignment management

Note: There were 2,909 HR respondents and 331 non-HR respondents.
THE LINK BETWEEN FINANCIAL PERFORMANCE AND HR CAPABILITIES

A central finding of our survey is the correlation between HR capabilities and financial performance. We segregated the top 100 and bottom 100 companies according to financial performance, as measured by average operating margins and average revenue changes during the previous two years (2012 and 2013), and we included only companies with at least 50 employees. (See Exhibit 6.)

We found that companies that are stronger in people management have a correspondingly higher financial performance. Among high performers, no HR subtopic is designated as being in urgent need of action.

In contrast, companies with the worst financial performance show a greater need for action across virtually all 27 HR subtopics, with seven clearly in the red zone and three more at the border.

This has been a consistent finding in previous Creating People Advantage reports and in publicly available research. Looking at the publicly listed companies that made Fortune magazine’s “Best Companies to Work For” ranking in 2014, and their share prices over the decade from 2004 to 2013, it is clear that the most successful people companies consistently outperformed the market, by nearly 100 percent.¹

In our survey data, there was a troubling difference in capabilities between companies that are high performers and those that are low performers. (See Exhibit 7.)

This was greatest in HR internationalization, social media, employee engagement, career models and competencies, and behavior and culture.

High- and low-performing companies also have different priorities in terms of future importance. HR internationalization, HR and workforce analytics, recruiting strategy, HR and people strategy, and career models and competencies are significantly more important in high performers than in low performers.

One possible explanation for the superior HR achievement of high performers is their strategic allocation of investment. (See Exhibit 8.)

Our analysis shows a strong relationship between the levels of effort invested and the future importance of the subtopics being addressed. That is, high performers are more strategic in the way they allocate their efforts; they take a systematic approach to improving capabilities; they are able to accurately distinguish high-priority topics from lower priorities; and they can then direct their resources accordingly, potentially improving their financial performance.

We found that low performers, by contrast, have a more arbitrary relationship between
EXHIBIT 6 | Companies with Strong Financial Performance Show Greater HR Capabilities

Note: High performers represent the top 100 companies (with at least 50 employees), which had the highest average revenue change and average operating margin in 2012 and 2013; low performers represent the bottom 100 companies (with at least 50 employees), which had the lowest average revenue change and average operating margin in 2012 and 2013.
efforts invested and the importance of areas targeted for improvement. Investments tend to be misaligned; the most important issues don’t necessarily win the greatest investment.

Prioritize. Great HR functions identify the most important and most urgent HR topics—both internal and external—for a company’s future and then prioritize their efforts accordingly. This allows them to get the biggest payoff for their allocation of financial investments and other resources.

This suggests that low performers don’t have a rigorous process in place for improving their people-management practices. Many companies lack a way to clearly identify the subtopics that are most important to their organization. They struggle to implement governance that effectively targets their resources, and they lack the discipline to enforce alignment with need over time—a necessity for the kind of sustainable improvements that can ultimately impact the bottom line.

The alignment issue also arises when looking at the urgency of specific HR subtopics. Again, top performers are more strategic in the way they invest their efforts, focusing on the subtopics that they deem to be most urgently in need of action.

For example, consider Pirelli, a leading tire manufacturer, which systematically prioritizes its HR processes to allocate investment according to urgency. As Christian Vasino, the company’s chief human resources officer, explains, “We conduct an annual internal survey to map the perceived sense of priority and satisfaction among 12 HR processes. The outcome of the survey was discussed within HR’s top management as a starting point for developing the people strategy.” Through this assessment, the company is now able to focus on its most urgent areas, which they define as strategic workforce planning, recruiting and on-boarding, training and development, and employee engagement.

NOTE
1. Market performance was measured by the S&P 500 index.
EXHIBIT 7 | Companies with Strong Financial Performance Report Higher Capabilities in Almost All 27 Subtopics

<table>
<thead>
<tr>
<th>Current capabilities</th>
<th>Low</th>
<th>High</th>
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<tbody>
<tr>
<td>HR internationalization</td>
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<tr>
<td>Social media</td>
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<td>Employee engagement</td>
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<tr>
<td>Career models and competencies</td>
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<td>Behavior and culture</td>
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<td>Talent management</td>
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<td>HR and people strategy</td>
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<tr>
<td>Employer branding</td>
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<td>Rewards and recognition</td>
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<tr>
<td>Other HR and workforce analytics</td>
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<tr>
<td>Generation management</td>
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<tr>
<td>HR communication</td>
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<tr>
<td>Recruiting strategy</td>
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<tr>
<td>HR services and systems</td>
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<tr>
<td>Leadership</td>
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<td>Performance management</td>
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<tr>
<td>Strategic workforce planning</td>
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<td>Assignment management</td>
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<td>Recruiting processes</td>
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<td>HR organization and governance</td>
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<td>HR staff capabilities</td>
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<tr>
<td>On-boarding</td>
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<tr>
<td>Diversity management</td>
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<tr>
<td>Training and learning</td>
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<tr>
<td>Labor costs and restructuring</td>
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<tr>
<td>HR processes</td>
<td></td>
<td></td>
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<tr>
<td>Works councils and union management</td>
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<td></td>
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</tbody>
</table>

Note: High performers represent the top 100 companies (with at least 50 employees), which had the highest average revenue change and average operating margin in 2012 and 2013; low performers represent the bottom 100 companies (with at least 50 employees), which had the lowest average revenue change and average operating margin in 2012 and 2013.
EXHIBIT 8 | High Performers Align HR Investments…

... with the most important subtopics

High performers

Low performers

Future importance

Future importance

HR and people strategy

Leadership

Performance management

Recruiting processes

HR organization and governance

Training and learning communication processes

Recruiting strategy and workforce analytics

HR services and systems restructuring governance

Career models and competencies

Employer branding

Social media

Generation management

Assignments management

Diversity management

HR internationalization

Works councils and union management

High

Low

Effort invested

Correlation = 0.92

Correlation = 0.67

75 percent of subtopics fall within each white corridor

High

Low

Future importance

Future importance

HR communication

Training and learning

HR processes

On-boarding

HR services and systems

Strategic workforce planning

HR organization and governance

HR and workforce analytics

Other HR

Talent management

Rewards and recognition

Behavior and culture

Performance management

Consulting strategy

HR staff capabilities

On-boarding

HR services and systems restructuring governance

Social media

Generation management

Other HR and workforce analytics

Assignment management

HR internationalization

Leadership

Employee engagement

Performance management

Assignments management

Correlation = 0.70

Correlation = 0.03

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Note: High performers represent the top 100 companies (with at least 50 employees), which had the highest average revenue change and average operating margin in 2012 and 2013; low performers represent the bottom 100 companies (with at least 50 employees), which had the lowest average revenue change and average operating margin in 2012 and 2013.

1The white corridors indicate the strength of the relationship between a company’s level of investment and the importance of any given subtopic: the narrower the corridor, the stronger the relationship.

2Urgency is determined by calculating the difference between future importance and current capabilities, and then multiplying that difference by future importance.
Another key finding is that HR leaders will have a seat at the table for strategic discussions only if they can demonstrate the business impact of HR. That is, they need to be able to quantitatively establish the areas in which HR supports the organization’s strategic decisions. Our experience has found that data-driven, analytical HR departments are more likely to play a strategic role in their organizations, and the survey data supports this. (See Exhibit 9.)

HR functions that use people-related KPIs and steering tools (such as simulations and forecasts) to measure areas such as workforce productivity and personnel costs, and then analyze and communicate the results throughout the organization, have a greater strategic role in the organization.

Yet our survey data also shows that using a data-driven approach is far from universal. Nearly half of the respondents (44 percent) said that if they use KPIs and steering tools, they do so only occasionally to track workforce productivity. An even larger proportion (55 percent) said that, at best, they use them only occasionally for tracking workforce productivity.

### Exhibit 9 | KPIs and Steering Tools Allow HR to Play a More Strategic Role

<table>
<thead>
<tr>
<th>Strategic role of HR</th>
<th>Strong</th>
<th>Weak</th>
</tr>
</thead>
<tbody>
<tr>
<td>≥ 4</td>
<td>≤ 11</td>
<td>19–20</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Use of HR KPIs and steering tools²</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of companies</td>
</tr>
<tr>
<td>≤ 4</td>
</tr>
<tr>
<td>4–11</td>
</tr>
<tr>
<td>19–20</td>
</tr>
<tr>
<td>≥ 20</td>
</tr>
</tbody>
</table>


¹The strategic role was determined by the average score in questions concerning HR’s role in the company; there were 979 respondents to this section.

²KPIs = key performance indicators; use of KPIs and steering tools was measured by the average score of responses to survey questions concerning workforce productivity, full-time equivalents, and personnel costs.
personnel costs—a relatively basic output metric.

An HR organization that does not use metrics and analytical techniques simply cannot play a strategic role in its organization. Without a clear, data-driven understanding of how the organization is leveraging its human capital,

“We are linking various analyses and data to create true insights for a select group of 300 managers, and we regularly discuss the results and define activities and HR support. For example, we have created and back-tested predictors for attrition risks—based on engagement scores, turnover, performance ratings, and other factors—which we frequently discuss with managers in areas that show an above-average risk of losing talent. The goal is to tailor developmental support to mitigate the risks.”

—The managing director and global head of compensation and benefits at a global Swiss bank

HR leaders have little to contribute to big-picture strategic discussions.

Such results reinforce a common stereotype of HR: that the function is better at working with “softer” aspects of human capital, such as training and development, and is less skilled at applying the economic logic required for higher-level areas, such as workforce productivity, planning, and forecasting.

The use of HR KPIs and steering tools is yet another point of differentiation between high performers and low performers. (See Exhibit 10.)

That said, there is still room for improvement among the high performers. While these companies were far more likely to define quantitative targets and have KPIs in place, there was still a noticeable drop-off in the number of companies that take the next step—using those KPIs to formulate new HR initiatives. So, the low performers need to become more data oriented, and both high and low performers need to use that data to take action.

**EXHIBIT 10 | High-Performing Companies Are More Data-Driven**

<table>
<thead>
<tr>
<th>Use of KPIs²</th>
<th>Often</th>
<th>Never</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Quantitative targets defined</strong></td>
<td>High performers</td>
<td>Low performers</td>
</tr>
<tr>
<td><strong>KPIs in place</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Actual use of KPIs to derive HR initiatives</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>HR initiatives tracked in terms of impact on workforce productivity</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Programs in place to identify and place high-performers in key positions</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Programs in place to address low performance</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Quantitative targets defined</strong></td>
<td>High performers</td>
<td>Low performers</td>
</tr>
<tr>
<td><strong>KPIs in place</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Actual use of KPIs to derive HR initiatives</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Benchmarking overall and by job function against industry standards and competitors</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>


Note: High performers represent the top 100 companies (with at least 50 employees), which had the highest average revenue change and average operating margin in 2012 and 2013; low performers represent the bottom 100 companies (with at least 50 employees), which had the lowest average revenue change and average operating margin in 2012 and 2013; there were 979 respondents to this section, of which 28 were high performers and 27 were low performers.

¹KPIs = key performance indicators.

²FTE = full-time equivalent.
Impact. Great HR functions generate a strong impact on organizational performance through a solid, data-driven approach, which includes implementing people-related KPIs. Using tailored metrics and analytical techniques strengthens the role of HR functions and gives them a seat at the table during strategic discussions.

Key performance indicators are crucial in assessing HR impact, yet many companies struggle to ensure that they’re measuring the aspects of performance that truly matter. For example, many companies look primarily at the “input” elements of HR, such as head count or costs, rather than the “output” elements, such as productivity. They neglect to track the effectiveness of their HR spending to ensure that it supports the company’s strategic orientation. (For more on KPIs, see the sidebar “How Lufthansa Consolidated Its KPIs to Measure the Things That Really Matter.”)

HOW LUFTHANSA CONSOLIDATED ITS KPIS TO MEASURE THE THINGS THAT REALLY MATTER

Deutsche Lufthansa AG operates one of the biggest aircraft fleets in the world and employs more than 115,000 people throughout its passenger and air-freight divisions, logistics functions, catering operations, maintenance and repair operations, and IT.

But until recently, the company’s KPIs were not centrally aligned. Because of decentralized governance, each business unit and division had its own definitions and data standards, and only a small percentage of the several hundred KPIs used could be applied across the entire organization.

The HR function realized that it needed to align its KPIs in order to assess its impact across the entire company. Therefore, Lufthansa conducted an audit of all potential KPIs—such as those currently in use by individual divisions, those required to align with the company’s overall people strategy and financial-reporting requirements, and those identified as external best practices. The total tally: 461 possible KPIs.

The process took several steps, but Lufthansa managed to consolidate the list and distill the number of KPIs to the 35 most strategically relevant, grouping them in four main clusters: financial HR indicators, workforce overview, HR and organizational efficiency, and HR core processes. (See the exhibit below.)

Deutsche Lufthansa AG Consolidated Its KPIs, Going from 461 to Just 35

Source: BCG project experience and analysis.
To highlight the biggest priorities for companies in various regions and industries, we looked at all 27 HR subtopics, using our urgency metric to determine those with the greatest need for action.

The Regional View: Leadership and Talent Management Show the Greatest Urgency

Across most countries, the leadership subtopic was ranked by far as the one most urgently in need of action, and talent management was ranked the second most urgent. Beyond those clear-cut results, however, we found considerable differences in the rankings of subtopics across countries. (See Exhibit 11.)

For example, behavior and culture, as well as employee engagement, were all ranked as more urgent in the U.S. than they were in most other regions. In that market, growth is slowly returning and unemployment is easing. As a result, the competition for labor—particularly in skilled positions—is becoming tougher. Increasingly, some companies are finding that they have to manage their employees on a long-term basis.

In other markets of the Americas, such as Brazil, the focus is still primarily on talent management, given the shortage of candidates for many positions. “The challenge that we see is a huge lack of qualified professionals in Brazil, which is restraining Brazil’s growth and, consequently, the growth of Brazilian companies,” says Simone Cristina T. Salsa Nunes, a corporate strategic people development manager at Queiroz Galvão, a Brazilian conglomerate with investments in infrastructure, energy, food, steel, and shipbuilding industries.

Notably, rewards and recognition were ranked as more urgent in Brazil than in most other markets. This is primarily due to the country’s current economic situation, with relatively low productivity growth and increasing salaries. As Brazilian companies lose competitive ground, they must work harder to motivate their existing employees.

The talent management challenge also exists for Asian countries. According to Joseph Batona, a human resources director at Indofood Sukses Makmur, “Indonesia has a talent crisis at the national level—in almost every sector, including government. The shortage of talent is not being addressed in higher education, whereby graduates are not really ready for the professional world. There is also a shortage of vocational training. Companies really have to invest more in developing people, even at the entry level.”

In many European countries, by contrast, demographic challenges, such as those posed by an aging labor pool, are compelling companies to adopt strategic workforce planning, which was ranked as far more urgent in Germany,
EXHIBIT 11 | Differences in the Urgency Ranking of Selected HR Subtopics by Country

<table>
<thead>
<tr>
<th>Subtopic</th>
<th>Americas</th>
<th>Europe</th>
<th>Middle East and Africa</th>
<th>Asia-Pacific</th>
</tr>
</thead>
<tbody>
<tr>
<td>Leadership</td>
<td>1</td>
<td>1</td>
<td>3</td>
<td>1</td>
</tr>
<tr>
<td>HR communication</td>
<td>9</td>
<td>10</td>
<td>2</td>
<td>9</td>
</tr>
<tr>
<td>Performance management</td>
<td>8</td>
<td>9</td>
<td>8</td>
<td>6</td>
</tr>
<tr>
<td>Training and learning</td>
<td>8</td>
<td>9</td>
<td>9</td>
<td>10</td>
</tr>
<tr>
<td>Social media</td>
<td>6</td>
<td>6</td>
<td>10</td>
<td>5</td>
</tr>
<tr>
<td>Rewards and recognition</td>
<td>5</td>
<td>4</td>
<td>4</td>
<td>5</td>
</tr>
<tr>
<td>Other HR and workforce analytics</td>
<td>7</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>HR staff capabilities</td>
<td>5</td>
<td>10</td>
<td>6</td>
<td>8</td>
</tr>
</tbody>
</table>

Source: 2014 BCG and WFPMA proprietary Web survey and analysis. Note: Urgency is determined by calculating the difference between future importance and current capabilities, and then multiplying that difference by future importance; there were 3,507 respondents in this section.

Among others, than the global average. (See the sidebar “The Global Workforce Crisis.”)

These dramatic shortfalls only underscore the importance of subtopics directly related to long-term human capital planning and preparation, such as strategic workforce planning, diversity, and generation management. Yet most organizations in northern Europe—with the notable exception of German companies—are not prioritizing those topics. (See the sidebar “Transnet Has a Clear View of Future Employment Needs.”)

Countries in southern Europe are facing a different set of challenges, namely sluggish growth and high unemployment. In general, the closer a country is to economic crisis, the more companies in that country will need to differentiate among their employees, to ensure that they can keep the most promising workers in the event of staff reductions.

The Industry Comparison: Energy and Financial Institutions Stand Out

An industry breakdown shows similar differences among the relative levels of urgency of specific subtopics. While leadership, talent management, and behavior and culture were ranked as the three most urgent across most industries, we uncovered several key insights. (See Exhibit 12.)

In the energy sector, leadership was rated the most urgent topic. Leaders in the oil industry are facing significant challenges, such as growing demand for environmentally sustainable processes, bad publicity from recent spills and other accidents, and pressure on financial results. Because of these factors, they have to move from traditional (technical) competencies in the sector to more twenty-first-century skills, such as how to manage uncertainty. Also, in the utilities sector, there are significant uncertainties with respect to supply, which means that leaders must navigate among, and negotiate with, multiple stakeholders. Talent management was the second most urgent topic in the energy sector, mainly due to the lack of talent—especially skilled technical workers—needed to meet the strong demand for new oil and gas projects.

Among financial institutions, several differences stand out. These companies are slowly...
THE GLOBAL WORKFORCE CRISIS

In *The Global Workforce Crisis: $10 Trillion at Risk* (BCG report, June 2014), BCG examined long-term labor issues in 25 of the world’s major economies, looking at imbalances in supply and demand over the next 10 to 20 years. As shown in the exhibit below, which summarizes the findings for 15 countries, some countries are likely to experience tremendous labor shortfalls. The workforce in Germany, for example, will likely fall 4 percent short of the country’s needs by 2020 and 23 percent short by 2030. Brazil is expected to experience a shortfall of 7 percent of its workforce needs by 2020 and 33 percent by 2030. In some of these countries—notably Germany—companies are already feeling the pinch, struggling to find qualified people to meet workforce demand.

### Some Countries Will Face Significant Labor Shortages by 2030

<table>
<thead>
<tr>
<th>Region</th>
<th>Country</th>
<th>Labor shortage or surplus in 2020 (%)</th>
<th>Labor shortage or surplus in 2030 (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Europe</td>
<td>France</td>
<td>6</td>
<td>-4</td>
</tr>
<tr>
<td></td>
<td>Germany</td>
<td>8</td>
<td>17</td>
</tr>
<tr>
<td></td>
<td>Italy</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Spain</td>
<td>-5</td>
<td></td>
</tr>
<tr>
<td></td>
<td>UK</td>
<td>17</td>
<td>-23</td>
</tr>
<tr>
<td></td>
<td>Russia</td>
<td></td>
<td>-1</td>
</tr>
<tr>
<td>Americas</td>
<td>Brazil</td>
<td>-7</td>
<td>-33</td>
</tr>
<tr>
<td></td>
<td>Canada</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mexico</td>
<td>-8</td>
<td>-11</td>
</tr>
<tr>
<td></td>
<td>U.S.</td>
<td>10</td>
<td>-4</td>
</tr>
<tr>
<td>Asia-Pacific</td>
<td>China</td>
<td>-6</td>
<td>-26</td>
</tr>
<tr>
<td></td>
<td>India</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Indonesia</td>
<td>7</td>
<td>-3</td>
</tr>
<tr>
<td></td>
<td>Japan</td>
<td>6</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>South Korea</td>
<td>5</td>
<td>0</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Sources: EIU CountryData database; ILO LABORSTA database; United Nations population database; BCG analysis.

Note: A surplus or shortage is determined by subtracting the labor demand for each time period (2020 and 2030) from the labor supply. The labor supply is the forecast of the total population (age 15 and over, divided into five-year age groups) multiplied by the labor-force participation rate (per five-year age group). Labor demand is defined as the number of people required to be employed to produce a desired amount of gross domestic product (GDP) based on a given output per person (labor productivity). The demand scenario is based on the assumption of retaining the average compound annual growth rate (CAGR) of GDP and labor productivity over the past 20 years. Russia’s GDP CAGR is based on the past 10 years, while its labor-productivity CAGR is based on the trend from 1995 through 2012. Mexico’s labor productivity CAGR is from 2001 through 2012.

1 A de facto shortage is defined as a surplus of 5 percent or less.

**TRANSNET HAS A CLEAR VIEW OF FUTURE EMPLOYMENT NEEDS**

Transnet—the largest logistics company in South Africa, with significant operations throughout Africa focusing on rail, port, and pipeline operations—launched its market demand strategy two years ago. Right from the start, Transnet realized that it needed to identify and respond proactively to skills requirements to anchor that strategy. The process was aimed at mitigating human-capital risk requirements and future employment needs so that the company would have adequate human-capital capacity to advance its goals and objectives. To mitigate the risk, Transnet decided to invest in strategic-workforce-planning tools. The goal was to establish a standardized process that could identify workforce risks both in current operations and in future stages of the investment program.

Transnet uses a holistic and flexible methodology for strategic workforce planning, structured along five key steps:

- **Skill Clustering.** The company developed a catalog that groups employees with similar positions and skills. This approach reduced complexity and allows Transnet to rotate employees among job families and groups.

- **Supply Analysis.** By linking the company’s supply analytics to its enterprise-resource-
resuming growth after the financial crisis. Accordingly, rewards and recognition were ranked as more urgent priorities than in other industries. By contrast, behavior and culture were seen as less urgent than in other industries. Given the fact that many financial-services companies promised to change the way they work after the crisis, this subtopic should be a bigger priority in the sector.

EXHIBIT 12 | Differences in the Urgency Rankings of Selected HR Subtopics by Industry

<table>
<thead>
<tr>
<th>Subtopic</th>
<th>Consumer goods</th>
<th>Energy</th>
<th>Financial institutions</th>
<th>Health care</th>
<th>Industrial goods</th>
<th>Insurance</th>
<th>Professional business services</th>
<th>Human resource services</th>
<th>Public sector</th>
<th>Technology, media, and telecommunications</th>
</tr>
</thead>
<tbody>
<tr>
<td>Leadership</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>Talent management</td>
<td>3</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>1</td>
<td>4</td>
<td>5</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>Behavior and culture</td>
<td>4</td>
<td>3</td>
<td>6</td>
<td>4</td>
<td>5</td>
<td>5</td>
<td>2</td>
<td>1</td>
<td>5</td>
<td>1</td>
</tr>
<tr>
<td>HR and people strategy</td>
<td>2</td>
<td>4</td>
<td>4</td>
<td>3</td>
<td>3</td>
<td>8</td>
<td>3</td>
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<td>Employee engagement</td>
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<td>6</td>
<td>7</td>
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<td>6</td>
<td>6</td>
<td>3</td>
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<tr>
<td>Strategic workforce planning</td>
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<td>8</td>
<td>5</td>
<td>6</td>
<td>9</td>
<td>8</td>
<td>6</td>
<td>2</td>
<td>2</td>
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<tr>
<td>Career models and competencies</td>
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<td>5</td>
<td>10</td>
<td>4</td>
<td>4</td>
<td>9</td>
<td>7</td>
<td>1</td>
<td>1</td>
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<tr>
<td>HR communication</td>
<td>9</td>
<td>8</td>
<td>8</td>
<td>10</td>
<td>4</td>
<td>4</td>
<td>7</td>
<td>7</td>
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<td>1</td>
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<tr>
<td>Performance management</td>
<td>8</td>
<td>10</td>
<td>9</td>
<td>9</td>
<td>10</td>
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<tr>
<td>Training and learning</td>
<td>8</td>
<td>9</td>
<td>10</td>
<td>9</td>
<td>10</td>
<td>9</td>
<td>9</td>
<td>9</td>
<td>1</td>
<td>1</td>
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<tr>
<td>Employer branding</td>
<td>8</td>
<td>10</td>
<td>2</td>
<td>5</td>
<td>8</td>
<td>7</td>
<td>7</td>
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<tr>
<td>Social media</td>
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<td>7</td>
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<tr>
<td>Rewards and recognition</td>
<td>9</td>
<td>7</td>
<td>10</td>
<td>10</td>
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<td>10</td>
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<td>Other HR and workforce analytics</td>
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<tr>
<td>HR staff capabilities</td>
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<td>7</td>
<td>7</td>
<td>7</td>
<td>1</td>
<td>1</td>
</tr>
</tbody>
</table>

Note: Urgency is determined by calculating the difference between future importance and current capabilities, and then multiplying that difference by future importance; there were 3,507 respondents in this section.
WHAT SETS GREAT HR FUNCTIONS APART

Based on BCG’s experience, and supported by the survey data, we see that great HR functions are critical differentiators that separate high-performing companies from the rest. Collectively, the three ideas below describe best-in-class HR functions.

• **Connect.** An HR department needs to connect with internal clients to ensure that its HR and people strategies are clearly linked to the overall business strategy. A fundamental component of this is getting the basics right. That is, if HR is to have credibility as a true strategic partner with the business, it must first establish strong processes and develop core capabilities, particularly in the areas of recruiting and communication.

• **Prioritize.** HR also needs to identify the most important and most urgent priorities for its organization and then target investments accordingly. As the survey findings show, talent management, leadership, and employee engagement are the topics that virtually all HR departments will need to focus on. Strong HR departments have precise and trackable leadership-development initiatives in place, along with enterprise-wide training measures and firm control over internal mobility. These departments shape engagement and leadership behaviors to foster a more vibrant and productive corporate culture.

• **Impact.** Robust HR departments generate and report people-based KPIs, which provide the data for formulating strategic actions and ultimately impact the business. This is particularly true for strategic workforce planning, which is increasingly important for most companies. People analytics—defined as the increased use of data to generate insights on people management processes—is now taking off in terms of use and importance. Just as other functions of a company increasingly rely on sophisticated algorithms in areas such as pricing and supply-chain management, HR analytics are becoming an indispensable tool to help HR functions impact the business.
After the first Creating People Advantage report in 2007, we have occasionally removed or added topics and subtopics for analysis depending on the trends and shifting priorities in HR and people management. In this year’s version, we looked at 10 broad topic areas, broken out into 27 subtopics. (See the exhibit below.)

The online survey was conducted from March through July of 2014. Using a six-point scale, respondents rated each subtopic on future importance, their companies’ current capabilities with regard to that subtopic, and the levels of effort invested in the subtopic in terms of time, money, and full-time employees over the past three years. We also calculated a
fourth metric—the urgency of individual sub-topics—as follows: future importance minus current capabilities, multiplied by future importance.

A total of 3,507 respondents from 101 countries replied to the survey. The bulk of the respondents (83 percent) were from HR functions, including HR generalists, HR business partners, members of a center of excellence (such as recruiting, talent, or diversity), and members of a shared-services center (such as payroll or IT). The remaining respondents were from non-HR functions.

The biggest industries represented in the survey were professional business services (18 percent of respondents), industrial goods (17 percent), the public sector (16 percent), consumer goods (15 percent), and technology, media, and telecommunications (12 percent). The remaining industries represented were health care (7 percent), financial institutions (6 percent), energy (5 percent), and insurance (4 percent).

We identified high and low performers through self-reports of financial performance overall, using operating margins over the prior two years (2012 and 2013) as the primary criterion. For companies that had similar operating margins, we used revenue change over the same time period as a secondary criterion. Also, we excluded from these analyses any companies that had fewer than 50 employees.
We thank the following executives for their valuable contributions in discussing the findings of this report. (This list includes only those who have agreed to make their names public.)

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Lhoist

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*Executive Vice President for Organizational Development*  
Cielo

Paulo Miri  
*Vice President for HR, Procurement, Business Excellence and Communications*  
Whirlpool Latin America

Flávio Morelli  
*HR Director*  
TIM Brasil

Simone Cristina T. Salsa Nunes  
*Corporate Strategic People Development Manager*  
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Sanoma

**France**
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Isabelle Gouyet  
*Director Human Resources*  
Crédit Immobilier de France

Daniel Lacabane  
*Vice President Executive & Talent Development*  
Renault–Nissan Alliance

Jérôme Nanty  
*Secretary General*  
Transdev

Philippe Rouxel  
*HR Director Western Europe*  
DBApparel

Marie-Christine Théron  
*Executive Director Human Resources and General Affairs*  
SFR

Hans Vanbets  
*Head of HR Strategy, People Management Policies & Diversity*  
BNP Paribas
Germany
Milagros Caiña-Andree
Member of the Board of Management of BMW, Human Resources and Labour Relations
BMW

Immanuel Hermreck
Executive Vice President Human Resources
Bertelsmann

Michael König
Member of the Board of Management of Bayer, Labor Director, Human Resources, Technology and Sustainability
Bayer

Kathrin Menges
Executive Vice President Human Resources and Infrastructure Services
Henkel

Margret Suckale
Member of the Board of Executive Directors of BASF, Industrial Relations Director
BASF

Uwe Tigges
Chief Human Resources Officer and Member of the Management Board
RWE

Thomas Wessel
Member of the Management Board, Chief Human Resources Officer
Evonik Industries

Greece
Athina Dessypri
General Manager, Human Resources
Eurobank

Vassilis Gavroglou
Head of Human Resources Strategy
National Bank of Greece

John Kollas
Group HR Executive Director
Titan Cement

Tina Moutzouri
Human Resources Manager
Thenamaris

Christine Roth
Chief Strategy Officer
Thenamaris

Indonesia
Joseph Bataona
Human Resources Director
Indofood Sukses Makmur

Aloysius Budi Santoso
Chief of Corporate Human Capital Development
Astra International

Italy
Luciano Carbone
Chief Corporate Officer
SEA

Andrea Faragalli
Director of Strategies and Resources
Intesa Sanpaolo – Corporate and Investment Banking Division

Salvatore Poloni
Head of Human Resources and Organisation
Intesa Sanpaolo

Monica Possa
Group HR Director
Generali

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Pirelli

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Personnel Managers Club (PM Club), Belgium

Asociación Boliviana de Gestión Humana (ASOBGHI), Bolivia

Institute of Human Resource Management (iHRM), Botswana

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Bulgarian Human Resources and Development Association (BHRMDA), Bulgaria

Canadian Council of Human Resources Associations (CCHRA), Canada

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Cyprus Human Resource Management Association (CyHRMA), Cyprus

The Association of Human Resource Managers in Denmark (PID), Denmark

Asociación Dominicana de Administradores de Gestión Humana (ADOARH), Dominican Republic

Asociación de Directores de Personal del Ecuador (ADPE), Ecuador

Estonian Association for Personnel Management (PARE), Estonia

Finnish Association for Human Resource Management (HENRY), Finland
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