The HR function, creator of financial value

An underestimated contribution

In the eyes of investors, the HR function remains above all a cost centre, a support function.
At most, they admit that it plays a role in the company's performance through recruitment or career management.

This article seeks to give back to the HR function its full weight by highlighting the paramount role that it has, or should have, on one of the benchmark indicators for investors: "financial value creation".

Definition of financial value creation

The market economy poses a postulate: a company creates value for its investors (shareholders and creditors) if, and only if, its profitability exceeds their expectations with regard to the estimated risks taken by investing in the company.

Generally, financial value creation is assessed according to two approaches:

- One, focusing on short-term visible results: the best company is one that achieves results better than expected at time "t", hence the importance of publications of quarterly, half-yearly, and annual results.
- The other, based on a longer time horizon, considering the creation of financial value over time, both quantitatively and qualitatively (significance of stability and/or recurrence of value creation).

This involves using concrete examples to demonstrate how the HR function can help to create financial value through these two approaches.

Three levers of financial value creation are available to the HR function

Revenue

Certain HR actions or initiatives can quickly contribute to increased revenue. The example of an "opportunistic" recruitment of employees, with a portfolio of proven customers or skills meeting a specific need, will immediately have a positive effect on revenue. However, in case of a sudden change in the market or the departure of one of these employees, the recurrence of revenue will be jeopardised.

Conversely, a recruitment "strategy" aiming to hire employees whose skills and development potential are consistent with the model and the growth of the company is critical for ensuring the recurrence of revenue in the medium/long term.
This is especially true if it is accompanied by compensation and evaluation policies based on the achievement of individual, collective and behavioural objectives aiming to create synergies serving the company.
In this case, commercial performance is no longer based only on a few individuals but on a team.

Operating costs

A compensation policy centred on the principle of encouraging individual employee performance, through the allocation of variable rewards based on achievement of annual goals (e.g. method of compensating sellers/traders in the trading room) contributes to controlling the company's operating costs over the year, in addition to boosting revenue. The amount of this variable compensation is thus perfectly predictable, as it is completely correlated with the growth of revenue.

However, excessive individualisation of the compensation policy may, over the longer term, generate a sense of frustration among employees by generating large compensation gaps, leading to an increase in the level of employee turnover.
It can also cause a compensation race with all of the associated negative ramifications, particularly a questioning of ethical principles (as seen in recent financial scandals).

The introduction of measures to integrate more collective concepts (e.g. profit-sharing) of performance incentives or integrating the company's earnings over several fiscal years (spreading out of bonus payments, compensation in shares or stock options) can lessen the negative effects of over-individualisation of compensation.

Economic risk premium

A succession policy for the company's key positions favouring external recruitment can help, in the short term, to create financial value by integrating the market's best talent (top manager), which may even result in some cases in a true competitive advantage (e.g. recruitment of one of the top designers in the luxury sector).

By comparison, the company opting for a **succession policy based mainly on internal mobility** and the enhancement of its human capital will strengthen its image as a company capable of developing and retaining its best employees, future top managers. This policy also leads to attracting new talent.

In both cases, investor confidence in the company's future can be ensured.

In summary, financial value creation, essential to business development, is the major factor of attraction for investors.

Based on the choices or directions, any HR policy can lead to the creation of financial value in the short or medium/long term by acting, depending on the case, on the various levers of revenue, operating costs, and economic risk premium.

An effective HR policy is one that can find a balance between short and long term, to create value and also to ensure that this value creation recurs over time. ■