



WHERE DOES HUMAN RESOURCES SIT AT THE STRATEGY TABLE?

BY COURTNEY HAMILTON, DAVID F. LARCKER, STEPHEN A. MILES, AND BRIAN TAYAN
FEBRUARY 15, 2019

INTRODUCTION

Two decades ago McKinsey advanced the idea that large U.S. companies are engaged in “war for talent” and that to remain competitive they need to make a strategic effort to attract, retain, and develop the highest-performing executives.¹ Since that time, some companies have pursued this objective by elevating the importance of the human resources department and broadening its responsibilities beyond workforce administration to include strategic talent and organizational issues.²

Studies have examined whether human resource (HR) departments have succeeded in this transition. For the most part, the results are negative, suggesting that significant gaps remain between the potential and actual contribution of HR to corporate outcomes. For example, research by The Conference Board and McKinsey finds that “business unit leaders view HR as lagging in strategic performance relative to transactional duties,” such as payroll, benefits, and recordkeeping.³ A 2016 study by Development Dimensions International finds that human resources leaders score below their peers on a variety of dimensions, including business savvy, financial acumen, and global acumen.⁴ KPMG finds that only a third (35 percent) of executives believe that HR excels in contributing to the company’s people strategy; only 17 percent believe HR demonstrates the value it provides to the business; and only 15 percent see HR as able to provide insightful and predictive workforce analytics.⁵ A piece in *Harvard Business Review* claims that “CEOs worldwide ... rank HR as only the eighth or ninth most important function in a company.”⁶

This assessment is reflected in compensation figures. According to Equilar, chief human resource officers are paid significantly below their peers in the C-suite, earning on average a third less in total compensation than chief marketing officers and general counsel, and half the amounts paid to chief financial officers.⁷

The problem, if it exists, might originate at the top of organizations. A 2013 survey by The Miles Group and the

Rock Center for Corporate Governance at Stanford University finds that talent development and workplace issues play a very insignificant part in the performance evaluation and bonus calculations for CEOs, suggesting that boards do not place the same weight on human capital as they do on other strategic and financial objectives.⁸

STRATEGIC HUMAN RESOURCES

To understand the contribution of the human resources department to company strategy, we surveyed 85 CEOs and chief human resources officers (CHRO) at Fortune 1000 companies.⁹ Unlike prior research, we find significant positive assessments of the role that human resources departments and CHROs play in strategic planning, workforce development, and company culture. Of note, we find no discernable difference in the perception that CEOs and CHROs have in the value of HR to the organization’s success, which are equally positive.

Ninety-six percent of respondents strongly agree or agree that the human resources department is vitally important to the strategic success of their company (see Exhibit 1). Respondents believe that HR plays a lead role in actively managing company culture and values (4.6 on a scale of 1 to 5, with 5 indicating “to a great extent” and 1 indicating “not at all”). They give a similar assessment (4.6) of the extent to which HR is highly attuned to employee sentiment, including workplace satisfaction and negative chatter. To a lesser degree, they believe that HR directly contributes to the financial performance of the company (4.0).

CEOs and CHROs share a positive assessment of the important role that the chief human resources officer plays in the senior management and strategic planning of the organization. Ninety-four percent of respondents say that the CHRO meets very frequently or frequently one-on-one or in small groups with the CEO. Ninety-one percent of respondents say that the CHRO very frequently or frequently discusses strategic, long-range personnel issues with the CEO. CEOs and CHROs widely believe that the CEO relies on the CHRO as a confidant or sounding board to

discuss strategic, cultural, or organizational issues (4.4 on a scale of 1 to 5).

One issue where we found significant disagreement between the CEO and CHRO is over the role that the human resources department plays in senior-level discussions about company culture: 71 percent of CHROs claim that they lead the discussion on culture, whereas only 36 percent of CEOs believe that the CHRO leads the discussion. Instead, CEOs say that the chief human resources officer contributes to the discussion but does not lead it.

Respondents state that the chief human resources officer plays an important role in communicating management's human capital issues to the board of directors. Eighty-seven percent say that the CHRO presents succession planning issues to the board, 80 percent say the CHRO presents on the company's talent development efforts, and 78 percent say this executive presents on the company's compensation and benefits programs. Other human capital issues presented to the board include talent recruitment (60 percent), workplace programs (54 percent), internal workplace issues (35 percent), and workplace policies (29 percent). That said, the CHRO rarely participates in a company's analyst or investor day conferences: only 3 percent of companies with an analyst or investor day invite the CHRO to present.

Sixty percent of companies in our sample have a formal talent-development program for senior executives. Among those, the CHRO plays a prominent role in the program, with 84 percent of respondents saying that the CHRO leads this program, 9 percent saying that the CHRO participates in but does not lead the program, and 7 percent saying that the CHRO plays no role in the management of the program.

CEOs and CHROs report a variety of challenges around talent development and recruitment at their companies. The most prominent of these are an insufficient leadership pipeline (24 percent), difficulty in finding talent (20 percent), and too much competition for talent (17 percent). Difficulty in developing talent (11 percent), lack of leadership attention to talent issues (10 percent), lack of resources for development and recruitment (6 percent), and difficulty in retaining talent (2 percent) are also referenced.

CEOs and CHROs are confident in the contribution that the human resources department makes to the strategic success of their companies; however, there is some indication of room for improvement. Only 18 percent rate their company a 5 on a scale of 1 to 5 when asked to what extent their HR department does an outstanding job contributing to the strategic success of the organization. Sixty percent rate the company a 4, and a sizeable

minority assign their companies ratings of 3 (15 percent) and 2 (5 percent). These numbers suggest that while respondents might be highly favorable of the contribution that the CHRO makes to the organization and its strategic management, the contribution that this individual makes might not cascade down through the HR department as a whole.

Overall, these survey results are surprising in their optimism, particularly in contrast to the studies cited in the introduction. While those studies rely on the opinions of a broad set of senior executives, the survey results here exclusively reflect those of the CEO and CHRO, suggesting a potentially wide disconnect between the viewpoints of those expected to lead human capital management efforts and the rest of the company.

This raises the question of how (and whether) the leaders of a company—CEO, the senior management team, and the board of directors—validate the quality and effectiveness of its human capital strategy.

In a general sense, approving HR strategy is analogous to approving corporate strategy, including the establishment of overall objectives for the organization, identifying the steps necessary to achieving those objectives, establishing targets and metrics to track progress, and developing the supporting budget. The CEO and CHRO cannot drive HR strategy alone; each leader throughout the organization must be aligned and accountable for prioritizing and delivering against the HR strategy (as they would corporate strategy). To further reinforce the concept that human capital is central to the success of corporate strategy, specific targets should be included in compensation contracts and bonus targets.

Furthermore, the board of directors plays an important role in assessing the acceptability of the human capital strategy. This includes not only advising senior management in HR strategy development but also challenging the CEO and CHRO to defend situations where their assessment differs from those of division heads and the broad base of employees. To facilitate the discussion, the board should request that management develop reliable metrics and demonstrate the success or potential areas to improve its efforts through data pulled from human resource management systems (HRMS).

For HR strategy to succeed, it needs to be treated more like corporate strategy, as opposed to an addendum to the board book.

WHY THIS MATTERS

1. Two decades after McKinsey coined the term “war for talent,” there is relatively little evidence that companies have made tangible progress developing and implementing strategies

- to compete for human talent. Broadly speaking, have HR departments grown beyond their historical role of workplace administrators and compliance specialists to contribute in the vital area of human capital development?
2. The survey data summarized in this Closer Look indicates that both CEOs and CHROs are highly positive of the contribution that the human resources department makes to the strategic success of the company. However, a variety of observers claim just the opposite. What role does HR actually play in the development of corporate strategy? Do they have an equal voice in this process, or are they junior members of the senior management team? How directly important is HR to the financial performance of the company?
 3. If human resources is vitally important to the strategic success of an organization, it should be a key area of interest not only for management but also for the board of directors. Do boards see human resources and human capital as critical to corporate performance? If so, what questions do they ask to ascertain whether management has the right human capital strategy? How does the process for developing an HR strategy differ from that of developing a corporate strategy?
 4. Companies are increasingly sophisticated in capturing information on human capital. How adept are they at using this data? What data do they review to monitor company progress? Do they ask the management team to mine data from the company's internal systems to gain insight into what programs and strategies work effectively and why? Are predictive analytic approaches used by top companies to explore these questions?
 5. What type of human capital information should the company disclose to shareholders and stakeholders? Many voluntary reports now consist of standard items like voluntary and involuntary turnover rates, hours of training, expenditures on human resource programs, and pay differential across employee gender. How informative are these data about the quality of the human resources effort? ■

¹ Elizabeth G. Chambers, Mark Foulon, Helen Handfield-Jones, Steven M. Hankin, and Edward G. Michaels III, "The War for Talent," *The McKinsey Quarterly* (1998).

² Prominent institutional investors, such as BlackRock, are also becoming more vocal in prompting their portfolio companies to pay more attention to workforce needs. See BlackRock, "Larry Fink's 2019 Letter to CEOs: Profit and Purpose," available at: <https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter>.

³ The Conference Board and McKinsey & Company, "The State of Human Capital 2012: False Summit," (2012).

⁴ Development Dimensions International (DDI), "High Resolution Leadership: A Synthesis of 15,000 Assessments into How Leaders Shape

the Business Landscape," (2016). See also: Ernst & Young, "The Call for a More Strategic HR: How Its Leaders Are Stepping up to the Plate," *Harvard Business Review* (April 24, 2016).

⁵ HR received the highest marks among these executives for its ability to "manage costs." See KPMG, "Rethinking Human Resources in a Changing World," (2016).

⁶ The viewpoint that human resource officers might not hold the same standing within organizations as other senior executives is suggested in a recent *Wall Street Journal* article about Goldman Sachs, which explains that in order to reduce the size of the company's management committee, "executives from nonrevenue divisions such as human resources and legal might be shifted to a broader, less-powerful operating committee." See Liz Hoffman, "Goldman Sets a New Path—David M. Solomon, Tapped as Next CEO, Will Push for Fresh Sources of Growth," *The Wall Street Journal* (July 18, 2018). See also Ram, Charan, Dominic Barton, and Dennis Carey, "People Before Strategy: A New Role for the CHRO," *Harvard Business Review* (July-August 2015).

⁷ See Equilar, "View from the Top: Executive Pay Beyond the CEO and CFO," C-Suite (Winter 2018); Equilar, "CFO Pay Has Remained Stagnant Since 2013," (October 9, 2018); and Equilar, "Human Resources Executive Pay Trends," (November 13, 2018).

⁸ Stanford Graduate School of Business, the Rock Center for Corporate Governance, The Miles Group, "2013 CEO Performance Evaluation Survey," (2013).

⁹ Proprietary survey of 85 chief executive officers and chief human resource officers at Fortune 1000 companies, conducted by The Miles Group and Rock Center for Corporate Governance at Stanford University in summer and fall of 2018. Breakdown of respondents: 33 CEOs, 48 CHROs, and 4 undisclosed. For convenience, we refer to the most senior human resource executive at a company as its chief human resource officer, even if this executive has a different title (such as VP, SVP, EVP, or chief people person) or more than one title.

Courtney Hamilton is Managing Director, The Miles Group. David Larcker is Director of the Corporate Governance Research Initiative at the Stanford Graduate School of Business and senior faculty member at the Rock Center for Corporate Governance at Stanford University. Stephen Miles is Chief Executive Officer, The Miles Group. Brian Tayan is a researcher with Stanford's Corporate Governance Research Initiative. Larcker and Tayan are coauthors of the books Corporate Governance Matters and A Real Look at Real World Corporate Governance. The authors would like to thank Michelle E. Gutman for research assistance with these materials.

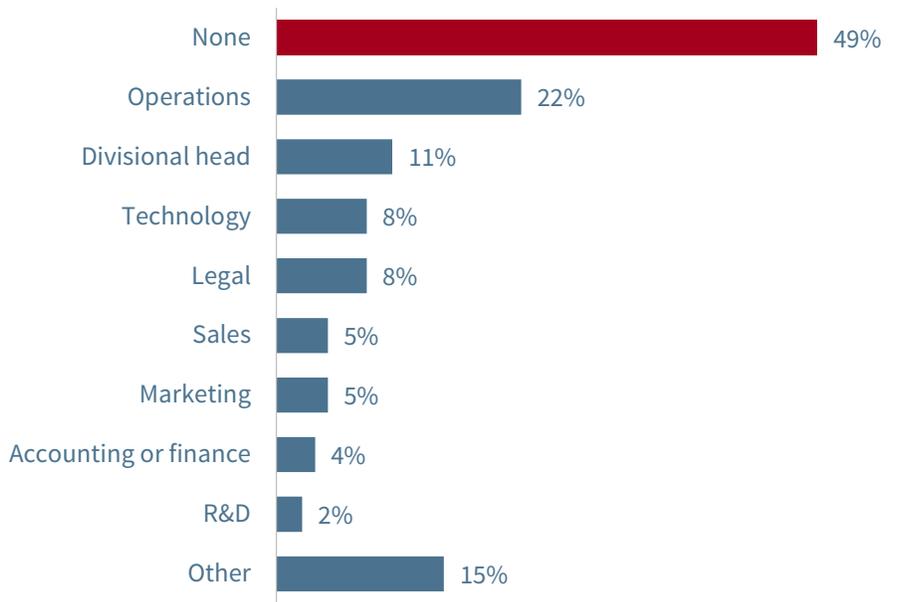
The Stanford Closer Look Series is dedicated to the memory of our colleague Nicholas Donatiello.

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EXHIBIT 1 — SURVEY DATA ON STRATEGIC LEVEL OF HUMAN RESOURCES

WHAT PRIOR EXECUTIVE-LEVEL EXPERIENCE, IF ANY, DOES THE CHIEF HUMAN RESOURCES OFFICER HAVE WORKING IN A FUNCTION OUTSIDE OF HUMAN RESOURCES? (SELECT ALL THAT APPLY)



TO WHAT EXTENT DO YOU AGREE THAT THE HUMAN RESOURCES DEPARTMENT IS VITALLY IMPORTANT TO THE STRATEGIC SUCCESS OF YOUR COMPANY?

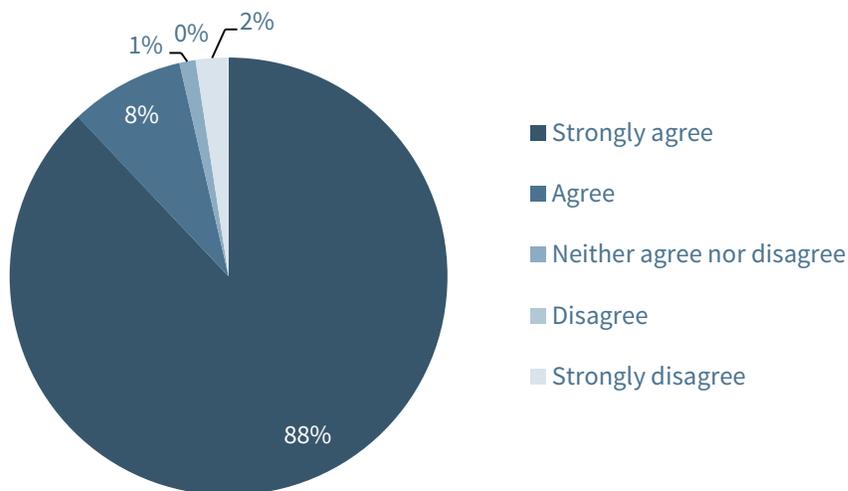
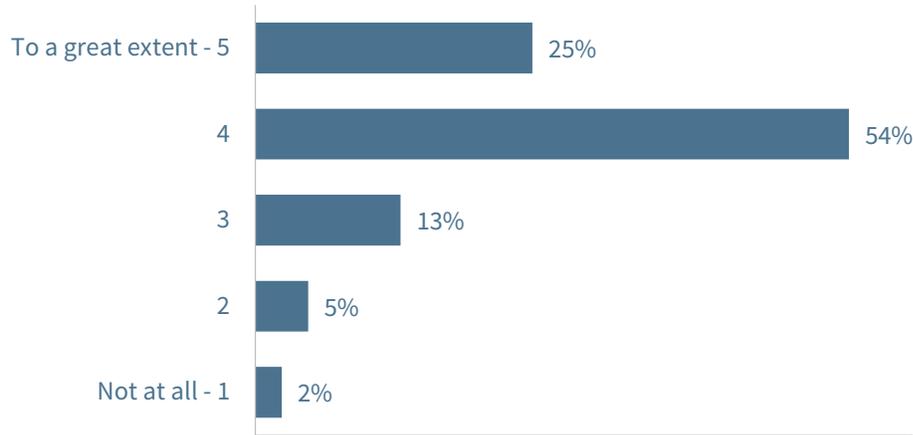


EXHIBIT 1 — CONTINUED

TO WHAT EXTENT DOES THE HUMAN RESOURCES DEPARTMENT DIRECTLY CONTRIBUTE TO THE FINANCIAL PERFORMANCE OF YOUR COMPANY?



TO WHAT EXTENT DOES THE HUMAN RESOURCES DEPARTMENT PLAY A LEAD ROLE IN ACTIVELY MANAGING THE COMPANY'S CULTURE AND VALUES?

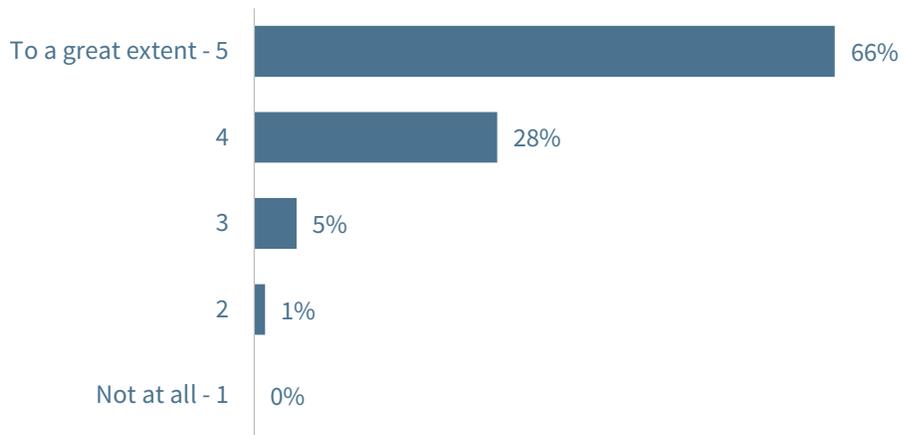
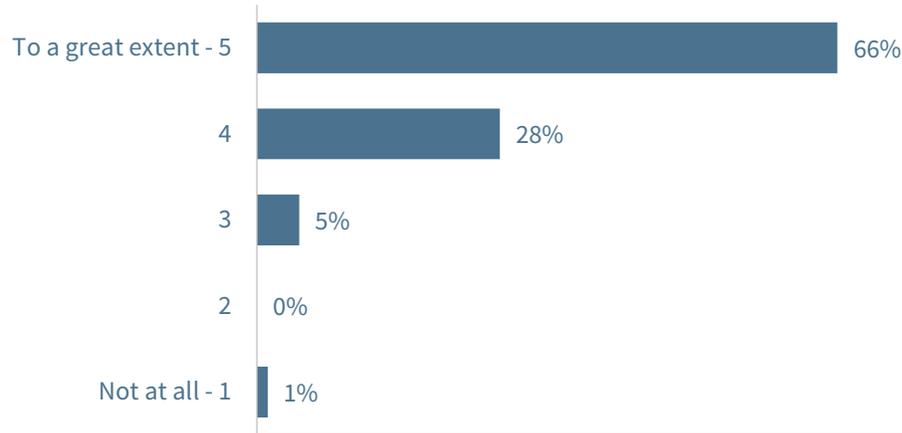


EXHIBIT 1 — CONTINUED

TO WHAT EXTENT IS THE HUMAN RESOURCES DEPARTMENT HIGHLY ATTUNED TO EMPLOYEE SENTIMENT, INCLUDING WORKPLACE SATISFACTION AND NEGATIVE CHATTER?



HOW FREQUENTLY DOES THE CHIEF HUMAN RESOURCES OFFICER MEET ONE-ON-ONE OR IN SMALL GROUPS WITH THE CEO OF YOUR COMPANY?

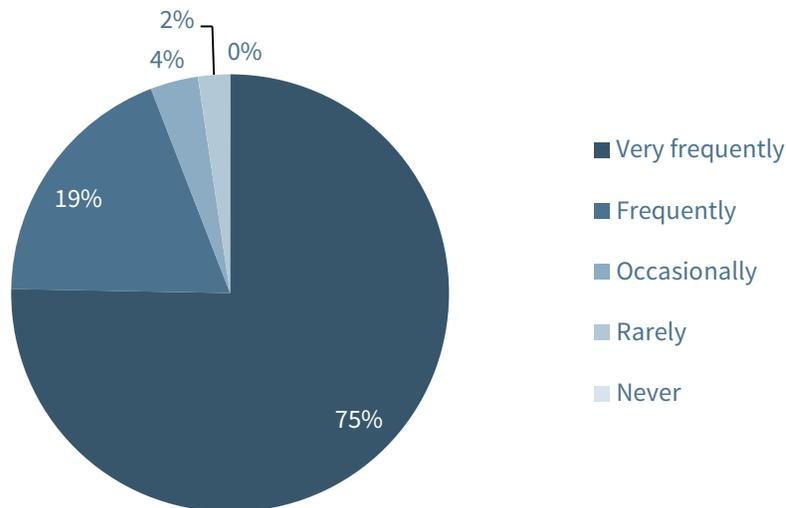
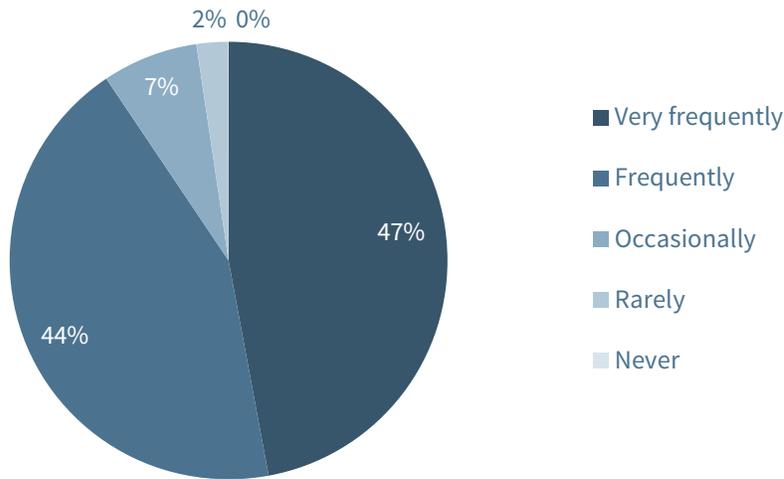


EXHIBIT 1 — CONTINUED

HOW FREQUENTLY DOES THE CHIEF HUMAN RESOURCES OFFICER DISCUSS STRATEGIC, LONG-RANGE PERSONNEL ISSUES WITH THE CEO?



TO WHAT EXTENT DOES THE CEO RELY ON THE HUMAN RESOURCES OFFICER AS A CONFIDANT OR SOUNDING BOARD TO DISCUSS STRATEGIC, CULTURAL, OR ORGANIZATIONAL ISSUES?

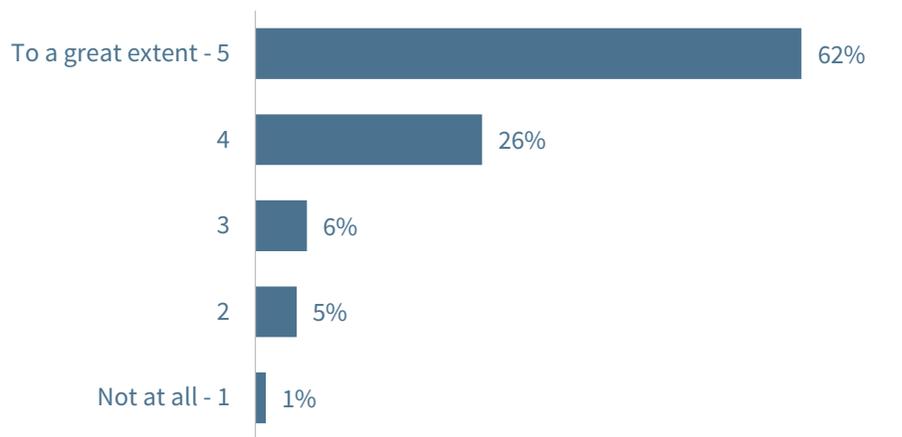
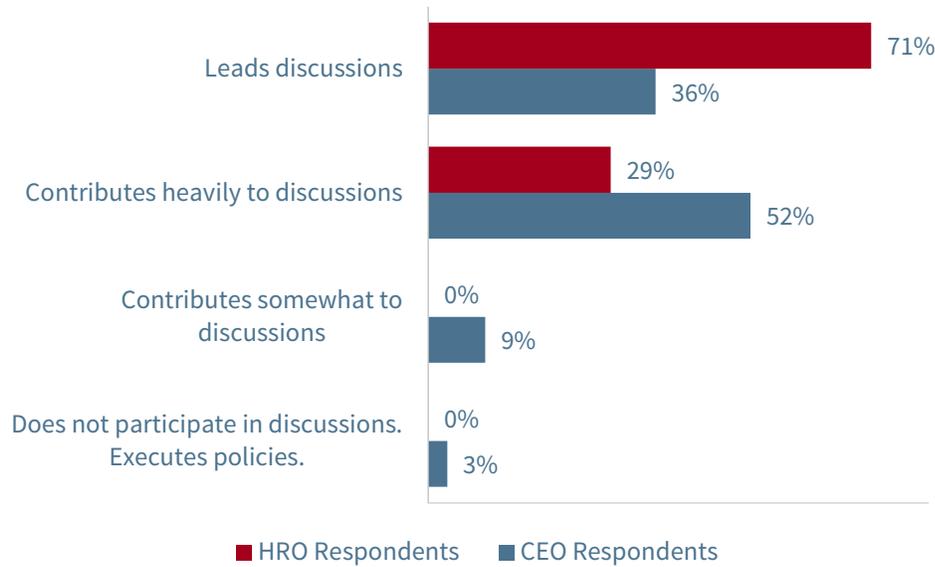


EXHIBIT 1 — CONTINUED

WHAT ROLE DOES THE CHIEF HUMAN RESOURCES OFFICER PLAY IN SENIOR-LEVEL DISCUSSIONS ABOUT COMPANY CULTURE?



WHAT INFORMATION DOES THE CHIEF HUMAN RESOURCES OFFICER PRESENT TO THE BOARD OF DIRECTORS?
(SELECT ALL THAT APPLY)

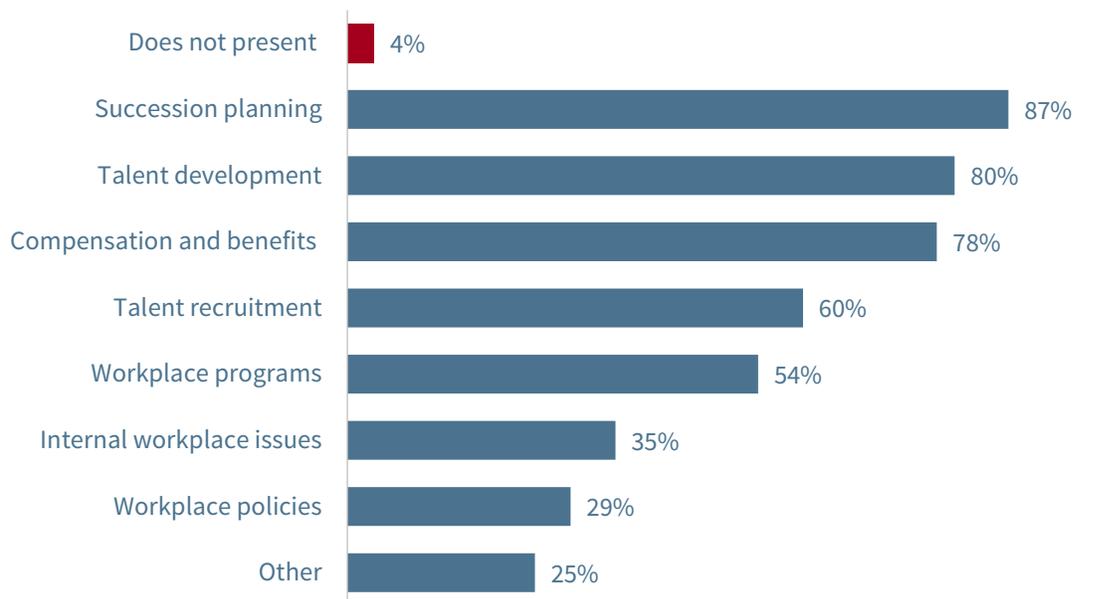
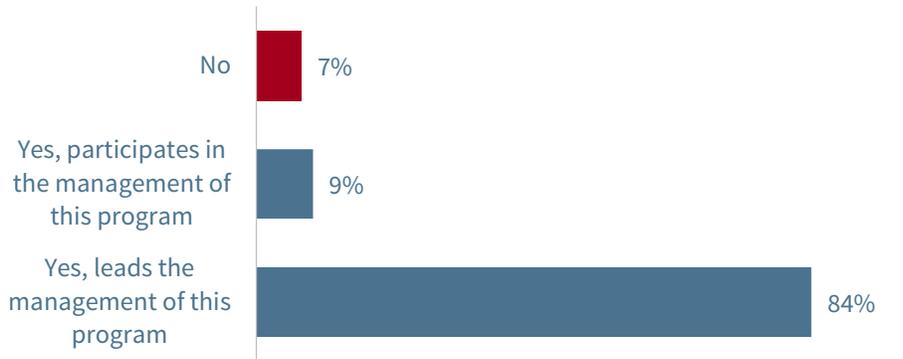


EXHIBIT 1 — CONTINUED

DOES YOUR COMPANY HAVE A FORMAL TALENT DEVELOPMENT PROGRAM FOR SENIOR-LEVEL EXECUTIVES?
 [IF YES] DOES THE CHIEF HUMAN RESOURCES OFFICER MANAGE THIS PROGRAM?



WHAT IS THE SINGLE GREATEST CHALLENGE AROUND TALENT RECRUITMENT AND DEVELOPMENT THAT YOUR COMPANY FACES?

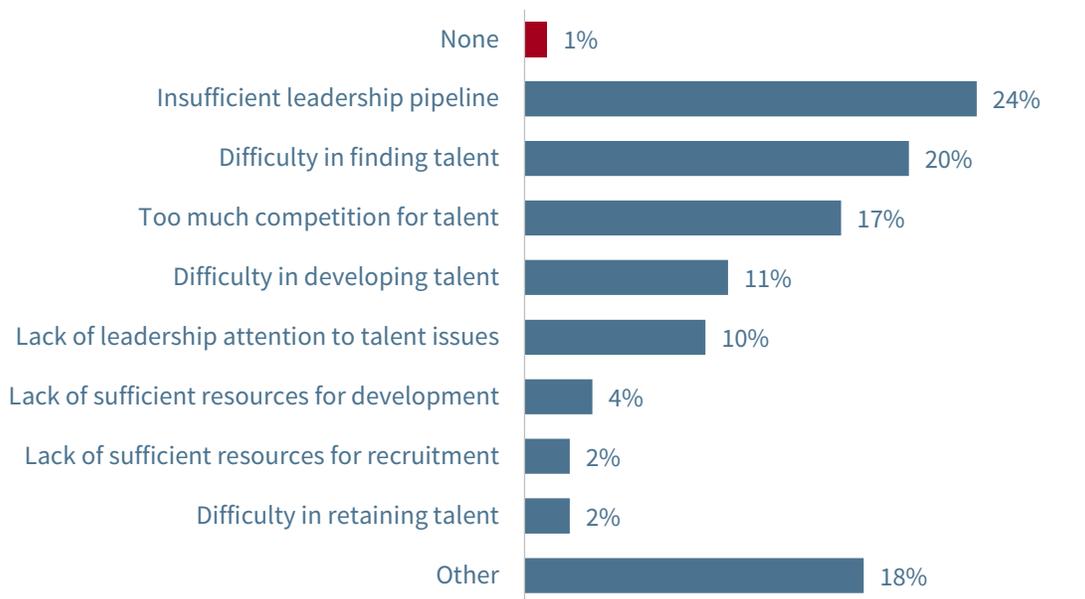


EXHIBIT 1 — CONTINUED

WHAT HIGH-LEVEL FUNCTIONAL SKILLS ARE MOST IMPORTANT TO YOUR ORGANIZATION'S STRATEGIC SUCCESS OVER THE NEXT FIVE YEARS? (SELECT ALL THAT APPLY)

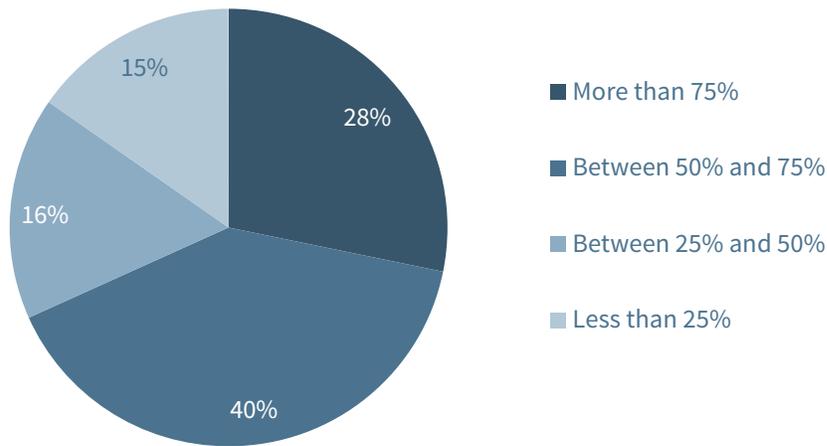


WHAT HIGH-LEVEL LEADERSHIP SKILLS ARE MOST IMPORTANT TO YOUR ORGANIZATION'S STRATEGIC SUCCESS OVER THE NEXT FIVE YEARS? (SELECT ALL THAT APPLY)

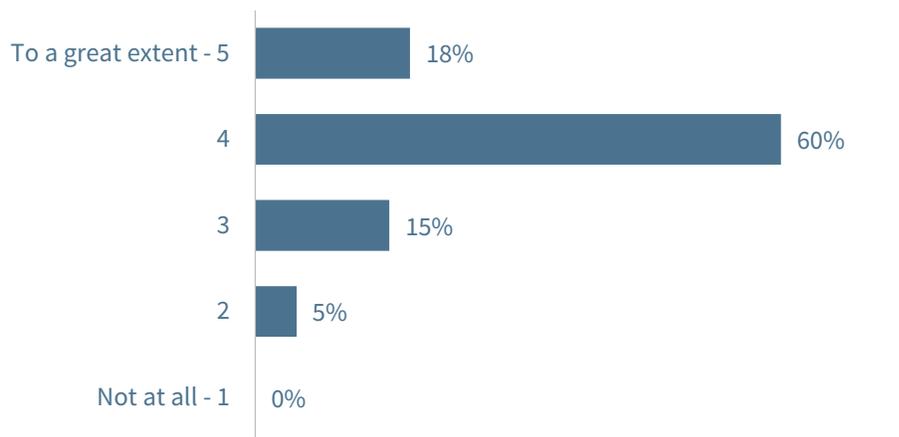


EXHIBIT 1 — CONTINUED

WHAT PERCENT OF YOUR SENIOR MANAGEMENT TEAM WAS PROMOTED TO THEIR CURRENT POSITIONS FROM WITHIN THE COMPANY (AS OPPOSED TO RECRUITED FROM OUTSIDE YOUR COMPANY)?



TO WHAT EXTENT DO YOU BELIEVE THAT THE HUMAN RESOURCES DEPARTMENT DOES AN OUTSTANDING JOB SUPPORTING THE STRATEGIC GOALS OF YOUR COMPANY?



Source: Proprietary survey of 85 chief executive officers and chief human resource officers at Fortune 1000 companies, conducted by The Miles Group and Rock Center for Corporate Governance at Stanford University in summer and fall of 2018.