Reversing the arrow: using business model change to tie HR into strategy

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If we read the popular literature, we could be forgiven for concluding that the HR function's very existence is under threat. It must, the story goes, increase its strategic capability or face the inevitable (and largely dire) consequences. But what might this Strategic Capability look like? Our solution to this challenge, is to Reverse The Arrow. This involves focussing less on the "HR for HR" side of the equation and much more on the contribution made to the business by the Function, or what we describe as Performance-Led HR.

With this end in mind, and at the request of our senior HR Director (HRD) partners, we embarked on the Centre for Performance-Led HR's first major research project exploring the journey made by HR functions in the last decade. Our aim was to examine how far HR has progressed since debate over the strategic contribution made by the Function was initiated by David Ulrich's Human Resource Champions.

In the Full Report we have lifted the lid on an issue – that of business model change – and in so doing reveal the complex and messy problems involved. We provide some rich research data to demonstrate this and introduce a lexicon of ideas and conceptual material to bear on this problem, in order to help HR make sense of their contribution in the arena. This Executive Report summarises the key arguments and ideas.

Ours was not a research agenda to establish the strategic credentials of the HR function. This we took as axiomatic. Leaving behind the circular debates initiated by a largely negative HR media, seemingly obsessed with the extent to which HR was at, or even on, the boardroom table, we took as our starting point HR functions who already had the backing of their top executive teams to step up to the strategic agenda. This provides valuable insights. It has allowed us to explore the variations in the development and characteristics in the execution of HR's strategic capability. We refer to the interchange between strategy, business model and HR architecture as strategic reciprocity.

For us, this meant unlocking and understanding what overarching strategy is within businesses as a whole, and understanding the interplay between business models and people strategies, how they are put in place by executives in order to underpin the strategic execution and delivery of their business' strategic intentions. The focus in this research on the issue of business model change provides one such opportunity to further explore and understand how the relationship between strategy, business model and people strategy affords HR a central role in business activities going forward.

In exploring how HR helps organisations to understand how best to implement strategy from a people perspective, we avoided the trap of much writing on strategic HR, which typically insists HR must be the common denominator to all things strategic. This report clarifies:

- How we should think about people strategy in the context of business model change?
- How we understand where HR is now?
- How we should look at strategy and understand the kind of people strategies that are associated with the emerging business models?
These are important questions, not least because the potential problems and risks associated with innovation in business models can be very high – events at Enron and more recently at Citigroup and Northern Rock attest to this. Many organizations within a sector essentially pursue the same strategy. Competitive advantage, however, lies in the differentiated ways in which organizations ultimately execute their strategies, in which people-related factors play a highly influential role.

The key messages that emerge from the study

We aim to show you that:

1) HR work at strategic level entails a deep understanding of an organization’s business model, in particular the way in which value is contributed to that model by all stakeholders (internal employee groups, partners, suppliers, service deliverers and so forth). Only by looking at the delivery of a business model in its totality can HR to be able to add value to the change

2) The transformational nature of business model change entails the primacy of an Organization Design (OD) agenda in HR at the highest level for it to be effective. However, as we shall demonstrate, what is meant by the term OD is changing.

   We call it “Architectural Design” to emphasise the distinction. Organization design should not be confused with organization development (though the latter is still an important issue).

3) HR “Strategy” ceases to exist in the ideal situation; there is business strategy, and this will be associated with an HR process. At the highest level, the two become synonymous with HR nested within the business strategy. Only then does the functional strategy become important

4) HR added value derives from an intuitive relationship with the line, an understanding of the organization’s strategy and business model, and a creative business-led explanation of how HR process integrates with it (a process we call “reversing the arrow” counterbalancing a recent trend in HR to install certain processes and structures with little regard to business model)

5) HR is in need of some useful analytical tools to better articulate its contribution.

   Understanding what these tools should be becomes clearer by carrying out a more refined analysis of business model change – based on the scale, and the stage, of change. This leads to a better understanding of the nature of HR work at each stage
Business Model: Business model thinking represents the core logic to create, capture and leverage value in a way that generates both profitable and sustainable revenue streams. A business model is the dominant performance logic that specifies how business is done, who the customers are, where the costs and profits are.

This logic outlines how and why the organization works as it does, how financial and non-financial resources have to flow through the organization and what organizational capabilities are necessary to ensure such joined up implementation of the business model.

The model typically involves the following elements: a value proposition; insight into the nature of business inputs (such as technology); an understanding about how to transform these inputs; the consequent nature of business outputs; the changes these make to the vertical, horizontal, and geographic scope of the organization and the nature of its customers; and how to organise in order to deliver all of these combined elements.

Innovation in the business model requires developments in the structure and/or the financial model of the business and so also includes strategic partnerships, shared services, or alternative financing vehicles.

Why look at Business Model Change?

In the field of strategy the issue of business model change is dominating the attention of business leaders and the term has entered mainstream thinking, we would argue for the following reasons:

1. Research on CEOs constantly reveals the centrality of business model innovation to competitive advantage, and constitutes executives’ main short- to mid-term strategic priority.

2. Strategy academics argue that whilst strategy – in short, the opportunities a company will pursue and those it will pass by – concerns the long term creation of value and the process of making strategic choices, business model analysis facilitates clearer articulation, testing, and validation of these choices together with a more finely grained differentiation in strategy because business models describe and capture both the organization’s value chain, and its unique resources or position within this.

3. Moreover, the economic value of business model innovation is increasing. A range of influential bodies and consulting firms believe that the way in which innovation is fostered is changing under the influence of globalization, information technology and resulting competitive processes, leading to a situation in which business model innovation becomes more transparent and easily copied. More decentralized ideas generation and handling inside organizations can be used to integrate elements of the value chain in more flexible, but also often disruptive, ways.

4. Organizations located in more developed economies are facing intensifying domestic and economic competition. For example, Taiwanese textiles contract producers that feed Western fashion and consumer goods companies are establishing design-networks, managed by supply-chain experts,
that bring together groups of just-in-time suppliers from across Asia into alliances that stay together only as long as each continue to learn. Similarly, the Indian software industry, is moving beyond a low-cost offshoring model, and is developing business models that bring together academic laboratories, start-ups, venture capital firms and large independent software firms and some of their most important customers.

5. Central to this competition is the ability to bring together the known constituents or knowledge bases associated with a new business model called “architectural capability”-9. HRDs in organizations undergoing business model change, are often aware that the people implications of the changing capabilities sought under the model are more profound than the top team, or other strategic functions, have bargained for.

6. In order for organizations to make their models work, they must understand the potentially deep implications they have for their people. People management experts have to make sure that those engineering the new business models are working on assumptions that can reasonably be executed.

7. Those organizations whose models remain the same are still having to prepare their workforce to compete with competitors whose models have changed. Facing such innovations from competitors located in different sectors, organizations may still face deep changes in systems, work practices, and the mindset of executives and employees alike. The need to respond vigorously just to maintain a market position still driven by an old model is often not accepted. However, better analysis using some of the concepts outlined in this study may allow HRDs to communicate to their workforce a more realistic understanding of the challenges that their organization faces.

8. Deep strategic and operational insights are just the starting point. Given the uniqueness of this knowledge and the need often to operate across partners, bespoke HR structures may be the best way of meeting business needs.

The Business Model Vacuum

A central task facing HR is to identify how its leaders, the function itself, and the people processes it manages, add value during periods of business model change. Nevertheless, discussion of the HR elements of business model change is almost entirely absent from academic or even practitioner literature (as opposed of course to the all pervasive coverage of Strategic HR). Consequently, our study is seeking to fill this vacuum in the HR executive knowledge base.

Business model thinking represents the core logic to create, capture and leverage value in a way that generates both profitable and sustainable revenue streams. It requires the specification of how an organization brings together both the pattern of, and importance of, existing organizational capabilities and/or innovations. Much work on how these aspects come together into one value chain under the aegis of HR architecture its infrastructure, its system or organization and employee behaviours has already been undertaken. Little work has been undertaken, however, on the possible ways in which such an HR architecture interchanges with existing business strategy and business models to add value. This interchange between strategy, business model and HR architecture we refer to as strategic reciprocity.
Strategic reciprocity: is more than the alignment of HR (and its architecture) within the larger system of a firm's strategy implementation. Strategic reciprocity captures the current state of HR in relation to the interchange that takes place during emergent strategy and business model change. Crucially, reciprocity does not suggest that HR strategy is determined by an overarching business strategy. Rather, it is complimentary to it. For example, whilst overarching business strategies and models may move through significant change, the underpinning business models and state of HR may be able to meet the people management aspects of such strategic changes whilst simultaneously remaining itself unchanged. It has been designed in such a way that it can adapt its capabilities to meet new ends. Conversely, whilst organizations may find themselves in a period of strategic consolidation with little overarching business model change, HR functions may be experiencing internal transformations involving the radical overhaul of their structures, capabilities, service orientation and, critically from our perspective, their underpinning business models and their correlation to overarching business strategies.

These critical capabilities are often a consequence of bringing together or understanding the interdependencies of systems. They might relate to the supply chain, distribution and logistics, product and service innovations, consumer insight, knowledge or information flows. The model may be delivered through an organization's own architecture, and/or through a network of partners whose own business model helps create, market and ultimately deliver value.

Understanding a business model therefore requires both deep strategic and operational insight. So, for HR, influencing thinking around the business model is more important and impactful than being aware of strategy and having a seat at the top table. Strategic capability, then, is about being situated in the operational hot seat in such a way as to ensure the alignment and execution of HR so that it drives the business models underpinning organizational strategy.

Business model changes alter the strategic value that is attached to particular types of knowledge (see below). It also changes the way that different types of knowledge have to relate to each other. In the box below we use the word knowledge. Of course, knowledge represents the starting point, but once this knowledge has become internalised into an organization and is supported by all of the supporting systems, structures, and processes, a deeper capability has existed.

The type of knowledge shifts involved in business model change

HR Directors can help the organization understand whether Business Model change might involve changes to only one, or to a combination of both, of the following:

Component knowledge (also called Operational knowledge): refers to an understanding of the nuts and bolts of the operations of the business. It is based on knowledge of the parts – or components of the business - rather than the whole. This knowledge of common components can be applied to the sub-routines or operations that overlap in the new business model.
HR Directors have to understand whether – and how – their organization can develop deep enough knowledge of all the various partners (such as internal functions or external business partners) expertise so that it can assimilate, interpret, apply and recognise the value in this knowledge. Only with deep component capability can new possibilities be explored.

**Architectural knowledge:** requires the shared understanding of how the new strategy and business models require interconnections between of all the operational (component) knowledge. In short, how things fit together. Knowledge of common architecture relates to the organization-wide routines (or indeed cross-organization and cross-partner routines) that have to be co-ordinated and combined, so that the various components can deliver their value. It is knowledge of the bigger picture. It requires the HR Director to be sure that the organization has thought through the strategy and business model and has understood the (potential) conflicts contained within this picture. This type of capability gives the organization a much better chance of to able to tweak and exploit the business model.

The ideas of Ulrich gave much impetus to the HR function from the late 1990s. They have propelled it forwards and helped it look at its contribution to value and the bottom line. However, by thinking more deeply about the changing value of knowledge inherent in business model change, and about the capabilities that HRDs need to align the HR contribution to this, we can move beyond this. Two contributions have been made by this work. It has helped HRDs think about the structures (generally based around how HR organises its processes) and role changes associated with a separation out into transactional work, HR business partners and centres of excellence. It has also helped change HR from a process-specific function into a business with its own P&L and concomitant transparency and ROI visibility.

**HR’s Contribution to Value**

However, we must now move beyond this towards an understanding of HR leadership as it relates to enabling business model change. Our analysis shows that jumping to off-the-shelf structures on the assumption that they will fit the challenge of business model change can be dangerous.

Before we move to the methodology section of the report it is worth outlining some of the language we used as the project developed that enable HRDs to demonstrate HR’s contribution to the business and its functioning, or more specifically how it contributes to value inside the organization. We increasingly believe that the HR value contribution is evidenced in three ways.
How do HR directors argue contribution to “value”?

1. **Value creation**: ensuring the organization has the ability to build and acquire talent and in turn develop the value proposition inherent in the business model. This requires: understanding the new organizational capabilities central to the business model; managing immediate and sustained talent challenges; and developing HR processes that engender the requisite performance outcomes such as innovation, customer service, efficiency or effectiveness.

2. **Value improvement and leverage**: enhancing the business model as it develops and learning how best to execute the business strategy. This requires: the HR function to be involved in transferring knowledge; to know how to optimise policies and practices; to manage the learning that results from any change or execution process associated with new business models; and to have multiple channels that ensure engagement of the business with such issues.

3. **Value protection and preservation**: making sure that any value that has been created does not then get lost. This requires: the design and maintenance of effective governance processes; constructive surfacing of the risks inherent in a business model and appropriate mitigation strategies; ensuring that the organization has a strong reputation across a range of stakeholders; and that it is able to retain its best capabilities (both people and systems).

Articulating how HR contributes to the creation, improvement and leveraging of value through the reconfiguration of business model change in our view now represents the central challenge to today’s HR executives. This is far from a straightforward process. Value may well have become, in Ulrich and Brockbank’s words, ‘the bellwether for HR,’ and the Function’s value remains very much in the eye of the receivers not givers of HR services.13

But there is no one-size-fits-all structure, silver bullet, or line of best fit we can use to combine business strategy, model and HR, as the daily challenges faced by organizations are highly contingent on the contexts in which they operate.

This study has purposefully been based on interviews with those senior line and HR players intimately involved in business model change processes. The issues raised present the opportunity both to understand the value that is added by HR to business model change and then deliver that value to the organization.
The project reported upon here focuses upon the original request of the centre membership — which was to discover by systematic research, what are the activities that HR departments should engage in, and be prepared to deploy, when faced by demands to support successfully all business model movement and change.

To understand this, in our research interviews, we questioned both operational and HR executives, within our member companies, about the key characteristics of the business model deployed both at the present time and potentially in the future and having clarified the characteristics and requirements of that model we then moved to discuss the contribution of HR.

We feel that only by combining the insights of Capability and Transformation Directors, Chief Executives, Business Directors and HR Directors can the people implications be truly understood.

The research is based on 30 primary interviews conducted across eight organizations, each organization facing a specific business context. The job titles of interviewees reflect high-level business understanding. The perspectives that we have explored include: two Chief Executive Officers, Managing Director UK Business-to-Business, Managing Director UK Consumer Business, Chief Information Officer, Finance Directors, Marketing Director, Transformation Director, Capability Director, Head of Transition, Superintendent Major Projects, Strategy and Marketing Manager, Group HR Directors and VPs, HR Transformation Director, HR Director Organizational Capability and Development, HR Director Shared Services, HR Capability Manager, HR Employee Engagement Director and a number of HR Business Partners.

To support the interviews we have analysed secondary material on each organization, such as public discussion of generic business models, annual reports, publicly available investor relations reports and presentations, as well as wider business media coverage. Behind this lies detailed literature reviews, under the headings of value creation, business models and strategy. The literature review is available in the Full Report.

In selecting the business contexts to analyse, we have attempted to capture the diverse realities faced by HRDs. Before embarking on the research we were clear that:

- The thinking inside organizations is at varying degrees of sophistication in terms of the level of insight into a new business model
- Regardless of the necessities for HR change dictated by a business model change, the relationship between the HR function and the business will reflect different levels of strategic embeddedness
- The degree of control that HRDs or indeed their CEOs have over the business model might be subject to other external influences
- The pace at which new business models have to be operationalized (the need for transformation) has to be balanced against the need to ensure safe steady-state operations

The findings in this report is based on an analysis of eight settings, each reflecting a different context, and different HR challenge.
A Typology of HR-Business Model Responses

When we look across these business contexts, and our analysis of other Centre partners, we can differentiate four different taxonomies that HRDs face with regard to business model change.

<table>
<thead>
<tr>
<th>Stage</th>
<th>Criteria</th>
<th>HR Headline</th>
<th>Case Examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Incremental Model Change</td>
<td>Stable or slowly evolving competitive landscape, Unchanged demand for value from customer, Business model relatively well known, already implemented, No change in strategic capabilities</td>
<td>Value through exploitation of performance logic of current business model, Continuous improvement of HR practices or reinforcement of capabilities relevant to model</td>
<td>Shell, McDonalds, Rowntree Nestlé</td>
</tr>
<tr>
<td>2. CHANGING the Rules of the Game</td>
<td>Organizations’ leaders proactive in driving transformational (business model) change, New capabilities needed</td>
<td>HR can be at centre of change through Architectural Design capability and innovative HR structures</td>
<td>NG Bailey, United Utilities, BAE Systems</td>
</tr>
<tr>
<td>3. The Changing RULES OF THE GAME</td>
<td>External change in the competitive landscape means organization value proposition is no longer valuable, New capabilities needed, Organization may or may not be responding with Business Model Change</td>
<td>HR reacts to short term strategic challenges, uncertainty, HR needs to help place business model change on the agenda</td>
<td>Royal Mail, Sellafield, Co-operative Financial Services</td>
</tr>
<tr>
<td>4. Fluidity</td>
<td>Continuous change in competitive landscape, entailing continual business model evolution</td>
<td>HR can be at centre of change, HR needs world class Design capability and highly flexible HR team, HR a strategic partner sharing and leading strategic evolution within the business</td>
<td>Vodafone</td>
</tr>
</tbody>
</table>

Figure 1: A typology of business model change scenarios
This typology is intended to be illustrative and not prescriptive. It represents the current state of strategic reciprocity in the organizations studied. Each of the examples positioned in the taxonomy have, and may well in future, evolve through the different stages shown. An important task is to understand the HR architecture associated within each, and in transitioning across each.

1. INCREMENTAL: Evolutionary Model Change

In the first taxonomy, the strategic landscape is known and comparatively stable or evolving slowly, and the business model is being refined and extended but concepts, and core capabilities, underlying the business model remain the same (franchising, or example, or the content of a financial transaction).

In the case of McDonalds, franchising as a business model is well established and is now being extended widely in the UK. Shell's competitive landscape has evolved in the last 10 years, and the company has added renewable energy to its strategic goals, but the underlying business model for the exploitation of hydrocarbons is relatively stable. The company is therefore aiming at exploiting its top quartile performance position in its market. Rowntree Nestlé acts as a disconfirmation of business model change. The business model has remained broadly the same. However, the shift in strategy means that in order to maintain the health of the model, investments were made in different components of it. The way the components fit together is broadly unaltered. It is easy to assume that just because there is a significant business improvement or process redesign programme that this automatically entails model change.

The key challenge for HR in these instances is therefore to advance their value proposition through better internal exploitation of the core performance logic of the current business model. At McDonalds, the HR focus is on continuous improvement of the engagement - performance link by (for example) setting up HR metrics to measure the link, clarifying HR's value proposition to employees, capitalising on a good social mobility position, and implementing coaching and development to improve restaurant level HR climate.

2. CHANGING THE RULES OF THE GAME: Internally Driven Business Model Change

In the second taxonomy, the change may be in response to a shift in the competitive landscape; but the organizations' leaders have reacted quickly to drive business model-led transformational change through the organization, often before competitors have reacted, or before others see the necessity of the change.

At United Utilities, the arrival of a new CEO began the drive to an entrepreneurial mindset from a public sector, bureaucratically – oriented mentality. At NG Bailey, the leadership team grasped the implications of intelligent building solutions as a value proposition despite the enormous shift this entailed from the company's traditional role as a subcontractor of maintenance services. At CFS, the Insurance and Banking arms existed as separate models until the arrival of the CEO brought them together under a single value proposition, architecture, and set of capabilities.
And at BAE Systems, the through-life capability business model is allowing them to take a lead position in a highly competitive landscape. Those organizations that understand both the key capabilities that get thrown up by the model - such as integrated business systems modelling or partnership arrangements – but can also demonstrate secure execution of these capabilities can capture significant value in existing markets and apply this learning to the development of new markets.

In this situation, HR has the opportunity to be on the ‘front foot’. Not only does the HR agenda have the potential to be central to the success of business model change, to an extent the HR agenda may be synonymous with it. Business model change entails redesigning the company’s value web, and developing new strategic (or “architectural”) capabilities, both firmly in the domain of HR expertise.

In each of these organizations there is still an element of the “Janus” effect, but there is likely to be much more forward-looking transformational activity on the part of the HR function. At United Utilities, the HRD is both leading a reorganization of the function to ensure that transactional processes are efficiently conducted through a shared services unit; at the same time as advising the Executive Team on what the new business model should look like. At NG Bailey, HR is leading the way on the creation of new organizational functions such as Business Development, and the development of new organizational capabilities for project managing long term building maintenance.

BAE Systems’ HR leadership has already reacted to the demands of changing the rules of the game by outsourcing of most of its HR function. At CFS, technology and regulation have placed demands for the increasing speed of financial transactions. Until recently the point of delivery of value to the customer and the nature of the product and service has been well established. This may involve taking the lead in advancing a case for the added value of HR where this is not well understood, so that at CFS, for example, the development of people-related capabilities (such as performance management, consumer intelligence, and leadership) to support organizational change has become central to the way the company is evolving, whereas previously these were considered peripheral at the Executive level.

3. THE CHANGING RULES OF THE GAME:
   Externally Driven Business Model Change

In the third taxonomy, a fundamental shift has taken place in the way that customers, or other key stakeholders (government, or regulators), perceive the value of the organization’s product or service. This will, ultimately, result in a threat to the survival of the organization, as its traditional capabilities will rapidly become outdated.
The organization should be reacting to this shift with a transformation of its business model; the nature and speed of this transformation will depend on how quickly the organizations’ leaders perceive the threat and are able, or free, to react to it. In Royal Mail, the threat is from competition from privatized companies and the internet, entailing its traditional offering—and its cost—becoming untenable. At Sellafield Ltd., the uncertainty of the Government’s position on the future of the Nuclear industry—only recently resolved—meant that until recently the organization knew only that the model was changing, without knowing precisely to what.

In this situation, HR may find itself “on the back foot”. It may not yet be clear what the future business model is; HR will therefore be reacting to operational challenges imposed by a shifting and uncertain landscape and—in the worst case—implementing HR strategy which is rapidly becoming outdated or irrelevant, and therefore losing its value to the business. HR may therefore have to look, Janus-like, in two directions: first, establishing stable, “best practice” HR processes to help the organization through a transition period; at the same time, keeping an eye on the strategic goal, where more fundamental changes to the HR architecture will be needed once the new business model is clear.

Thus at Royal Mail, the HR strategy has to date been to get to a “steady-state” position—stabilizing the industrial relations climate following investment in new technology, implementing major cost reductions, and moving the HR department to a modern operating model. At Sellafield Ltd., the HR team has been focusing on maintaining the capability needed to ensure continuous safe operations, assisting the organization to develop cross-functional structures, and developing new ways of working as the company shifts from cost—plus to fixed—price contracts. In both organizations, however, the transformation of the business model has yet to take place.

4. FLUIDITY: Continuous Business Model Change

In the fourth and final taxonomy, the competitive environment is in a state of continuous and rapid evolution. The organization cannot afford the luxury of crystallizing one business model for any length of time, due to the volatility of particular the market place, and at the risk of being left behind by competitors. Continuous evolution of the business model is central to competitive advantage and ultimate success within the market place.

At Vodafone, the most recent challenges are the technological shift in its customer value proposition from voice to data, and the political/economic conditions of a maturing Western European market and a rapidly emerging Eastern Europe. This type of continuous innovation demands that the HR department is world-class in what we refer to architectural design capability—a combination of old-fashioned macro OD with strategic consultancy and a well-developed competence in commercial and economic realities. Engagement—the reinforcement and measurement of employee discretionary effort—also moves close to the top of the HR agenda.
Key HR Activities and Capabilities

In this section of the report it is our intention to outline those key elements of HR strategy and practice identified by our respondents that need to be “mastered” by HRDs and their teams in order to contribute effectively to business model ongoing management and to any proposed change to the model: fluid or incremental.

We focus upon the responses to questions given by both operational and HR executives regarding both the leadership and support to the business model that HR provided. We identify those elements of that leadership and support which were considered to be positive and viewed as successful, which were less so and what were regarded as key HR strengths. In addition in a number of interviews we probed for what were the key learning points for operations, support services and HR.

Outlined below are the key activities/functional competences that were nominated in the research as being crucial in terms of allowing HR functions to be both proactive and effective in this lead and support role in sustaining successful business model operation.

Before we describe those key activities/competences it is worth outlining some qualifying points to note:

- First and foremost the following five activities may be viewed as a totality that, if all are present, should provide for a high level of proactivity within that HR function. There is a logic that links each capability to the next, and this logic has dictated the order in which each must be presented

- However we suspect that few HR functions, at the present time, would have “mastery” of all the capabilities outlined

- Our view would be that the balance of HR capability that a particular function needs to possess is dependent upon the business model cluster that they inhabit. So, for instance, a company operating within the Fluid cluster may require a more comprehensive OD resource than one operating within an Incremental change cluster
1. A Symbiotic CEO/HRD Working Relationship

**Headline issue:**
Does the CEO ‘get’ the people proposition? When they do, do they really think that the HR agenda is as important as any other part of their responsibility?

**Strategic imperative:**
HR’s role in organization strategy, especially at a time of Business Model change, is largely dependent on the attitude of the CEO. If the answer to the headline issue is “yes”, fine; HR strategy will eventually be indistinguishable from business strategy. If the answer is “no”, then do not even try and talk about HR’s strategic role. Put in place good efficient processes, and look elsewhere if you really want to do strategy. Otherwise you can talk about it, but it won’t happen.

**Must-win battle:**
Make sure that as HR Director you quickly develop an intuitive relationship with your CEO, as close as any other in the senior team.

Throughout the project the theme of a healthy and mutually supportive relationship has been highlighted as a key component of effective HR activity within our member companies. Our HRDs have frequently cited the crucial importance of “connecting” and the simple but crucial element of frequent meetings between CEO and HRD.

An effective relationship with the CEO is a precondition of all the subsequent capabilities outlined in this section. The extent to which the HRD has become socialized into operating through such a relationship helps them of course into a deeper understanding of the business model change, but can also enable HRDs to lead the top team towards a progressive and people-based insight of the organizational issues involved.

It is significant that the need for the healthy relationship at this level is not only cited by the HRDs. A number of the Managing Directors and CEOs interviewed also dwelt, at some length, upon the importance of a strong relationship. One CEO stated:

“There’s nobody that I’m more intimate with than my HR Director. Typically the person the General Manager is closest to is the Finance Director. Part of my philosophy is that the two people I’m closest to are my finance man and my HR man.”

Clearly if the relationship is not present then implementing effective HR leadership will be a formidable task.
2. HR for the Business

Headline issue:
If one considers HR activity as a value chain, at what point on the value chain does one commence the HR contribution? Does the HR function start from HR best practices and HR performance management, or from the opposite perspective, a clear and thoughtful evaluation of internal client needs?

Strategic imperative:
People are of intangible value. One manifestation of the CEO “getting” the people proposition is that HR have to “get” the business proposition in return. Only then can they release the people value inherent in the business. HR act as value brokers in this regard. Business model change provides a perfect opportunity for HR to provide this value brokerage.

Must-win battle:
The HR Director needs to be driven by the analysis and nature of BM change and then the shaping of organization structure and HR processes, not the other way round. Measurement of performance becomes the end of the process, not the beginning; “reversing the arrow” means developing a clear, business – oriented explanatory framework for the centrality of HR.

This issue was discussed within a number of the respondent companies as being a key perspective on the part of the HRD and the HR function if HR was to provide relevant contributions to the business and in terms of the business model. In essence if one considers HR activity as a value chain, at what point on the value chain does one commence the HR contribution? Does the HR function start from HR best practices and HR performance management, or from the opposite perspective, a clear and thoughtful evaluation of internal client needs?

A view is emerging from the research, of the criticality of HR bringing value to the business model and to do that pre-conceived notions regarding HR policies, priorities and practices can be damaging to meaningful value contribution.

HR must be fully responsive to the strategy and business model of the business. HR is not a rule for itself. It is not “HR for HR”, but HR (as broadly defined across the competing stakeholders whom HR has to satisfy) for the business.

One HRD put it thus:

“I think we’ve done it back to front. I think we’ve defined the (HR) model before we know what the organization is. To what degree is responsibility transferred to the line? And where is the best commercial value for that? Because I think in HR we have a view that says it’s the HR model that dictates it and not just coming from it from our internal customer, but our external customer.”
3. Organizational Design as a Prime Capability

**Headline issue:**
- What are the key steps you take, and in what order, to support Business Model Change?
- To what extent does your HR function march in lockstep with the change?
- Where are you? Have you arrived yet?

**Strategic imperative:**
We observe that some of the five key capabilities/competences outlined in this report are essential whatever the business model situation that the organization finds itself to be in, whereas some are more appropriate to specific business model situations.

The OD team must possess high levels of credibility.

**Must-win battle:**
- The HR Director must recognize the primacy of OD expertise in Business Model change
- They must agree what is implied by this capability. We use the term Architectural Design to signal that the understanding of this capability is still vague, but its contours are being shaped by the need to develop the architectural knowledge that is required to deliver changing business models.
- This capability might not be seen as being anything to do with HR. HR Directors need to lay claim by having a good OD resource or recruit one fast. The OD discussion is at the heart of the strategic discussion.

We would observe that some of our key capabilities/competences are essential whatever the business model situation that the company finds itself to be in whereas some are more appropriate to specific business model situations. Our research indicates that OD capability is most required in the Fluid and Changing Rules of the Game clusters but particularly Fluid where both structures and teams will be changing in orientation and membership constantly.
There is, of course, a long and - mainly - distinguished history of organization development in the HR field. But there is a crucial difference between whether the D in OD refers to design or development. The Development ‘D’ refers more to understanding the processes necessary to progress a specific strategic path, the centrality of people issues within this as an important leverage factor, and the consequent development implications for these people. The Design ‘D’ is a much harder-edged capability. It is based on principles of organization analysis, linking strategic outcomes to the structures and system architectures that create them – a more prescriptive and highly-business aware science.

Organization Design (OD) refers to the combination of strategy, structure and internal control and co-ordination systems that provide an organization with its operating logic, its rules of resource allocation and its mechanism of corporate governance.

It is the Design D that has been elevated to the centre of the HR agenda, when the strategy involves a change in business model.

We acknowledge here that understanding this new capability is now a pressing challenge for practitioners and researchers alike. Indeed, it forms one of the bases of our next stream of work.

One suspects that in Fluid companies the OD discussion is at the heart of the strategic discussion. Also the OD team must possess high levels of credibility. As one member HRD said:

“The OD people … must be in the space, not only advising on different organizational models, but in the strategic direction of the business, and advising that that thinking should be going on around that organizational change … if you’re at the heart of the OD thinking the rest follows, the resourcing, the engagement piece. It’s all about the relationship with the key guys, the rest follows.”

Another stated:

“We’re taking an OD oriented approach (to change). We define the OD principles and we’ve created a state of readiness and in order to prove that you’re ready for change we’ve created a checklist, you have six boxes. When you have six you’re ready to go, so it’s incremental, go when you’re ready, everything has to be defined before you change.”
4. The Business Utility of the 3-Box Model

Headline issue:
How do you organize your HR function and delivery service to employees? What does the nature of this delivery look like? Does the context of business model change alter the business utility of Ulrich’s 3-Box model?

Strategic imperative:
The current dominating influence of the Ulrich 3-Box Model upon HR structures was amply demonstrated by the frequency with which the topic occurred during the research project. In our interviews both HR and operational managers demonstrated familiarity with the characteristics of the model and what it could imply for the HR contribution.
Overall we seemed to be witnessing some advocacy for thinking through carefully whether an introduction of the 3-Box Model structure would enable HR to lead and support the business model. Does it fit what HR aspires to achieve?

Must-win battle:
HR Directors need to ensure that the Ulrich model – even if it is the right high level structure for HR – follows the analytical process we described above, and does not precede it.

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“What (the previous HRD) had told people before I arrived is that as a HR model we would go with the Ulrich model which I’m incredulous at because I’ve never described the model we use from a HR point of view from a business text book because it immediately makes people feel very uncomfortable. It is impractical and the devil is in the detail.” (Partner HRD)

Others seem more confident regarding the model’s implementation based on previous experience:

“Within each of the operating companies we’re moving towards a 3-Box Model. I have an HRD in each of the operating companies, and each operating area will have a centre of expertise, with an OD person, a reward person etc then generalist HR practitioners, called Business partners now to deliver the end to end HR service, to whatever the customer base looks like.” (Partner HRD—note this company has a central internal HR transactional centre)

We need to reflect whether the project has unearthed any evidence of “post-Ulrichian” thinking and structures. We feel that at this point we have not but that some partners may be very close to moving into new structures and HR philosophies.
5. Future Proofing Talent

**Headline issue:**
To what extent does HR concentrate on strategic capability (as opposed to building its internal talent management practices, functional capability, and knowledge)?

**Strategic imperative:**
Dealing merely with the HR agenda of competence or talent management fails to engage properly with the immediate issue of strategic capability, which is an organizational characteristic of which the people agenda is only part.

**Must-win battle:**
The project unearthed a strong level of awareness on the part of senior operational executives that, based upon the now accepted notion of the possession of talent being a key component of competitive advantage, HR made a vital contribution to business model health by establishing and managing a talent pipeline that provided for both present and future business model requirements.

However, future proofing talent requires that HR Directors understand the skill formation process taking place within their organization’s business model, and then take out all options necessary to manage this process.

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“The task is to future-proof talent.”

Or as one Managing Director expressed:

“Where the business model is about differentiation it is very people dependent.”

“With certain roles you can choose from a wide spectrum of people but when you move to senior management, then the quality of people is crucial, particularly when the industry is made up of companies where a lot of people are pretty average.”

In another partner company a director responsible for transformation stated:

“The piece we’re missing, in two or three critical dimensions we simply don’t have the capability, it’s not about deploying a capability differently, it’s about simply not having it.”
Conclusion: The Evolving Strategic Capability of HR

In order to build on the data analysis we ran a Research Interpretation meeting among the Centre partners. This identified seven broad areas of action for senior HR players. We briefly synthesize each theme and raise the questions that should direct the future research agenda.

It is clear from our research that the commitment and effective deployment of talent inside a business drives the economic returns of organizations. Moreover, the spoils of high performance go to those organizations whose HR functions can reverse the arrow and who understand that the viability of the function itself lies not just in world class architecture comprised of systems, people and behaviours but also to those whose functions' architectures play a central role in enabling the business models put in place to execute overarching strategies. This is far from a straightforward task.

1. Organization Design: The New Strategic Capability

Many leading commentators agree that the Function’s future will be different from its past. Much of what we know today as HR architecture will no longer exist a decade from now. For Pfeffer and Sutton, ‘what actually provides competitive success and what is difficult to copy is not so much knowing what to do deciding on the right strategy but instead having the ability to do it’ 15. For Gratton the challenge for HR is one of understanding how to put people at the heart of corporate purpose16. For Becker and Huselid the challenge is one emphasizing, ‘the role of HR management systems as solutions to business problems rather than individual HR management practices in isolation’17. And finally, returning to where it all began, for Ulrich, the challenge facing HR has been and in many ways remains one of delivering value and recognizing the shift in importance from organizational structure to capabilities18.

All of these authors are united in their view that it is those charged with devising and leading the execution of business models that will ultimately shape the destinies of their organizations. With them lies the responsibility for creating value for those inside the organization (employees) and outside it (customers and investors).

Significantly, and clearly underlined by this report on Reversing The Arrow, has been the clear rise to prominence in the eyes of CEOs and other executives of those who are capable of delivering value being those people charged with leading the HR function. This is not to say HR’s strategic capability is revealed by the HR Director’s having a seat at the boardroom table. On the contrary, it is the close working relationship between CEO and HR Director that will drive the talent and future performance agenda inside organizations.

This close working relationship will centre on the capability of senior HR leaders to identify for themselves and their executive colleagues value releasing and value creating ideas across the business. This new demanding role clearly demands a new cadre of HR executives fluent in business strategy making and execution. It goes without saying that these individuals may not necessarily be those who come from a traditional HR background. A new generation of executives are eying up the growing challenges and concomitant resources of talent within the business with speculative eyes.
The HR executive market place will place a high premium on these same individuals who understand the alchemy involved in using OD to catalyze the strategic capability of organizations. These individuals will be capable of engaging in top-table dialogue, business function interchange and reconfiguration, and all the issues from globalization that accompany them; knowledge of their markets, change specialists, evidence-based analysts, and be capable of articulating, perhaps even from time-to-time fighting their corners, for a particular vision of the future strategic direction of their businesses.

In pointing to the overwhelming evidence for the primacy of an OD capability in HR to add value to Business Model change. We have also begun to use the term “Architectural Design” as a label, to put clear water between this capability and the more traditional HR “macro and micro” Organization Design agenda which has a certain – not always positive – resonance with HR and line people.

The precise definition of this new capability, and its implementation in HR structures, is the area of action we have identified. Certainly the centre of excellence – if that is how it must manifest itself – will borrow much of its expertise – and possibly its people - from outside traditional HR areas.

Indeed its very strength may be the cross – functional nature of the talent pool from which it draws its complement.

The opportunity for the HR function is to move into entirely new areas of expertise, while retaining control of a capability that is central to the organization’s strategic agenda. The questions which arise are:

- What will be the precise nature and positioning of the AD capability?
- If a centre of excellence, how will its members relate to the wider organization – through the BP, or directly to the line?
- To what degree is it possible for the BP to possess advanced skills in this field?

What will be the nature of those skills?

And there are two critical, related, risks to explore for the future of the HR function

1. As expressed by one HR Director: “do we want consultants to grab the Organization Design space?”

2. If the answer to this question is “no”, then where will HR recruit and develop the required talent for this new Architectural Design capability, even if it remains an HR function responsibility?

2. From Silos To Strategic Reciprocity

Simplistic views of strategic alignment paint a linear picture of an HR function adapting to changing strategic imperatives. In our new strategically capable HR world the function has greater nimbleness and agility but a sure-footed assertiveness to remain in “steady-state” when all else around it melts into air. This reciprocity is reflected in our taxonomies which reveal complementarity, as opposed to co-determinacy in the relationship between corporate business strategies and goals on the one hand, and steady-states of strategic HR deployment on the other.
Strategic reciprocity helps us to understand how HR and its accompanying architecture can be in different states to the emergent overarching strategies and business models of the parent organization. For example, where strategy might be described as emergent, especially fleeting and subject to frequent and radical transformations, HR's underlying state can, in contradistinction to this, be in ‘steady state’ or incremental in character. A certain calmness presides in one organizational subsystem at the centre of what can easily be depicted as a “strategic storm.”

Similarly, business models can be in an incremental, steady state, whilst the fluid models underpinning HR can be undergoing substantial redesign. Many HR functions struck us as falling into the middle of these two disparate types, hence the other two middle-state taxonomies, which say more about the emergent development of strategy than the tidy and normative, rational and linear world framed in the highly prescriptive classical strategy school textbooks.

HR executives can take comfort from this apparent dichotomy between overarching corporate and HR models. The complimentarity of business model fit does not prescribe a determined end-state of HR, to be read off by HR Directors and their colleagues: this is not a simple, ‘if situation or model x is in operation, we should deploy y version of HR.’ On the contrary, as Quinn has observed, ‘strategic decisions do not lend themselves to aggregation into a single massive decision matrix where all factors can be treated relatively simultaneously in order to arrive at a holistic optimum’.

In reality, strategic reciprocity releases HR from a number of ghosts that have dogged the function’s development over the last two decades. First, where there is new found confidence from boardroom discourse, this can free HR from the performance debates which were threatening to drag HR into a battle with the accountants not of its own making. HR was always likely to lose such a battle.

3. A Post-Ulrich Agenda?

HR might possibly be moving out into what might be described as the Post-Ulrichian agenda. New forms of modularity have released HR from the drudgery of transactional services. What has been described throughout this report as the “3-Box model” of HR has in some instances metamorphosed into a 2-Box model comprising strategic facing business partners and supporting HR experts who can live with the new and fast-moving world of strategic capability.

Each of our sponsors is thinking deeply about the structure of the HR function. This is taking them beyond the standardized prescriptions of widely disseminated theoretical models. They are, of course, in different places on this journey, but the destination appears to be the same: HR structures which respond closely to the requirements of unique, sector-specific business models.

We have seen some early signs of these “post – Ulrich” structures emerging in our current research. One, we mentioned above. Advanced structures have moved entirely beyond transactional HR work, which has been outsourced, resulting in something more akin to a “two box” model. A Business Partner (BP) is one side of the model, and we have seen this role encompassing work far broader than that normally prescribed in a Strategic HR textbook, or a CIPD qualification, to the extent that “HR” is no longer an adequate label. We deal with this role in more detail in a separate theme, below.
The other side of the model comprises the HR expert who offers value – adding HR consultancy services either to the HR BP, or directly to Line Managers. In certain areas of expertise – notably Organization Design or Transformation, Engagement, and Talent Management, a Director may be appointed, temporarily or permanently, to galvanise HR’s effort in that area.

However, the devil, as one HR Director pointed out, is in the detail; and it is the detailed planning and implementation of these new structures that will engage the Centre partners over the next phase of research. One such area of detail is the increasing importance of Organization Design work.

The next steps must now be to identify the new principles on which these HR structures can be based, and to understand their characteristics:

• why do they vary?
• what business drivers lead to these variations?
• how might these new structures capture and retain value for the business?

4. Remodelling the Business Partner role

The move out of HR into the line represented by the HR consultant and now business partner role required a transformational shift in the minds of those embedded in the world of HR transactions. A new transformation from business partner to strategic partner is now well and truly underway which pulls together the skills and capabilities of business generalists as well as HR careerists to construct and deploy new people-specific solutions.

A successful business model change demands a great deal from the HR BP. The HR Director leads the way, adding value to the strategic decision making process by advising on people related elements, and facilitating the senior team through Business Model Transformation. Knowledge of the competition, key markets, service – profit chain, capability management, and financial structures become as much a part of the BP’s portfolio as their HR expertise. Further down the organization, BPs at every level need to mirror this breadth of knowledge in their own Business Units.

Using the distinction we made earlier in the report between component and architectural knowledge, there is an argument that many existing role specifications for HR BPs provide a façade of strategic integration. BPs may only be able to embed HR into one component of the new business model, and whilst these individuals have general HR responsibility within that component, they are neither true HR generalists nor might they understand how all the pieces of the business model fit together. A priority for HR functions is to engineer multiple connections into the line, with BPs being one important such connection, but one with limitations.

Several questions remain, however – all of them raised by our Centre partners during the first phase of our research.
To what extent has the BP role moved entirely away from HR and into another capability domain altogether?

- What are the consequences of this move for the HR function?

- Is it possible to “map” more precisely the capabilities of this new role and to establish charters for its governance?

- Is it possible to develop a typology of different BP roles according to the nature of a particular business, or its stage of transformation?

5. Talent-Proofing The Organization

Our findings reveal to us three particularly important “must win” battles facing the deployment of the future strategic capability of the function. The first is represented by the challenge of human capital strategy essentially mapping the future talent requirements of the business both in the short- to mid-terms, and a longer, more strategic view of the required future leadership pipeline of the business.

Second, given the emerging evidence underpinning the performance case of “engaged” employees the continuing challenges of maintaining their discretionary effort will be met by those organizations who understand best the demands of their talent and provide competitive advantage through unique employee value propositions. Third, a function rising to the OD challenge prescribed by this new strategic capability will require an HR workforce with a new and highly demanding set of skills well beyond the capacity of current supply.

The research has shown the importance for HR Directors of second-guessing the talent requirements of their business going forward. In many ways this traditional form of HR has evolved into the new “Dark Arts” of human capital strategy and talent management. This is an art form requiring the “Janus-like” qualities of being able to service talent requirements in real time, while developing future pipelines of talent at all levels of the business and covering the different types of knowledge we have drawn attention to. It also requires being able to advise on capability matters during strategic debates, new models of delivery and retaining enough workforce agility for future reconfigurations should these debates require changes. This is the world of changing the engine while the plane is still in the air.

Strategic capability takes as read people strategies that accommodate models, systems and processes to drive a disproportionate amount of discretionary effort from employees. This is the world of retaining people through maximizing their chances to leave, boardroom transparency and concomitant exposure to the importance of employee engagement scores reported in company annual reports alongside the soon-to-be-legal obligation of quantifying the people value proposition for the forthcoming legislation surrounding the Operating and Financial Review people accounting criteria.

If all this were not enough, a recent report from McKinsey menacingly entitled *The Dearth of HR Talent* has predicted a shortfall in the supply of people with the requisite skills to support the world we have unpacked in *Reversing The Arrow*. Indeed, there is evidence to suggest it is already happening, with
the salaries of HR directors climbing at multiple levels of underlying inflation no easy task at the time of writing as organizations and their boards recognize the value of talent's talent who can recruit, retain and add value to the business.20 The McKinsey report sets out the challenge:

“At first glance, this model may appear to be fine, but the lines have not been drawn clearly enough when it comes to execution. To deliver on what the business needs, HR must put its own house in order, starting with the skills and capabilities of its staff.”21

The analysis in this report of the complex business model changes that face organizations, the observation that these models require transformations in the types of knowledge needed, that this in turn alters the strategic currency associated with a range of different capabilities, but that amongst all this turmoil a number of HR systems can represent an oasis of stability should give heart to the function. A range of intervention tools and techniques flow from the analysis in this report and these can address the challenge noted above.

6. Risks and Opportunities for Developing the HR Talent Pipeline

Each of these themes returns inexorably to the development of future talent in the HR function. Although we have not dealt directly with this issue in our research to date, it emerges as a central concern.

At the heart of the concern is, quite simply, the revolution entailed in the range of capabilities now expected of HR people if they are to be able to add value in the emerging business environment. Let us not forget this is a challenge faced by almost any significant function inside organizations. However, as one CEO commented to us, it is very rare to find an HR Director who possesses the required breadth of competencies to perform an advanced BP role at a senior level. We can be sure that the same comment is likely to apply at lower levels in the HR function; the level of expertise may change but the breadth remains the same.

We have also pointed to the expansion of HR capability entailed by the increasing demand for Architectural Design capability. Naturally, the opportunity is to transform the function by attracting a broader range of talent. One possibility is to make it “normal” practice to have a much freer transfer of talented people into, and out of, the function from other disciplines at both junior and senior levels. Several questions arise:

- Is the HR function attracting the kind of talent necessary to fill these new roles?
- Does the usual suite of CIPD or related qualifications deal sufficiently with these new demands?
- Are the development processes of young HR professionals entering the profession sufficient?
The consensus answer to these questions is: “no”, or not to the degree necessary to guarantee the future of the function. How can the function respond to this talent gap? At least part of the challenge appears to be the perennial problem of the negative—or, more charitably, perhaps—incorrect—perception of HR by people outside the function, and, occasionally, by those inside.

7. Rebranding HR

The last area of action therefore concerns the poor image of the HR function. One cannot help but be struck by the large cognitive gap between the findings of the research (which demonstrates the centrality of the function to adding value to business model change) and the low level of interest in HR from current general management students, who still treat the strategic HR agenda as very much secondary to the “usual suspects” of strategy, finance, and marketing.

There are signs of response to this challenge. Some organizations are beginning to talk about “people strategy”, and not “HR strategy”. “HR Directors” are becoming known as “Talent Directors” or “Transformation Directors”. There is perhaps an argument to suggest that the “HR” label should disappear with outsourced transactional services.

Back in the 1980s the move from Personnel to HRM was criticised for in many instances simply putting old wine into new bottles. Our research here shows that once again there is a need for substantive change in the role of the people making up the HR function. As we have said elsewhere, this may ultimately also reflect the demise of the function as we know it today.
References

7 This view has been expressed by the OECD, Booz Allen Hamilton, Boston Consulting Group and the McKinsey Global Institute.


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