

The critical relationship between the CEO and human resources

How to help executives
make well-informed
decisions about the
workforce

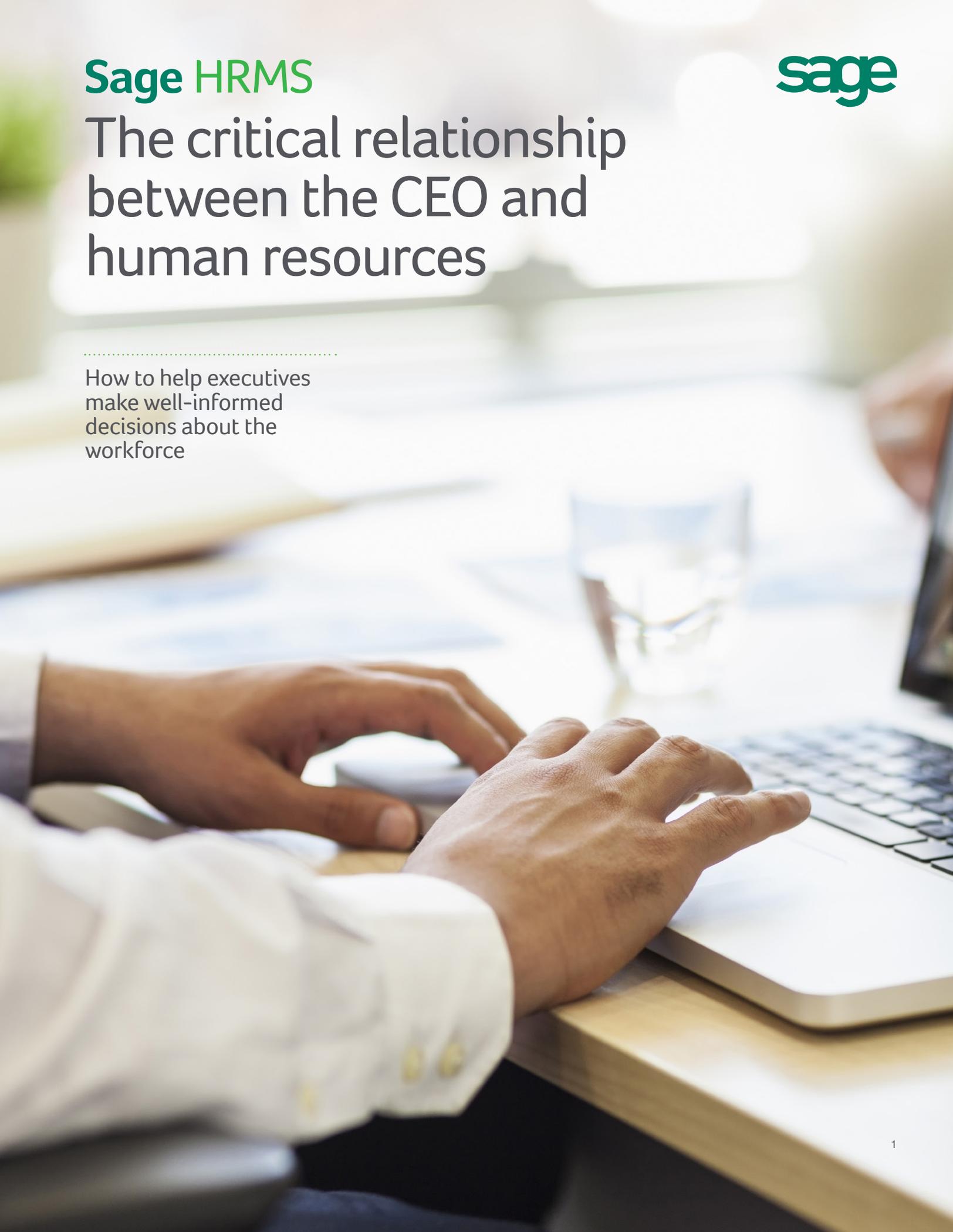


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Top business challenges for today's CEO

After years of economic downturn, North American CEOs are finding reasons to be more confident in many areas. Domestically, their economies continue to improve, and CEOs are reassessing international opportunities after years of trying conditions. However, in spite of this growing optimism, the global economic recovery continues to be fragile, and uncertainty is still a predominant theme, making it a continuing challenge to manage costs.

What the C-suite worries about

Top threats to business growth cited by chief executive officers (CEOs)¹

- 92% government response to fiscal deficit and debt burden
- 83% continued slow or negative growth
- 81% increasing tax burden
- 81% overregulation
- 70% availability of key skills
- 57% inability to protect intellectual property
- 57% speed of technological change
- 52% rising labor costs in high-growth markets
- 48% high and volatile raw materials prices
- 41% high or volatile energy costs

Top concerns of chief financial officers (CFOs)²

- Healthcare
- Finance and accounting talent war
- Cybersecurity risks
- Technology
- Uncertainty in regulation
- Uncertainty in economic recovery

In many ways, the economic troubles of the Great Recession have served to shine a spotlight on workforce management issues for many executives, and many leaders found that their organizations were not as nimble or flexible as they would like.

The global economic recovery continues to be fragile, and uncertainty is still a predominant theme, making it a continuing challenge to manage costs.

1 PriceWaterhouseCoopers, (2014). Good to grow: 2014 US CEO Survey.

2 Nance-Nash, S. (2014, January 30). CFOs' Top Concerns 2014. Retrieved from: www.proformative.com/articles/cfos-top-concerns-2014

The changing landscape

For today’s CEOs, new technologies and a workforce that is evolving as Millennials come of age are rapidly changing the business landscape. New business models that companies are beginning to implement in order to adapt require new talent with new skill sets. CEOs are focused on making sure the proper talent is in place, and 62% were planning on increasing headcount in 2014; however, 70% of CEOs polled¹ were also concerned about the availability of key skills. This highlights the fact that it’s a never-ending battle to attract and retain the right people, and key employee retention is becoming a major challenge for organizations.³ Increased voluntary turnover is resulting in pressure to hire quickly, resulting in a recent drop in hiring quality.

To combat high-performer turnover, poor hiring quality, and rising work costs, companies are looking for a greater return on their workforce investment by acquiring HR tools to help with:

- Talent management.
- Leadership.
- Workforce planning.
- Advanced workforce analytics.

The HR capability gap

As an HR leader, your department plays a critical role in maintaining your organization’s effectiveness—while also containing rising costs. That is why you have to stay abreast of its performance and identify possible capability gaps. Current research involving 2,500 CEOs shows that the capability gap is an area of concern for many companies. While HR spending is rising for many companies,⁴ companies report generally low levels of readiness to respond to HR trends. On average, 36 percent of respondents said they were “not ready.”⁵

HR capability gaps ranked according to importance⁵

Highly urgent	Urgent	Very important	Important
Leadership	Reskilling HR	Performance management	Workforce capability
Talent and HR analytics	Talent acquisition and access	Retention and engagement	Diversity and inclusion
	Overwhelmed employee	Global HR and talent	Learning and development
	HR technology		

While HR teams may understand their current programs, capabilities, and readiness in these areas, survey results also indicate many business leaders may not. It is important for HR leaders and teams to engage with top management to ensure capability gaps are identified and addressed.

3 PriceWaterhouseCoopers. (2014) State of the Workforce. Results from PwC Saratoga’s 2013/2014 US Human Capital Effectiveness Report.

4 Short, E. (2014, May 9) HR Spending on the Rise. Retrieved from: <http://www.talentmgt.com/articles/hr-spending-on-the-rise>

5 Deloitte University Press (2014) Global Human Capital Trends 2014: Engaging the 21st-Century Workforce

Current HR trends⁵

Trends rated as urgent or important by companies with high-performing HR and talent teams.

Leadership:	88%
Talent acquisition and access:	85%
Reskilling HR:	84%
Retention and engagement:	83%
Talent and HR analytics:	82%

To deliver strategic value, keep an eye on the bottom line

How HR manages the workforce has a direct impact on achieving profitability objectives. One of the best ways to set your HR strategy is to align workforce management goals with corporate objectives. Keeping an eye on how your programs and decisions will impact the bottom line can dramatically improve financial performance.

Has HR joined the executive team?

In a recent survey conducted by The Economist, only 55% of CEOs polled believe that the head of HR is a key player in strategic planning, but over 70% of CEOs want the head of HR to be a key player. However, a significant number of respondents believed HR heads are preoccupied with the HR agenda, focusing too much on processes and rules, while 37% believed they didn't understand the business well enough.⁶

To add strategic value, HR leaders should step outside the human resources arena and truly understand the business. What does your company do? How much does it cost to deliver products? How does the competition do it? Who are your customers?

For HR to take on a bigger role in driving growth, you need to develop a workforce that supports the company's goals and customers and help the executive team stay ahead of HR issues by finding answers before they ask questions. Are HR departments fulfilling this mission today? According to HR professionals, the answer is still no.

One of the best ways to set your HR strategy is to align workforce management goals with corporate objectives.

⁶ The Economist Intelligence Unit (2012) CEO Perspectives: How HR can take on a bigger role in driving growth.

The importance of metrics

The role of HR has transitioned from caretaker to strategic partner, and an important function for the department is to relay pertinent data to the CEO that can affect strategic thinking and planning and to do so in a timely fashion. To that end, an HRMS dashboard is now an indispensable tool. Think of the dashboard as an easy-to-access scorecard. It gives personnel important metrics that they need in an easy-to-view format that they can then share with the CEO (among others) who can then take action on it.

With that said, let's take a look at some of the metrics that a CEO will be most interested in and HR can provide.

Key metric: Labor cost revenue percent

This metric describes labor costs in terms of the amount expended for each dollar of revenue the business generates. It is basically the return on investment for your labor force. Divide total annual labor costs by revenue and express it as a percentage:

$$\text{Labor cost Revenue percent} = \frac{(\text{Compensation} + \text{benefits cost}) \times 100}{\text{Annual revenue}}$$

Labor costs vary widely depending on industry, and people-intensive industries such as professional services have a higher labor cost revenue percent. The average for your specific industry is a good measurement for competitiveness.

Recruiting and staffing

Strategic executives avoid the nitty-gritty details of day-to-day human resources issues, preferring to take a broader perspective. Executive priorities include recruiting and staffing, turnover and succession, compensation, and benefits. These are the most expensive functions of HR and the organizational challenges having the greatest impact on company objectives. Finding and hiring the right employees is essential to business success. The right hire can bring a team together and deliver brilliant new ideas. The wrong hire can be a disaster, resulting in lower team morale and missed objectives.

A CEO needs his or her company to be seen as an employer of choice by potential candidates.

HR must plan for the workforce needed today—and in the future. Employ these strategies:

- Cultivate relationships with talent not yet on the market.
- Develop a wish list of professionals for critical positions. Ideal candidates can be internal or external. If you experience turnover, you have a list of potential candidates to recruit from.
- Make word of mouth your best recruiting tool.
- Implement referral bonuses for employees who bring you excellent candidates.

What the CEO needs: Staffing reports

The CEO needs to know the big picture of what is going on with recruiting. How many openings do we have? Is that creating any backlogs in production? What will it cost to fill the positions? A staffing report provides a nice overview without getting into the individual details of each hiring decision or new vacancy.

When preparing staffing reports, be sure to include:

- Positions filled.
- Turnover rates.
- Cost per hire.
- Difficult-to-fill positions with strategies for overcoming the obstacles.

Key metric: Cost per hire

Departmental managers are clamoring for additional head count. The CEO and CFO must decide whether to authorize new hires, so they need to know how much it will cost to recruit qualified employees. Calculate cost per hire by dividing recruiting and hiring costs by new hires.

$$\text{Cost per hire} = \frac{\text{annual recruiting and hiring costs}}{\text{total number of hires}}$$

When calculating recruiting costs, be sure to include: recruiting department salaries and overhead, outside recruiting agency payments, advertising costs, hiring bonuses, referral bonuses, relocation costs and bonuses, and any immigration costs.

The CEO needs to know the big picture of what is going on with recruiting.

Turnover and succession planning

Most executives would like to minimize turnover. There are times when economic conditions necessitate losing employees to layoffs. Some companies make a policy of routinely turning over the lowest performing employees within the organization, in an attempt to create excellence. But as a general rule of thumb, turnover is very costly to an organization. Layoffs or resignations can disrupt team momentum, slow production, and lower morale. You risk losing some or all of the departing employees' job knowledge. On average, it also costs between one-and-a-half to three times an employee's annual salary to recruit, hire, and train a replacement.

Executives need help from HR to plan for changes in the workforce. This includes modeling scenarios for changes in the organizational structure such as layoffs or promotions, identifying worst performers, creating career development and retention plans for top performers, and planning succession for mission-critical positions in the event of an unexpected departure.

What the CEO needs: Plans for top performers

Not all employees are created equally. Some workers perform average work, as expected. Some hardly contribute at all and need to be replaced. And a few employees are the driving force behind your company's success. These top performers, usually about 20% of your workforce, are responsible for 80% of the work performed. They are your big idea people. They work hard and they work efficiently. Your CEO does not want to lose the high achievers, so HR needs to have a plan for retaining them. This involves making sure that top performers are given plenty of new challenges in their work, opportunities to move up in the company, and recognition and compensation that reflect their value to the organization.

Key metric: Monthly turnover

Your staffing report to the C-suite should include the percentage of turnover your company is experiencing each month. It's an easy way for the CEO to spot worrisome trends, such as a spike in employee resignations. Calculate it by dividing the number of employees who left the company this month by the average number of employees working this month:

$$\text{Monthly turnover} = \frac{\text{Employee separated}}{\text{Average number of employees}} \times 100$$

If you find calculating an average number of employees too difficult or time-consuming, you can use the number of employees employed on the fifteenth day of the month, as long as you're consistent about it. On an annual basis, this should average out without significant variance.

Your CEO does not want to lose the high achievers, so HR needs to have a plan for retaining them.

Compensation

Compensation is a critical part of any workforce strategy. You don't want to discourage high-performing employees with low pay, or worse, lose them to your competitors. On the other hand, it's harder to reach corporate profitability objectives if you are paying your workers too much. The CEO needs help from HR to determine how to compensate employees at a rate that is equal to their value to the organization.

Compensation rates vary based on many factors, including:

- Specialized skill sets and/or professional certifications.
- Amount of employee experience.
- Your industry.
- Your business location.
- What your competitors pay for similar skills.

What the CEO needs: Competitors' compensation plans

Salaries can be one of the biggest headaches for a CEO. Every manager worries about turnover of their top performers and wants to pay them more. Your CEO wants to establish the company as an employer of choice, so you can recruit great talent and retain the best employees. But you need to achieve that status at the lowest possible cost. So it's essential to gather information about how much your competitors pay for key positions, and how they incentivize performance with bonuses, stock options, or other perks.

Provide the C-suite with comparative analyses for your industry, as well as your geographic location. How do your salaries compare with key competitors' plans? For your business location, are you paying attractive wages compared to the cost of living? Are there creative programs that could enhance the "total compensation package" without adding much cost?

Key metric: Compa-ratio

Compa-ratio is often used as a benchmark to determine how close an employee's salary falls to the midpoint of the salary range established by your company. It is calculated by dividing an employee's salary (or group's average salary) by the median of the salary range.

$$\text{Compa-ratio} = \frac{\text{Employee's salary}}{\text{Midpoint of the salary range}}$$

A compa-ratio of 1.00 means the employee's salary is exactly at the midpoint; higher indicates above the midpoint. Employees with compa-ratios lower than 1.00 are at high risk for job dissatisfaction and turnover. Employees with high compa-ratios may be overpaid.

Your CEO wants to establish the company as an employer of choice, so you can recruit great talent and retain the best employees.

Benefits

What the CEO needs: Future benefits cost projections

To plan for business growth and maintain profitability, the CEO needs to be able to project both revenues and costs as accurately as possible for one year, three years, or even five years into the future. In HR, the greatest uncertainty surrounds the future cost of benefits. Provide your CEO and CFO with projections for the cost of benefits next year as soon as open enrollment is completed. For further-out timeframes, provide the best projections you can, possibly with a range that models best-case/worst-case scenarios.

The new healthcare reform law has made projections even murkier, as it is difficult to tell how high insurance companies will raise premiums while they can in the next few years. Executives of smaller businesses who are not mandated to offer health insurance will need help weighing the pros and cons of dropping health insurance benefits. This includes the perceived value of health coverage by employees and the impact that dropping it would have on employee retention.

Key metric: Average benefits cost per employee

To help executives get an idea of the big picture on benefits costs, show them the average employee's share of total benefits costs. Divide total benefits costs by total employees. Include healthcare costs, retirement plans, savings plans, life and AD&D insurance plans, tuition reimbursement, and automobile expenses.

$$\text{Benefits cost per employee} = \frac{\text{Total benefits cost}}{\text{Number of employees}}$$

If your benefits cost is high, provide the CEO with an analysis, drilling down into what is driving the costs. Is it rising healthcare premiums? Or additional retirees using benefits? How do the benefits in question affect employee retention or engagement? What are potential strategies to contain or reduce these costs?

The CEO needs to be able to project both revenues and costs as accurately as possible.

The bottom line

As the economy continues to pick up steam, CEOs face many challenges ahead in the constantly changing business landscape, and it is HR's duty to help them cultivate and maintain an optimal workforce in order to ensure stability and profitability.

It is important for the executive team and HR leadership to view HR as a strategic partner in the company's future and not as a caretaker. To help overcome any resistance from doubtful executives, HR leadership must move beyond its historical role of viewing things through a narrow process-oriented prism and adopt a big picture mindset and truly understand the business if it is to be truly accepted as part of the executive team.

While there are a number of modern HRMS tools that can help HR's efforts in the areas of talent management, leadership, workforce planning, and advanced workforce analytics, one of the most indispensable in regards to decision making is an HRMS dashboard. A dashboard is ideal for identifying critical data that needs to be acted on, particularly when it can affect strategic thinking and needs to be relayed to the CEO.

In today's competitive environment, to succeed, it takes an executive team that has up-to-date information to help it make better decisions, and that means having the support of a modern HR department with up-to-date tools. The question is: How well prepared is your company to compete?

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About Sage

Sage is committed to supporting small and medium-sized companies by developing solutions that create greater freedom for them to succeed. For more than 30 years, we have been a leader in the development of Human Resource Management Systems (HRMS) and payroll software.

For more information about our products and services, visit: [SageHRMS.com](https://www.sagehrms.com)

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