

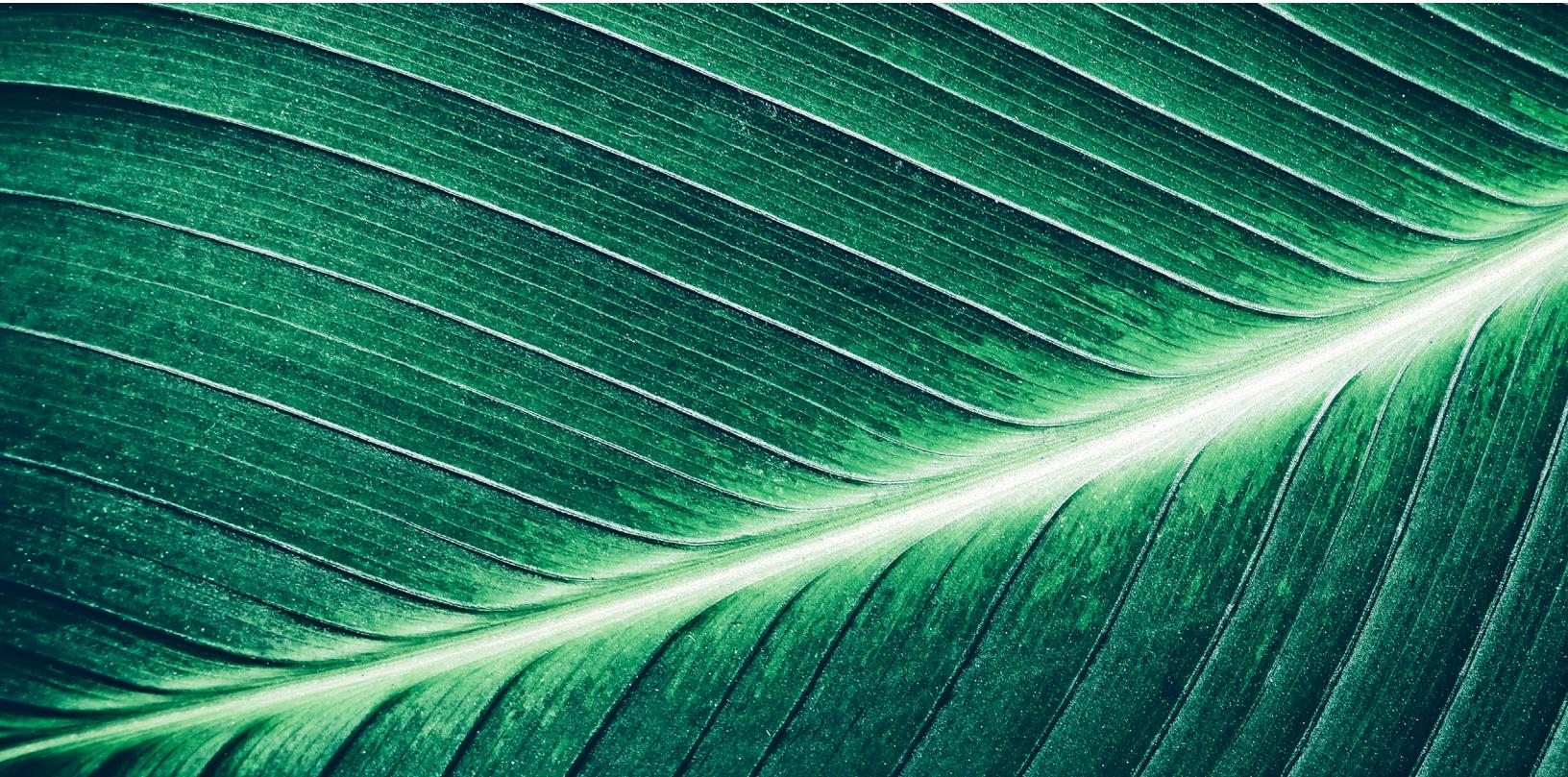


People & Organizational Performance Practice

HR's new operating model

Interviews with more than 100 chief human resources officers and people leaders reveal how the HR operating model is changing to drive value in a volatile business environment.

by Sandra Durth, Neel Gandhi, Asmus Komm, and Florian Pollner



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The way in which organizations manage people used to be relatively straightforward. For more than two decades, multinational companies generally adopted a combination of HR business partners, centers of excellence, and shared service centers, adjusting these three elements to fit each organization's unique nature and needs.

Today, this approach—introduced by Dave Ulrich in 1996¹—is rapidly evolving. In interviews with more than 100 chief human resources officers (CHROs) and senior people leaders from global multinational businesses, we identified five HR operating-model archetypes that are emerging in response to dramatic changes in business and in the world—including heightened geopolitical risks, hybrid working models, and the rise of majority-millennial workforces.

These emerging operating models have been facilitated by eight innovation shifts, with each archetype typically based on one major innovation shift and supported by a few minor ones. The key for leaders is to consciously select the most relevant of these innovation shifts to help them transition gradually toward their desired operating model.

Eight innovation shifts driving HR's new operating models

Today's increasingly volatile, uncertain, complex, and often ambiguous business environment is forcing companies to transform at an unprecedented pace. The global COVID-19 pandemic and rapid evolution of workplace technology have accelerated the adoption of various alternative, hybrid working models—as well as new challenges in monitoring employee conduct and performance. The emergence of majority-millennial workforces has led to a profound shift in employee preferences. And the “Great Attrition” of workers,² exacerbated by demographic developments in many parts of the world, has intensified existing talent shortages.

HR plays a central role in navigating this upheaval, creating a need for the function to rise to a new level of adaptability and responsibility.³ While every organization has its own trajectory and HR operating model, our interviews with senior leaders revealed that organizations are innovating in ways that are collectively changing the HR function from the “classic Ulrich model”:

1. *Adopt agile principles* to ensure both strict prioritization of HR's existing capacity and swift reallocation of resources when needed, enabling a fundamentally faster rate of change in the business and with people and how they work.
2. *Excel along the employee experience (EX) journey* to win the race for talent in the time of the Great Attrition,⁴ enabling both employee health and resilience.
3. *Re-empower frontline leaders in the business* to create human-centric interactions, reduce complexity, and put decision rights (back) where they belong.
4. *Offer individualized HR services* to address increasingly varied expectations of personalization.
5. *'Productize' HR services* to build fit-for-purpose offerings with the needs of the business in mind, and to enable end-to-end responsibility for those services through cross-functional product owner teams in HR.
6. *Integrate design and delivery with end-to-end accountability* to effectively address strategic HR priorities, reduce back-and-forth, and clarify ownership.
7. *Move from process excellence to data excellence* to tap into novel sources of decision

¹ David Ulrich, *Human Resources Champions: The Next Agenda for Adding Value and Delivering Results*, first edition, Boston, MA: Harvard Business Review Press, 1996.

² Aaron De Smet, Bonnie Dowling, Marino Mugayar-Baldocchi, and Bill Schaninger, “Great Attrition” or ‘Great Attraction’? The choice is yours,” *McKinsey Quarterly*, September 8, 2021.

³ Laura Blumenfeld, Neel Gandhi, Asmus Komm, and Florian Pollner, “Reimagining HR: Insights from people leaders,” McKinsey, March 1, 2022.

⁴ “‘Great Attrition’ or ‘Great Attraction’?”, September 8, 2021.

making using artificial intelligence and machine learning.

8. *Automate HR solutions* to drive efficiency and capitalize on the power of digitalization in HR.

These innovation shifts are driving the emergence of new HR operating models, albeit with different degrees of influence depending on the nature of individual organizations (Exhibit 1). In analyzing the drivers, we identified five HR operating archetypes.

Five emerging HR operating models

These eight innovation shifts have enabled companies to rethink how they manage their people and the best way to do so. Exhibit 2 shows the five emerging HR operating models we identified, which are all enabled by two core elements: a strong, consistent data backbone and a user-friendly, highly reliable service backbone. When asked which

two archetypes best fit their HR operating model, 48 percent of people leaders attending a recent webinar selected Ulrich+, 47 percent EX-driven, 36 percent leader-led, 31 percent agile, and 6 percent machine-powered.⁵

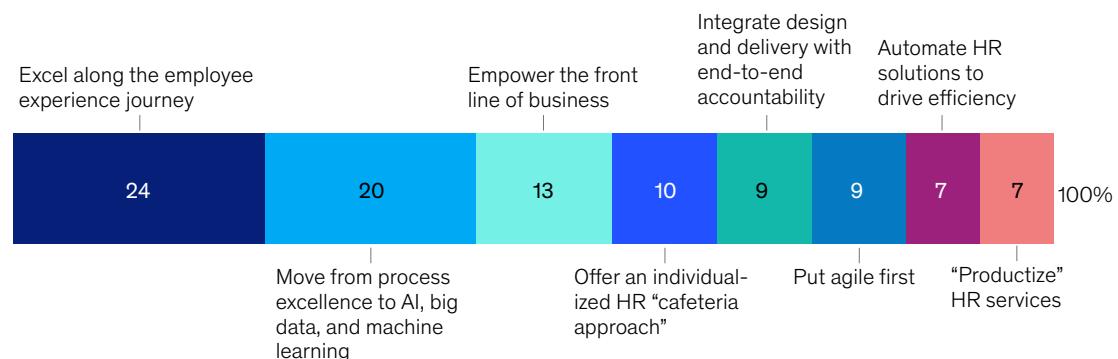
Ulrich+

This model is an adaptation of the classic Ulrich model, with HR business partners developing functional spikes and taking over execution responsibilities from centers of excellence (CoEs). In turn, CoEs are scaled down to become teams of experts and selected HR business partners. They are supported by global business services and have a digital operations backbone. Many CHROs believe the classic Ulrich model is not up to solving today's HR challenges, with HR business partners lacking the skills and time to keep up with the latest HR developments. Inflexible CoEs limit agile reactions, while other organizational boundaries have steadily become more permeable. Multinational businesses

Exhibit 1

HR leaders think excelling along the employee experience journey will have the most impact.

Which innovation shifts will have the most impact?, % (n = 128)



Note: Numbers may not sum to 100%, because of rounding.

Source: Reimagining HR Webinar Survey, McKinsey, November 2022, n = 128 HR leaders

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⁵ Reimagining HR Webinar Survey, McKinsey, November 2022, n = 140 senior people leaders. Figures do not sum to 100%, because of the possible selection of multiple answers.

Exhibit 2

There are five emerging HR operating models.

1 Ulrich+	2 Agile	3 EX ¹ -driven
<ul style="list-style-type: none">– Human resources business partners (HRBPs) develop functional spikes and take over execution responsibilities from centers of excellence (CoEs)– CoEs in headquarters (HQ) are scaled down and get support from virtual teams of top experts in HQ and from selected business partners– Business services are global and operations are digital	<ul style="list-style-type: none">– Number of HRBPs is reduced, with a focus on management advice and organizational development– Size and number of CoEs are reduced, with a focus on deep expertise and critical topics– End-to-end responsibility manifests in two ways:<ul style="list-style-type: none">• flow-to-work pools• task-to-team logic	<ul style="list-style-type: none">– HR function focuses on excellence in selected “moments that matter” along the EX¹ journey– All other HR activities are highly standardized– There is end-to-end responsibility for strategy, policy, and execution
4 Leader-led	5 Machine-powered	
<ul style="list-style-type: none">– People leadership tasks are transferred to line managers, including budget responsibility (eg, hire, onboard, and develop)– HR enables line managers with intelligence, HR tools, and services– Policies are minimized except for legal and compliance	<ul style="list-style-type: none">– HR focuses on high-touch interaction with employees, such as counsel and advice– Most HR decisions and processes (eg, training needs and assessment) are automated with AI-enabled tools– Reskilled and new AI or analytics experts exist within HR	

¹Employee experience.
Source: McKinsey analysis

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with mature and stable business models are often the ones that experience these pain points.

Agile

This model calls for a smaller number of HR business partners, with an emphasis on counseling top management, while CoE professionals focus on topics such as data and analytics, strategic workforce planning, and diversity and inclusion. The freed-up resources are pooled to implement cross-functional projects. CHROs who favor this operating model believe that HR needs to accelerate to keep up with the increased focus on execution exhibited on the business side and to prevent HR from hindering rapid transformation. Companies are applying this and other agile methodologies when experiencing rapid

growth or discontinuity. (For an example of this model, see sidebar “An agile transformation.”)

EX-driven

This model is meant to help CHROs gain a competitive advantage by creating a world-class EX journey. Putting EX first means allocating disproportionate resources toward “moments that matter.” For example, HR, IT, and operations experts could be granted full responsibility to jointly plan, develop, and roll out a critical onboarding process. By creating a world-class EX, HR becomes the driving force in bridging cross-functional silos and in overcoming the patchwork of fragmented data and processes that many organizations suffer from today. The companies

An agile transformation

A global financial institution underwent an agile transformation with a focus on IT delivery, supported by an agile HR operating model with 2,000 staff members. It first structured its HR function along the employee life cycle, aligning resources to the employee experience (EX) journey: when they join, work, develop, perform, and exit. The evolution to an agile model was supported by three HR innovation shifts:

- reducing the number of handovers by integrating run (servicing and operations) and change (product delivery) activities into “workstreams”
 - setting up workstreams with end-to-end service responsibility (for example, design and delivery of recruiting), common goals, and steering
 - allocating resources to agile pods with product crews for each workstream and agile ways of working
- Projects that cut across multiple product crews were supported with a center-of-excellence initiative manager at the divisional level, and the stream-by-stream transition plan was phased over two years.

employing this model are highly dependent on their top talent, with a small set of clearly defined competencies. (For more on this model, see sidebar “Optimizing the employee experience.”)

Leader-led

In this model, CHROs transition HR accountability to the business side, including for hiring, onboarding, and development budgets, thereby enabling line managers with HR tools and back-office support. This archetype also requires difficult choices about rigorously discontinuing HR policies that are not legally required. Too much oversight, slow response times, and a lack of business acumen in HR have led some companies to give line managers more autonomy in people decisions. Companies exploring this choice typically have a high share of white-collar workers, with a strong focus on research and development.

Machine-powered

With this model, algorithms are used to select talent, assess individual development needs, and analyze the root causes of absenteeism and attrition—leaving HR professionals free to provide employees with counsel and advice. As digitalization redefines every facet of business, including HR,

CHROs are looking for ways to harness the power of deep analytics, AI, and machine learning for better decision outcomes. Organizations that are experimenting with this are primarily those employing a large population of digital natives, but HR functions at all companies are challenged to build analytics expertise and reskill their workforce.

Innovation shifts shaping HR model archetypes

While innovation shifts have shaped the traditional HR operating model and led to the emergence of new archetypes, not all innovation shifts are equal. Each archetype is typically based on one major innovation shift and supported by a few minor ones (Exhibit 3).

For example, a leader-led archetype is mainly shaped by the shift of empowering the leaders and the front line. At the same time, it gives more flexibility to the needs of the individual (the “cafeteria approach”) because leaders have more freedom; it also builds on digital support so leaders are optimally equipped to play their HR role. Alternatively, an agile archetype is strongly focused on adapting agile principles in HR, but it typically

Optimizing the employee experience

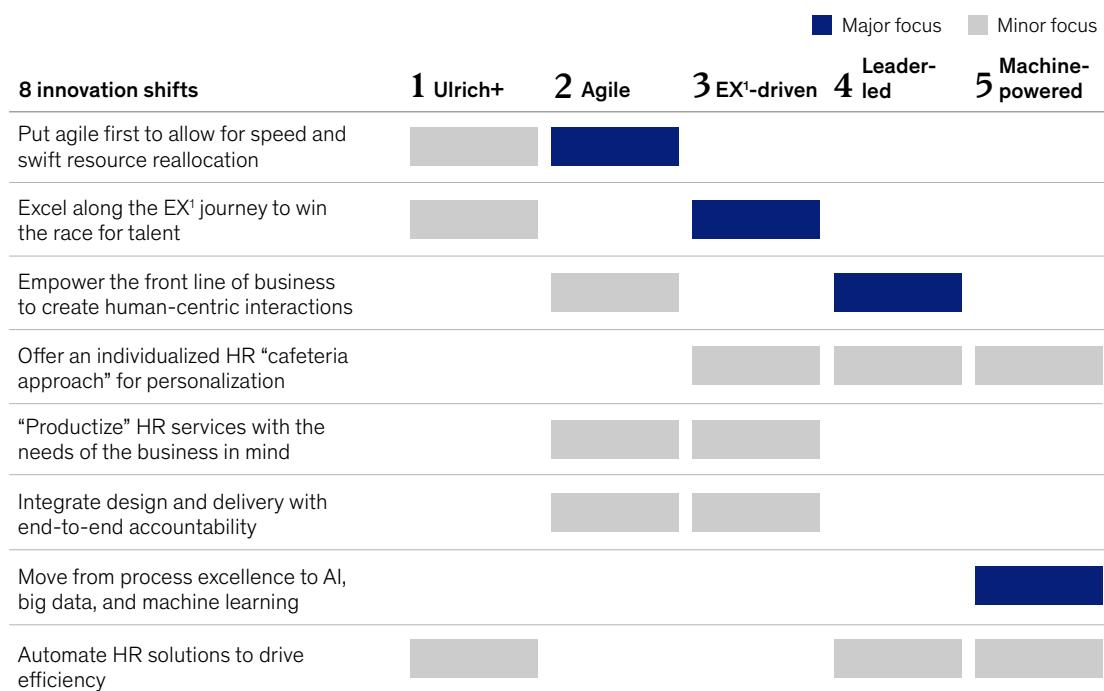
A global software company adopted a new business strategy to maximize the customer and employee experience, committing to a two-year transformation journey. Its first step was to mirror the customer experience for employees by identifying and revamping “moments that matter” along the employee life cycle. Three HR innovation shifts facilitated this: persona-driven HR services began following a customized approach; product owners took on end-to-end responsibility over HR concept, design, and delivery to deliver moments that matter; and HR, IT, and business operations combined into a comprehensive data function.

also aims to move toward a productized HR service offering and strives for end-to-end accountability.

The critical decision for senior people leaders is to consciously select the most relevant of these innovation shifts to transition gradually toward their desired operating-model archetype. For example, the leader-led model puts business leaders, rather than HR, in the driver’s seat, allowing line managers to choose the right HR offerings for their individual teams. And for companies that decide to deploy machine-powered HR, the key is building and relying on deep analytics skills. This model uses integrated people data to make targeted, automated HR decisions.

Exhibit 3

Different operating models are based on different innovation shifts.



¹Employee experience.
Source: McKinsey analysis

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In large, diversified organizations, CHROs may find that different archetypes fit the differentiated needs of specific businesses better and may adopt a combination of HR operating models.

Transitioning to a target operating model

Transitioning to a future-oriented archetype is typically a three-step journey. First, CHROs and their leadership teams align on the right operating-model archetype for their organization based on the most pressing business needs, expectations of the workforce, the wider organizational context, and the company's dominant core operating model. In large, diversified organizations, CHROs may find that different archetypes fit the differentiated needs of specific businesses better and may adopt a combination of HR operating models.

Second, HR leadership teams prioritize the three or four most relevant innovation shifts that will move their function toward their chosen operating-model archetype. When doing this, people leaders need to reflect on strategic HR priorities and, even more important, the shifts required to establish the operating model given its feasibility, the potential

limits to the speed of implementation, and the magnitude of change. (Today, we find that the capacity to change the HR information system is often the most limiting factor.) For example, if a company is operating in a traditional hierarchical "command and control" way, the sole shift of HR into an agile archetype requires profound and demanding changes to ways of working, likely beyond only HR. Similarly, a business accustomed to a "high touch, concierge service" HR approach will find that a shift to a leader-led archetype is challenging and requires significant effort to implement.

Finally, teams think comprehensively about the transition journey, working toward core milestones for each of the prioritized innovation shifts individually and ensuring a systemic, integrated transformation perspective at the same time. This requires mobilizing for selected shifts, building new capabilities, and acting on an integrated change agenda in concert across business and HR.

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