

STRATEGIC MANAGEMENT OF HUMAN CAPITAL IN THE ENERGY SECTOR

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INTRODUCTION

The energy sector appears poised for a period of global growth. At the same time, the industry faces challenges in meeting its demand for talent to take full advantage of the growth opportunities around the world.

Among the principal challenges facing energy organizations, two of the most well known are:

- An aging workforce, particularly in the highly skilled segment of the workforce. Recent studies, such as one completed by the Cambridge Energy Research Associates, estimate that more than half of engineers employed by the industry will retire by 2015.¹
- A lack of talent in the human capital pipeline. The industry as a whole has "... failed to recruit or retain sufficient human capital to assure enough career employees will be available to meet requirements. ... Nor have energy companies been able to attract a new generation of energy workers ..."²

These industry-specific challenges are playing out against the backdrop of shortages among highly skilled talent in labor markets across the globe – shortages that persist even in face of widespread unemployment. As such, it is unlikely that the natural mechanisms for equilibrating labor markets – talent mobility and pay adjustments – will be sufficient to make these shortages quickly self-correct. Significant public and private impediments to talent mobility stubbornly remain. And with intense competition for highly skilled talent, nothing short of concerted action by governments, business organizations, universities and not-for-profit organizations will suffice to break through the talent logjam. That will take time.³

Given these pressures, organizations in the energy sector need to significantly enhance their approach to workforce management. Specifically, they need to become as *scientifically disciplined* and foresighted in managing the processes by which they find, access and develop their workforces as they are with the processes by which they secure, produce and deliver their energy products and services. This is not pie-in-the-sky musing about the future. It is already happening. As we will see later in this paper, the energy giant Saudi Aramco figured this out some years ago and has moved aggressively to bring a rigorous, quantitative discipline to managing and deploying its talent pipeline. Consistent with its engineering culture and embrace of "systems thinking," the organization uses a sophisticated, evidence-based approach to strategic workforce management and planning that helps identify and mitigate talent risks. If an organization as financially and institutionally strong as Saudi Aramco feels the need to do this, can others sit on the sidelines and leave their talent needs to chance?

An *evidence-based approach* to strategic workforce management and planning can help organizations address their current talent challenges and pre-empt future talent gaps. Specifically, it helps them:

- Anticipate future workforce requirements
- Measure, understand and manage the dynamics of the current and future workforce supply
- Prudently invest in building the capabilities they require
- Quickly adjust internal deployment of employees to minimize unproductive situations of excess supply and/or excess demand

¹ Source: Cambridge Energy Research Associates Study, 2007

² Source: Boyden Global Executive Search, 2011

³ A detailed discussion about the issue of global talent shortages and examples of multistakeholder collaboration to strengthen mobility as an instrument for closing talent gaps can be found in the World Economic Forum/Mercer report, *Talent Mobility Good Practices: Collaboration at the Core of Driving Economic Growth*, Geneva: World Economic Forum, January 2012.

Put another way, this approach enables organizations to better navigate the external labor markets with which they interact and to help manage their own “internal labor markets” (ILMs) to shape their workforces to their business needs.

This paper explores some of the core components of evidence-based management of human capital. It shows how specific analytical methods can be applied to both the demand and the supply sides of workforce management and planning and how the integration of qualitative and quantitative data – that is, perceptions *and* realities – can strengthen the fact base on which decisions are made. The case of Saudi Aramco is reviewed in depth as an example of how such an approach is being used effectively in the energy sector. Finally, we also review data from recently completed studies of employee engagement and current compensation and benefit trends and costs to show how such information can be tapped to strengthen decision making around talent. Our goal is to provide practical insight to help employers gain enduring competitive advantage in the global competition for talent in the energy sector.

MANAGING HUMAN CAPITAL IN TODAY’S ECONOMY

The key workforce imperatives faced by employers today include:

- Finding, securing and developing the *right* talent – now and in the future
- Motivating and engaging that workforce in a post economic crisis and increasingly multicultural world
- Optimizing labor costs

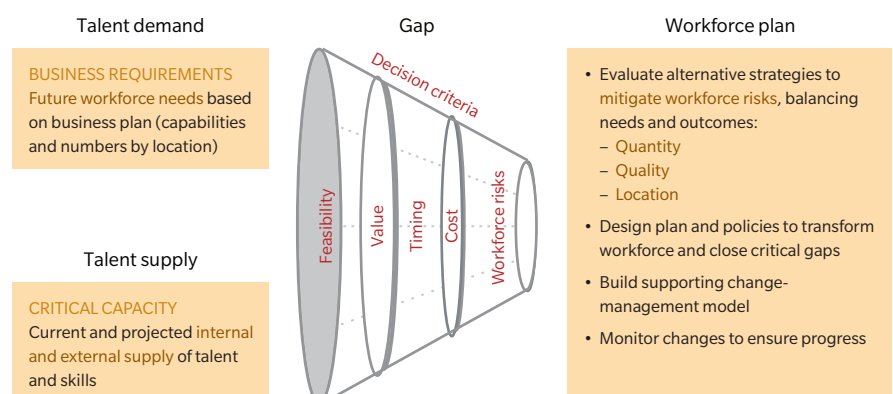
Since actual labor cost reflects both compensation expense and workforce productivity, effective cost management requires tracking and anticipating changes in compensation levels and trends in global labor markets as well as measuring and understanding what actually drives workforce productivity, including productivity differences across labor markets. In what follows, we discuss each of these imperatives in turn.

EVIDENCE-BASED STRATEGIC WORKFORCE MANAGEMENT AND PLANNING

The first and primary charge of workforce management is to help ensure that the organization has the talent required to support business objectives. As in all market-related activities, the problem has both demand and supply dimensions. Future demand and supply need to be estimated and gaps between them quantified. That knowledge can then be used to create a realistic plan that appropriately balances the quantity, quality, mix and location of critical talent to deliver the required workforce at the right cost.

The hallmark of the new approach to strategic workforce management and planning is its heavy reliance on empirical evidence to support decision making. The empirical emphasis plays out for both the demand and the supply sides of the workforce planning exercise.

Figure 1
Workforce Planning Quantifies the Gap Between Talent Demand and Supply, Providing the Basis for the Development of an Effective Workforce Plan



LABOR DEMAND

Traditionally, the focus on the demand side was on determining the number of full-time employees in specific roles that were required to meet future business demand. That was what the old “manpower planning” was all about. But increasingly, the real challenge for workforce planning is gauging how and to what extent the quality and mix of workforce capabilities need to change to support business objectives. Evidence-based workforce planning offers a new, more systematic approach to answering these questions – one that combines qualitative and quantitative data to provide a more reliable basis for anticipating future needs.

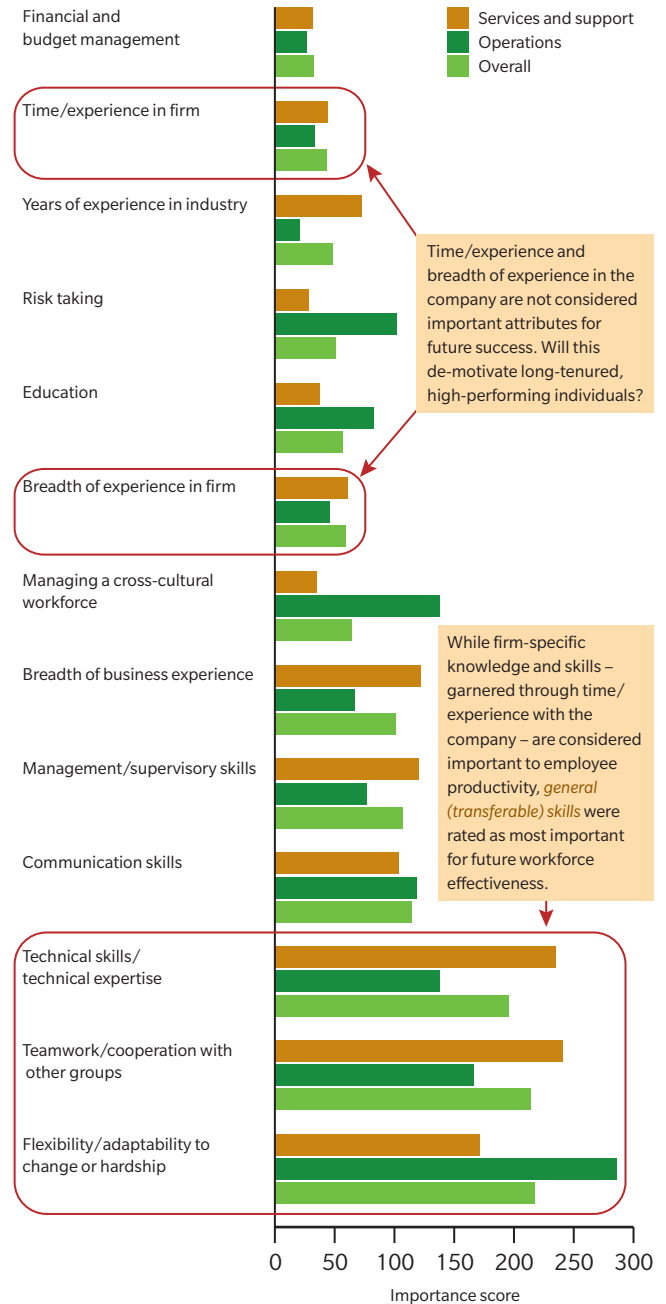
Since workforce planning is about the future, expert opinion about future workforce requirements is essential. More sophisticated tools for eliciting expert opinion, such as conjoint analysis, can now be used to help leaders – those with the best understanding of where the business is going and its key strategic differentiators – carefully think through the human capital implications of their business design. Specifically, leaders need to develop a workforce “blueprint” that spells out the mix of skills, knowledge and experience required as well as the workforce behaviors and attitudes needed to make the workforce productive.

For example, to help identify future workforce requirements, a large energy company used a formal survey process based on conjoint analysis to elicit input from business leaders and their HR partners across the segments. Specifically, they were asked to indicate which workforce characteristics and behaviors were most important to future business performance, selecting from among a group of paired comparisons offered in the survey. The company learned from this process that the more generic capabilities and behaviors – such as technical knowledge, teamwork and adaptability to change – were universally judged to be critical across all their business segments whereas firm-specific factors – such as employee tenure and breadth of experience in the company – were judged to be of little value. This was particularly striking given the strong orientation of the company’s current talent and reward strategies to the development and retention of firm-specific capabilities. It became evident that the current

talent and reward strategies were simply not geared to deliver what business and HR leaders believed they need to be successful. A serious talent risk had been identified.

Figure 2
Leaders in This Energy Company Rank General Skills and Behaviors – Including Technical Expertise, Teamwork and Cooperation – as Most Important to Future Company Success

Please indicate how important the following skills and experiences are for your workforce to be effective *in the future*.



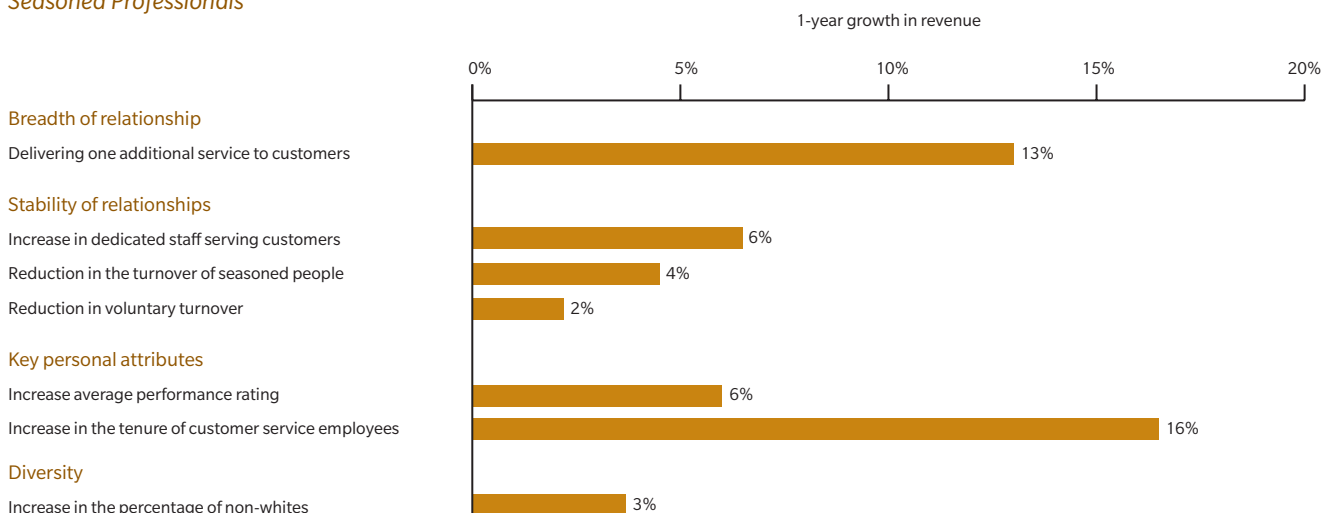
Sometimes opinion – even expert opinion – is not enough. *Believing* that a certain workforce attribute or capability is important is not the same as *knowing* it is important. In this highly competitive environment, those who *know* it will have the upper hand. In the best of worlds, organizations can go beyond opinion to tap into hard evidence about what workforce characteristics and behaviors actually matter to business performance.

A global professional services firm had the opportunity to examine the running record of revenue growth over multiple years to determine whether there were any clear indications of which workforce characteristics and management practices actually created the most value. Using controlled statistical modeling, the firm was able to discover linkages between growth in revenue and the way in which it structured sales and delivery teams.⁴ Among other things, the analysis uncovered that length of service of those in customer service roles was the single biggest driver of year-to-year growth. It dwarfed almost all other factors in its contribution to economic performance.

This result surprised business leaders, who tended to discount the value of employee tenure. If anything, they were biased against employee tenure, associating it with an entitlement mentality and resistance to change – the attitudinal enemies of a “performance culture.” The facts said otherwise, as they demonstrated, unmistakably, that the future workforce profile required more home-grown talent in customer-facing roles. Most important, they showed how much it was worth for the organization to invest in policies and practices designed to grow tenure in this part of its workforce. Quantification of the expected impact is what makes an evidence-based approach compelling. It provides an economic grounding to workforce management that has traditionally been absent in the workforce planning field.

Aside from assessing qualitative changes required in the workforce, effective workforce planning still must deliver reliable forecasts of how estimated future demand translates into future headcount requirements for relevant roles. From a headcount standpoint, increasingly sophisticated and agile

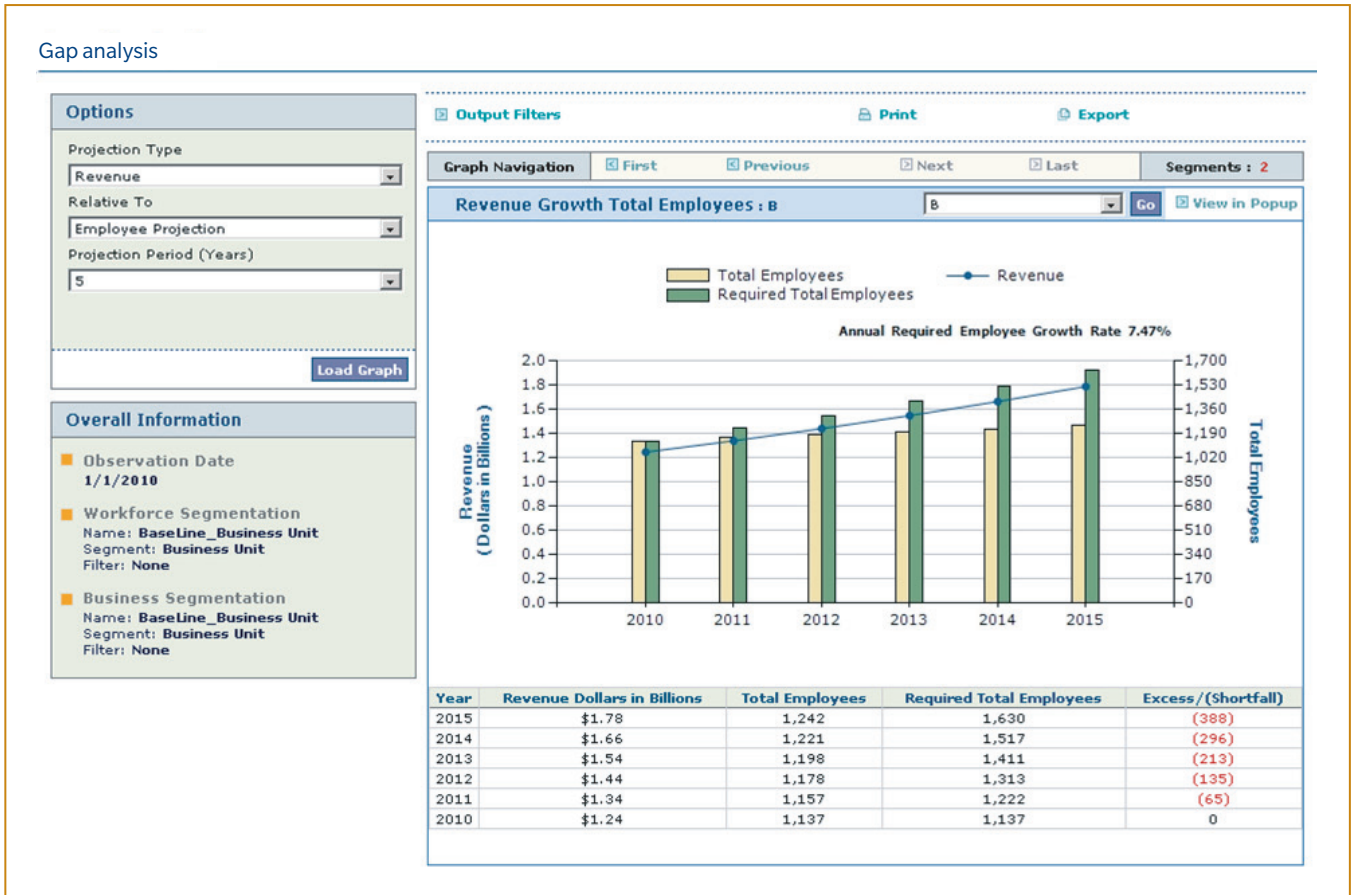
Figure 3
Evidence From Business Impact Modeling® Confirmed That Future Growth Depended on Cross-segment Teams Led by Seasoned Professionals



⁴ The specific methodology used by this organization is called Business Impact Modeling®. A detailed explanation of the approach can be found in chapter 6 of the following book: Nalbantian H, Guzzo R, Kieffer D and Doherty J. *Play to Your Strengths: Managing Your Internal Labor Markets for Lasting Competitive Advantage*, New York: McGraw Hill, 2004.

Figure 4

Given Current Trends, This Business Will Have a Shortfall of Employees by 2015 – Results From ILM Analysis® Could Help Determine the Most Effective Way to Close the Gaps



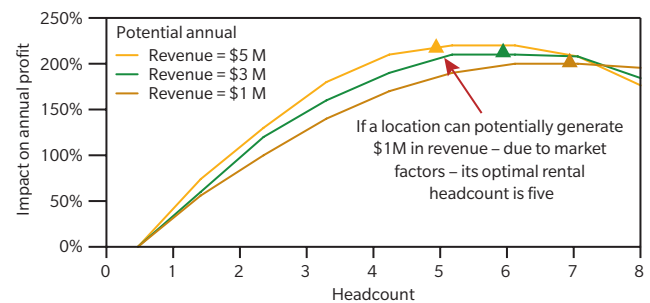
forecasting tools enable organizations to project headcount requirements under various scenarios. The default may simply be projections from the current baseline relationship between labor and output, assuming workforce productivity remains constant. Other scenarios may take into account likely changes in workforce productivity over certain periods and may also allow for altering assumptions about future turnover or absence rates – factors that could also affect what the optimal headcount will be.

But even here, application of more sophisticated workforce analytics can enhance the quality of decisions. It is possible in some circumstances to forecast headcount and staffing mix requirements based on hard evidence about what is optimal under alternative scenarios. Take, for instance, the case of a US equipment rental company under strong pressure to reduce headcount to lower its labor

costs. The company’s leaders decided they needed something better than reliance on conventional wisdom. They needed to follow the evidence trail.

Figure 5
For Rental Company, the Optimal Headcount Increases With Potential Revenue

For each level of potential business, a trajectory shows the impact of headcount on annual profit



Given their potential, some locations have headcounts that exceed the optimum, and others have headcounts that are smaller – growth prospects can be best enhanced by reducing headcount in the former set of locations and increasing it in the latter.

Potential revenue predicted from a supplementary model that controls for the number of households and business establishments in area.

Using sophisticated statistical modeling methods, they examined the running record of profitability across all their locations to identify optimal headcount conditional on other internal and external market factors also affecting profitability. The external factors related to the characteristics of customers in each market and the extent of competition from rival firms – factors that affect the “potential revenue” available to local operations. The statistical modeling identified the most efficient staffing models – relative to market opportunity – that were already operating within the organization. It revealed, in effect, what could be accomplished if internal best practices were replicated broadly across the firm.

The results showed that many of the units were operating with significantly larger headcount than necessary, and some were actually understaffed relative to what local markets could sustain. Indeed, revenue would grow significantly in some markets if headcounts were increased, and it would do so more than enough to offset the higher costs from the higher headcount. Management immediately used this information to inform its new staffing model. Moreover, these modeling results could be used to forecast future headcount requirements based on projected changes in potential revenue in current and prospective locations. Optimization based on hard evidence of this kind provides a powerful platform for more reliable and effective workforce planning.

LABOR SUPPLY

The same empirical approach can be applied to questions about labor supply. The proliferation of workforce data both inside and outside of organizations along with advances in modeling capabilities makes possible powerful quantitative assessments of labor supply and effectiveness.

Evaluating External Labor Markets

Obviously, effective workforce planning cannot take place without careful assessment of the current and future availability and quality of the kinds of highly skilled talent required by the business. The progressive integration of labor markets across the globe has increased the overall stock of talent available to organizations, but it has also rendered the process of talent searching more

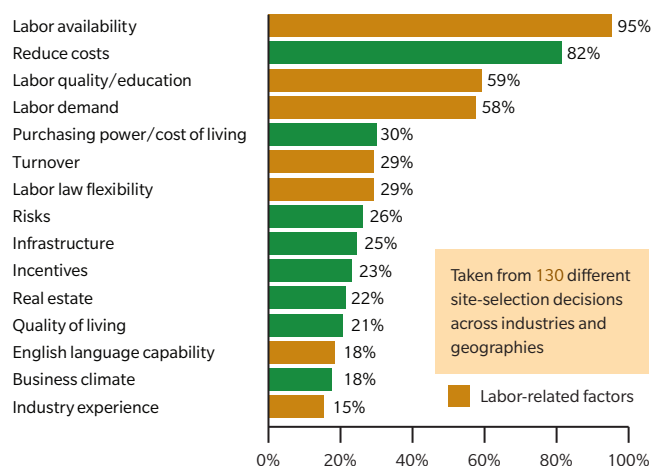
complex and competitive. The complexity rises because decisions about the sourcing of talent require the evaluation of numerous labor markets that exhibit different demographics, educational standards, cultures, work rules, labor unions and laws. And increasingly, it involves considering the potential to move jobs to where the talent is – that is, “job mobility” – rather than simply finding and moving the people to where the work is currently located – that is, “people mobility.” Organizations must constantly evaluate the economics of both sides of this talent equation.

For all the talk about a mobile global workforce, recent history shows that it is actually job mobility that has grown the most. An estimated 2 million jobs were created through foreign direct investment in 2010. In contrast, the World Economic Forum/Mercer survey of mobility patterns and practices suggests that mobility within firms has remained largely constant, with overall mobility limited to a small fraction of organizations’ workforces and traditional geographic mobility remaining the predominant form of movement.⁵ Multiskilling, job rotations and moving people across job families and roles as a means to close talent gaps remain underutilized.

Interestingly, Mercer’s extensive site-selection work with large global organizations has revealed that labor factors increasingly dominate location decisions.

Figure 6
Labor Availability Is the Most Common Criterion in This Sample of Site-Selection Decisions

Frequency criteria appears in location decision making



⁵ See *Talent Mobility Good Practices: Collaboration at the Core of Driving Economic Growth*, Geneva: World Economic Forum, January 2012.

Specifically, labor availability trumps all other factors, including cost, as a prime consideration behind location choice. And near the top of the list as well are considerations of labor quality (as measured by education) and labor demand (quantified by the level of competition for experienced workers or by wage growth and turnover).

Besides labor availability, these additional factors receive the highest weights assigned, on average, in site-selection decisions. Only cost competitiveness tends to be weighted higher.

These trends may pose a greater challenge to energy companies, particularly producers, than to employers in many other sectors. Because the core jobs themselves are tied to where the energy resources are located, energy companies may not avail themselves as readily of the kind of job mobility that helps other industries address their talent shortages. Reliance on such alternatives may be limited to support functions and other managerial or professional positions that do not require direct proximity to exploration and production employees. For most other jobs, the focus has to be on 1) improving access to talent available at or near the production site(s), 2) finding ways to effectively compete for the requisite talent at work in other geographies with significant energy sectors or 3) investing in broader industry or country-wide education and training efforts to develop new talent with the relevant skills.

Clearly these kinds of efforts are happening in the energy sector. Reliance on expatriate labor is high, as is investment in education and development. Migration of talent has become almost universally eastward, with competition for talent in the sector strongest in parts of Asia, Latin America and Canada – a decided shift from the pattern just five years ago.

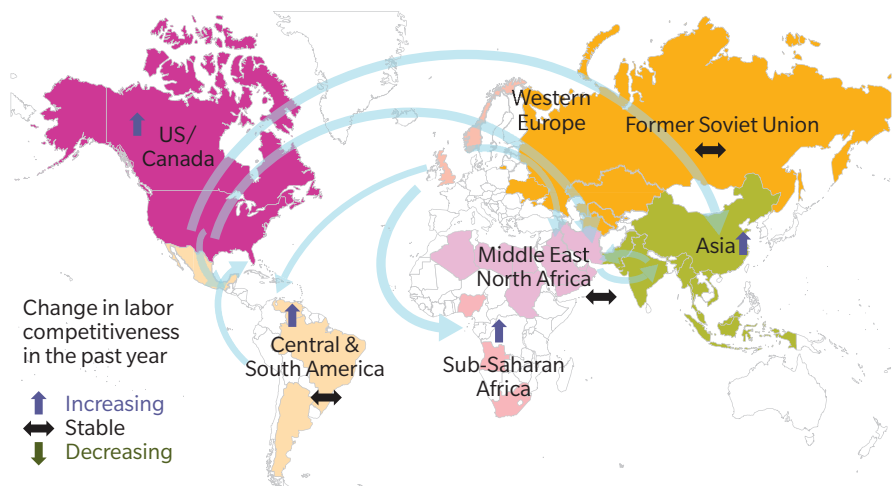
Given the global nature of talent sourcing in the sector, energy companies need to avail themselves of more readily available data on talent pools and on competitor activity in relevant labor markets around the world to identify where the right talent can be found. Careful prioritization with business and operational leaders of the relative importance of various labor factors can provide a more objective way to determine which markets to focus on and how to balance people and job mobility.

Figure 7
Trends in Talent Migration in the Oil and Gas Sector Back in 2007



Source: Mercer Oil & Gas External Labor Market Analysis, September 2007 update

Figure 8
Trends in Talent Migration – More Recently



Source: Mercer Oil & Gas External Labor Market Analysis, May 2010 update

Decisions about expanding the geographic reach of talent search are contingent on a proper understanding of the economic realities of labor markets at home. One of the large energy companies in the Middle East meticulously scans its home labor market to gauge the proportion of the overall pool of younger workers that is practically available to the firm. It takes into account such factors as how well those in the target demographics match up against key employment criteria, how many of them are projected to apply, the estimated attrition rate of candidates during the recruitment process, and the likely offer and acceptance rates, among other things. In this way, the organization gets a real handle on the effective talent pool in its home market and creates an empirical basis to optimize its recruitment, selection and development practices.

UNDERSTANDING YOUR ILM

Perhaps the most compelling advance in workforce analytics related to the supply side concerns methods that can be used to understand the dynamics of those all-important labor markets that reside inside organizations – that is, ILMs.

An organization’s workforce is determined not only by the availability and quality of talent in labor markets with which they interact, but, even more important, by how the organization manages its own ILM. Organizations do, in fact, run labor markets of sorts. They draw people in from the

outside. They move them through various assignments, jobs, locations and career levels. They keep some and lose some through voluntary and involuntary turnover. And they reward people in various ways – in the process, implicitly valuing the host of skills, abilities, experience, behaviors and attitudes displayed by employees across time. Rather than accomplishing these things through arm’s length transactions of the kind of characteristic of external labor markets, they rely on administrative processes and procedures inside the firm. Nonetheless, these are fundamentally market transactions and they accomplish the same things that external labor markets do:

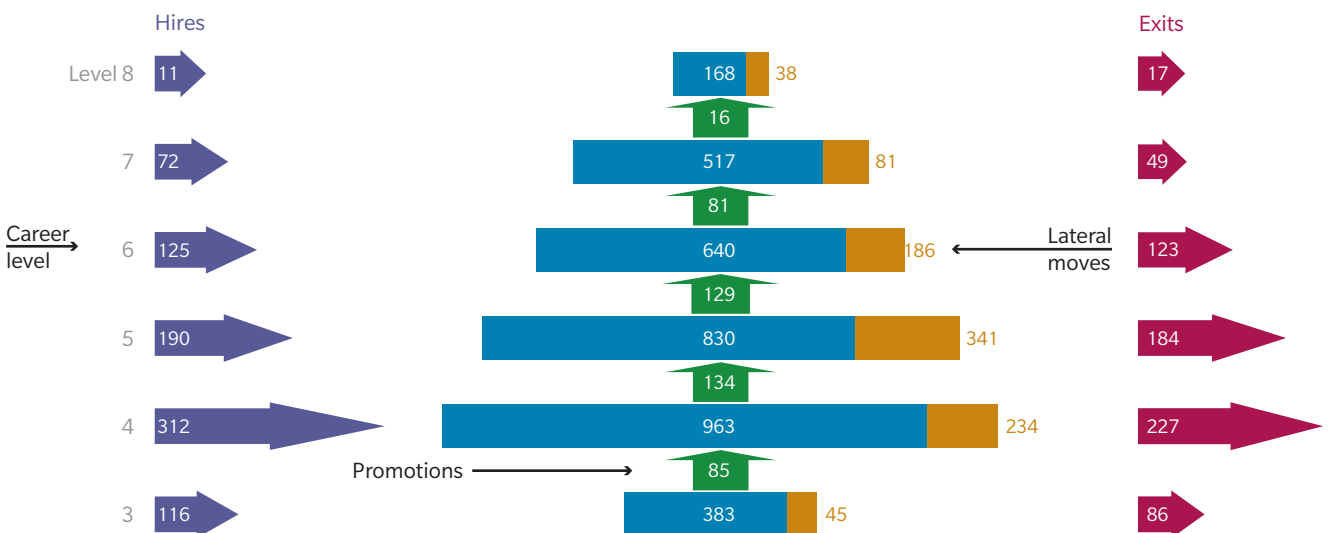
- Match people to jobs
- Motivate effort and diligence to perform those jobs
- Price those jobs

How well an organization manages its ILM affects the kind of workforce it has today and the workforce it will have in the future. Hence, it is incumbent upon the organization to measure and understand the dynamics of its ILM to be able to shape the workforce outcomes to its business needs.

In order to understand your ILM, you should start by mapping the flows of talent in, through and out of the organization over time. The following ILM map is a simple way to capture the core talent flows over a specified period, usually three to five years.

Figure 9
ILM Map

An organization’s workforce is the outcome of these highly inter-related labor “flows” and associated rewards



Each of the bars in this chart depicts average annual headcount in the various career levels that define the organization's hierarchy. Usually these are defined to capture significant career events, such that transitions between them represent a meaningful change in authority, responsibility, job scope, impact on the business and, yes, pay. Arrows in from the left show the average annual numbers of new hires into each level; arrows out to the right represent average annual exits, which can be further broken down into voluntary and involuntary turnover. The arrows between levels reflect average annual numbers of promotions. Finally, the map also displays the average number of lateral moves per year – job changes that do not involve promotion.

These are the core talent flows that characterize the organization's ILM. They determine who comprises the workforce and what it is becoming. The flows depicted in the map are purely descriptive but nonetheless can be revealing about the nature of the organization's talent strategy – for instance, whether an organization is prone to build or buy its talent, or whether it is hierarchical or flat in career structure, among other things.

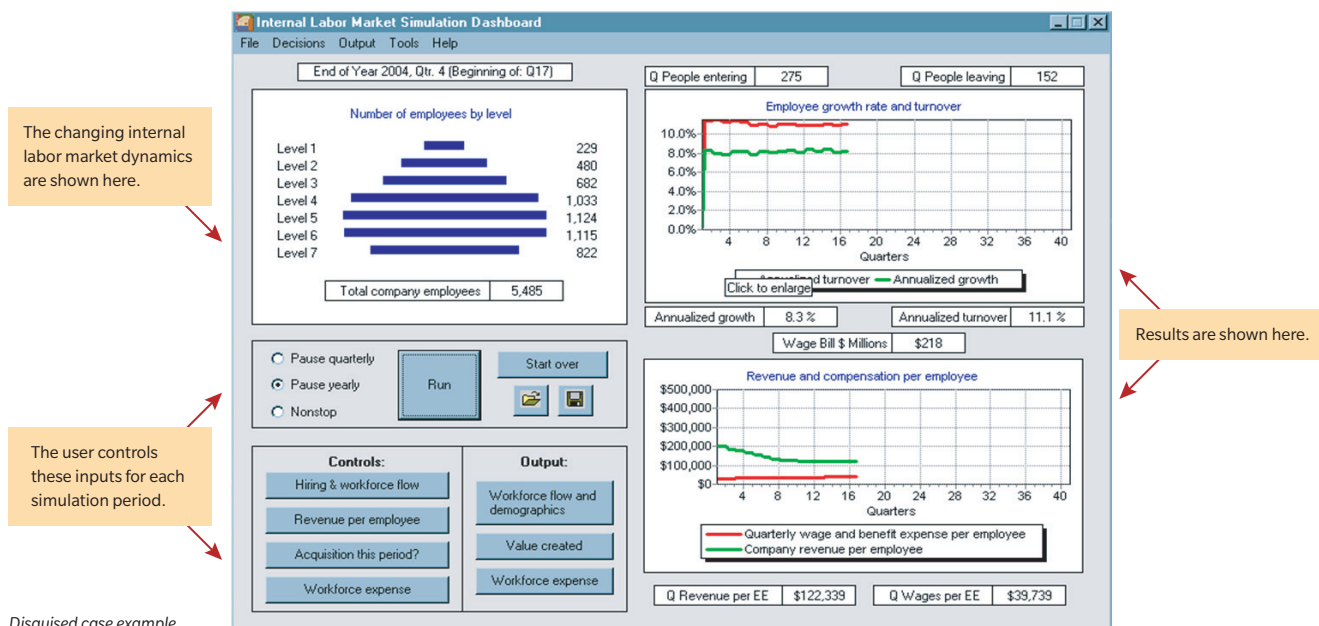
Beyond providing such high-level insights into the nature of talent management in the organization, these talent flows can be used to project, for planning purposes, what the organization's workforce will look like in the future. Such forecasts can help determine the likely distribution of employees across levels and the cost implications of changes in that distribution going forward.

And they can speak to other areas of concern, such as the future demographic makeup of management and leadership, with an eye toward meeting diversity targets.

MOVING FROM DESCRIBING TO EXPLAINING

Being able to manage your ILM requires more than simply describing it. From planning and management standpoints, the real power comes from learning *why* your ILM looks the way it does and how your policy actions can actually change the outcomes, particularly those outcomes that do not align with business needs. Statistical modeling of the drivers of each of these talent flows and associated rewards – what we call ILM Analysis® – can provide an empirical understanding of how your ILM is functioning and what you can do to ensure that you deliver what the business requires.⁶

Figure 10
The Information From an ILM Can Be Used to Develop a "Simulator" to Play Out Future Workforce Scenarios



Disguised case example

⁶ ILM Analysis® is a long-standing, proven approach to modeling and interpreting ILM dynamics. It consists of a set of integrated statistical models of the drivers of such key workforce outcomes as attraction, retention, promotion, ratings and pay. For a more detailed presentation of this methodology, see chapter 5 in the following: Nalbantian H, Guzzo R, Kieffer D and Doherty J. *Play to Your Strengths: Managing Your Internal Labor Markets for Lasting Competitive Advantage*, New York: McGraw Hill, 2004.

Beyond the simple descriptions revealed by an ILM map, for workforce planning purposes, you need to *know* a few core things about what *drives* your ILM:

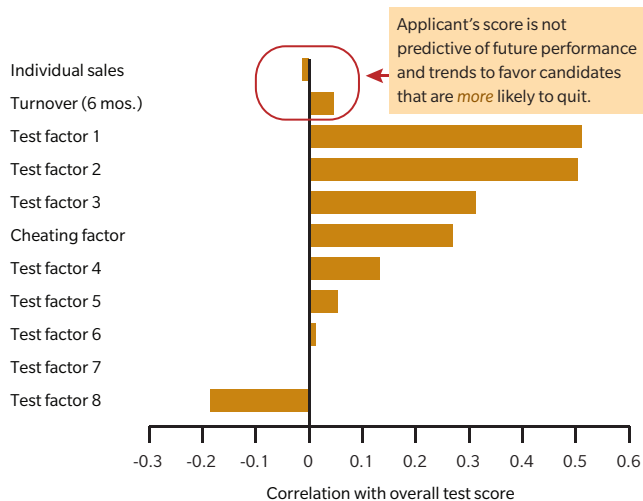
1. *Know* who you are attracting into the organization and whether they are the right people.

Understand who tends to be coming into your organization – both the people’s backgrounds and experience and from what sources they are coming from – and what happens to them over time. Is your target population actually performing better than comparable employees, as judged by ratings or measured productivity? Do they advance faster? Are their pay raises or bonus payments larger? Are they more likely to stay with you longer than others?

As an example, one sales organization discovered that those who performed better on the tests they used to screen candidates performed no better than those with lower scores and, in fact, were more likely to leave. Interestingly, some of the component factors of the test did, indeed, correlate well to future performance and retention, but the way they were aggregated into a composite score effectively nullified their predictive power. The evidence pointed most of all to a need to recalibrate the aggregate test score to get a more reliable selection-screening mechanism.

Figure 11
Know Who You Are Selecting ... and How They Fare

This selection instrument not only failed to be predictive of success, it also tended to select individuals with a higher propensity to quit.

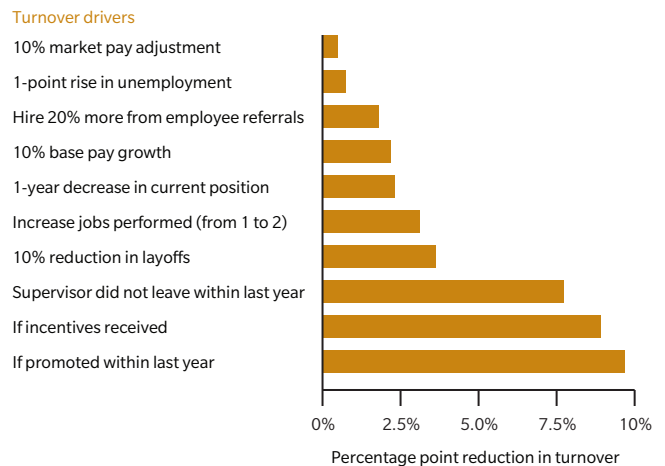


2. *Know* who are you retaining and why.

Identify who is leaving the organization and whether the pattern is aligned with business needs. Are top performers more likely to stay than average or low performers? Are the lower performers the most likely to leave? Are those with hot skills, technical expertise and/or leadership capabilities the most likely to stay? And what management practices most influence actual turnover? Do they play out differently for different workforce or business segments?

Figure 12
Know What Retains Employees ... and What They Actually Value

Analysis of actual turnover behavior



Previous surveys of perceptions suggested that pay and workload were most critical to employee commitment (in this organization).

Our analysis of actual behavior showed that career development and management stability most affected retention.

So, for instance, this services organization discovered that its high and soaring rates of turnover were driven by career-related factors – such as speed of promotion, frequency of job changes and managerial stability – and not nearly as much by pay and workload, the two suspected causes identified from exit interview data. Predictive modeling of actual turnover showed that strengthening career opportunities and reducing supervisor turnover would have, by far, the biggest effect in reducing turnover compared with any other interventions. And subsequent actions in these areas quickly proved the predictions to be accurate.⁷

⁷ A more detailed review of this example and the turnover modeling behind it can be found in Nalbantian H and Szostak A, “How Fleet Bank Fought Employee Flight,” *Harvard Business Review*, April 2004.

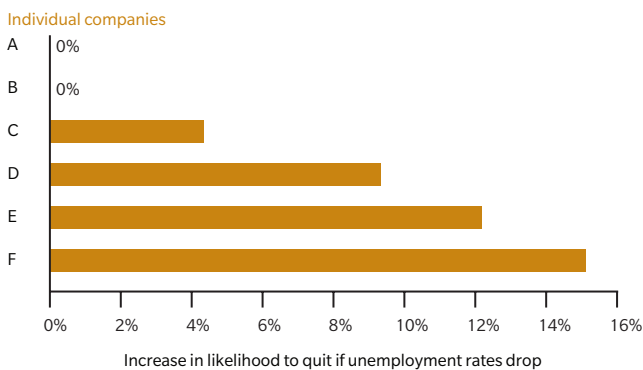
3. **Know** how vulnerable you are to changes in labor market conditions.

Understand how much of your unwanted turnover (or lack thereof) is directly attributable to changes in labor market conditions. Are you effectively insulated from outside market pressures or do small changes in outside conditions translate quickly into changes in turnover in your organization?

The following chart shows comparable results from predictive models of turnover likelihood estimated for six organizations.

Figure 13
Know How Susceptible You Are to Changing Labor Market Conditions ... and Whether Various Business or Workforce Segments Respond Differently to Outside Opportunity

Not all companies are equally affected by changes in unemployment rates



The bars indicate the estimated impact on voluntary turnover of their own employees of a change in local unemployment rates across their areas of operation, all else being equal statistically. The first two of these organizations have no sensitivity at all – what we call zero “elasticity.” Changes in labor market conditions, within the range of variance they experience, do not spur or diminish turnover among the workforce. In stark contrast, the firms toward the bottom of the chart show very high sensitivity to market conditions. They seem to be on a hair trigger: Even small reductions in local unemployment rates would significantly increase their turnover.

Why these differences? Some organizations manage to insulate their workforces from outside market forces, either through backloading of pay and benefits or by maintaining a premium reward proposition or employment brand. Others are more oriented to the “here and now” of markets; they don’t link pay and benefits significantly to tenure but are careful to meet current market rates. In such circumstances, any slowness to adjust pay or other rewards to market rates will, indeed, tend to result in higher turnover. There is little to deter employees from voting with their feet.

We are not suggesting that one of these profiles is inherently preferable to another. If instability in your workforce is a problem, and/or if you have high levels of unwanted turnover, greater insulation from the vicissitudes of the market might be desirable. On the other hand, if you need to change substantial parts of your workforce, and/or if your sector is so highly dynamic that you need to constantly import new ideas and the new talent that generates them, exposure to market influences can be a benefit to the business. Insulation from the market can block you from receiving market signals about how different workforce capabilities are being valued among other employers. Missing such information can make it more difficult for you to compete effectively in the future.

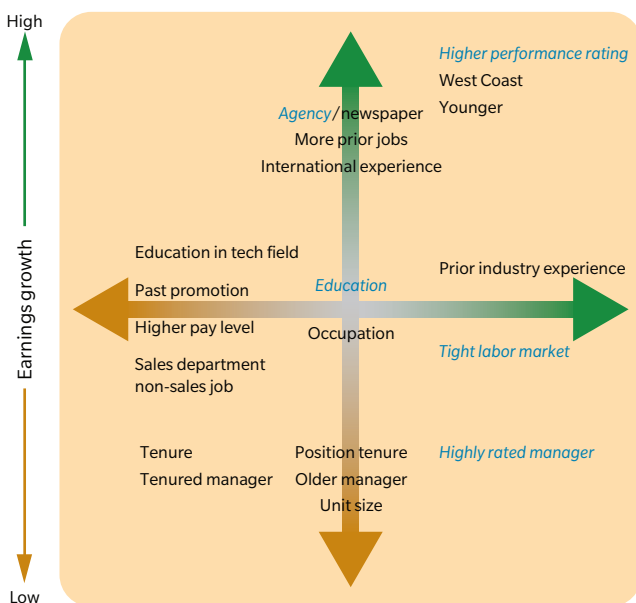
Whatever is the right profile for your organization, it is very useful to have this information. Indeed, it is hard to imagine how workforce planning can be effective without the capacity to forecast how anticipated changes in labor market conditions will likely affect turnover within your workforce. In a time of talent shortages and stiff competition for the best talent, guessing or using rules of thumb is not enough. Firm quantitative estimates based on hard evidence are what the top competitors will need to have.

4. **Know** what you are actually rewarding.

Understand what you actually value through your various rewards programs. Most organizations have an array of rewards they offer to employees – some related to pay, some to benefits and others to career opportunity, learning and the work environment. While almost all organizations know well what programs they have in place and what they intend to reward, few can look through the tangle of multiple rewards to see what, on balance, they collectively value – that is, what, in effect, determines who in the workforce gets higher levels of these rewards. Simply put, you need to know who does better in your organization. What are the attributes of those most likely to be promoted or of those who get the higher annual merit increases or annual bonuses?

The rewards grid is a practical visual of results from the statistical modeling of the drivers of three of the most tangible rewards: promotion likelihood, annual pay increases and pay level.

Figure 14
Know What Your Organization Actually Rewards ... and Whether Such Rewards Are Aligned With What Your Business Actually Needs



Factors in the upper-right corner, such as high performance rating or working in the company’s west coast operations, are associated, all else being equal, with a higher probability of promotion and larger pay raises. Factors on the lower-left corner are the opposite – they contribute negatively to those rewards. Factors in blue, such as higher performance ratings or educational attainment, are associated, all else being equal, with higher pay levels.

So, for instance, this organization was happy to find out that it strongly valued higher performers through all three elements of rewards. It was surprised to see how thoroughly tenure was devalued, even with respect to pay levels – something uncommon in similarly positioned enterprises. The biggest concern was the finding of how little higher education benefited employees once employed by the organization. Sure, these individuals had higher pay levels – a result of market realities. But once in the organization, those with higher degrees were no more likely to advance or see their pay grow rapidly than otherwise comparable employees without the degrees. For an organization developing an increasingly sophisticated business model with more complex products and more sophisticated production and sales processes, there seemed to be a fundamental misalignment of rewards with business requirements – one that brought with it a significant talent risk.

Why is this reward grid important? Because, as in all markets, prices matter. And rewards are the equivalent of prices in an ILM. Over time, you become what you reward. If length of service is a source of value, but your reward system ceases to value tenure, you are more likely to lose tenured workers and far less likely to encourage new hires to stay and build a career. If your business model requires a more educated workforce – as this organization believed – but you allow the market premium for those with higher degrees to erode once they are in your organization, you are more likely to lose those with higher degrees. And this will affect your ability to effectively compete for such talent in a world in which highly skilled talent is in big demand.

5. **Know** how careers unfold and what ways exist to effectively accelerate employee development.

Finally, organizations need to understand how their employees develop, both through formal education and training and through the process of job transition that drives their careers. Few organizations have a real handle on how these programs and practices actually play out within their workforces. Does formal education or training provide a real return to their investments? Do some types of programs work better than others in helping employees perform better and advance up or through the career ladder? And does the way people move from job to job affect how well they ultimately do in both performance and speed of advancement?

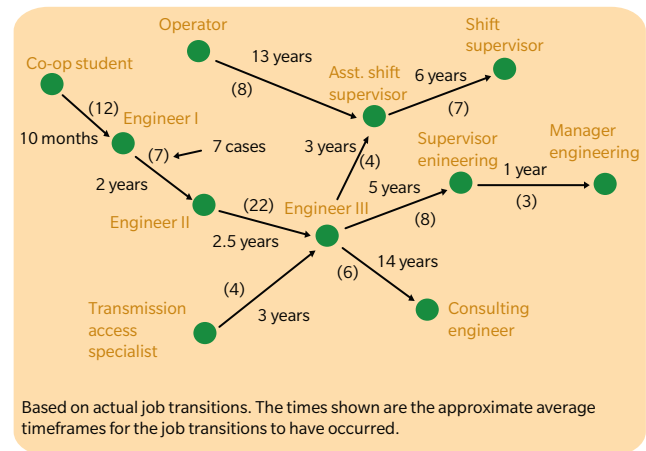
A leading energy company was concerned about future shortages of talent in its engineering ranks, particularly among some categories of engineers (for example, nuclear engineers), for which external supplies were clearly inadequate, largely because of insufficient attention in university curricula.

Leadership realized that the outside world offered no magic bullet that would fix this looming problem. The leaders needed to focus intently on the management of their ILM and develop solutions involving a combination of delaying anticipated retirements among the relevant populations, improving retention of talent in the pipeline and, related to that, accelerating development of the best among those same employees.

To support the latter, it helped to gain a better understanding of what the various development paths actually were and how long it typically took employees to pass through them. Career maps, such as the one depicted in Figure 15, helped leadership identify, for the first time, the multiple sequences of progression and transfer actually employed in the organization.

Figure 15
Know How Careers Unfold ... and Whether There Are Potential Ways to Accelerate Effective Development

An example of opportunity pathways in an energy company



This was the starting point for deeper dives aimed at determining what made some alternatives more successful than others and what conditions needed to be met in order to maximize the likelihood of more quickly producing engineers well qualified for the advanced roles they would need to assume. Without this understanding, workforce planning at this energy company could have become an exercise in futility, suggesting no economically viable and efficient ways to solve the talent problem. By understanding the internal development chain, the leaders were able to rely on changes in ILM management to close the gap.

BRINGING IT ALL TOGETHER

These are fundamental questions for workforce planning purposes. Once these answers are delivered and come together with a proper assessment of labor availability and quality on the outside, an organization can have a workforce plan that is tight, granular and fact-based – one that specifies practical actions you can take to improve workforce outcomes. Those with hard, tangible answers – not guesses – surely have the upper hand in the ongoing war for talent.

One of the best examples of evidenced-based workforce management and planning is that deployed by Saudi Aramco. In what follows, we review some of the core elements of its methods and practices.

EVIDENCED-BASED WORKFORCE MANAGEMENT AND PLANNING AT SAUDI ARAMCO⁷

Saudi Aramco is the largest oil and gas company in the world and the dominant economic power in Saudi Arabia. Managing proven reserves of 260 billion barrels of crude oil and the fourth-largest gas reserves in the world, Saudi Aramco and its affiliates operate joint ventures and subsidiaries in China, Japan, the Netherlands, the Republic of Korea, Malaysia, Singapore, the United Arab Emirates, the UK and the US.

The company relies on and plays a key role in developing the country's technical and leadership talent. Current and projected shortages of seasoned petroleum engineers and technical experts, combined with an anticipated increase in retirements, have increased pressure on the company to optimize its use and management of talent to prepare the next generation effectively and tap into new talent markets around the world.

WORKFORCE PLANNING – THE CORPORATE MANPOWER PLANNING MODEL (CMPM)

Saudi Aramco uses effective strategic workforce planning and development practices to maintain a steady flow of talent in the company and the Saudi economy at large through active collaboration with multiple stakeholders. Saudi Aramco recognized its need to firmly grasp the dynamics of both its ILM and the external markets from which it draws talent so it could properly respond to the uncertainties of a volatile industry. In response, Saudi Aramco developed and implemented a state-of-the-art strategic workforce planning methodology.

Encompassing the company's full-time workforce of nearly 55,000 employees, the planning model forecasts talent needs, anticipates gaps and identifies effective strategies to close those gaps. The company then uses this information to guide finely calibrated recruiting and mobility decisions.

This approach, which requires intricate collaboration across the various business functions, is helping the company secure a continuous supply of industrial and professional workers to fill specific jobs. "We take the CMPM projections seriously because they serve as a reliable guide for key workforce decisions, such as recruitment targets and development investments," said Samir Al-Tubayyeb, Vice President of Employee Relations and Training, Saudi Aramco.

TALENT DEVELOPMENT

Saudi Aramco makes massive investments in training and development, in excess of US\$10,000 per employee annually, sometimes beginning before employment and extending across an employee's career. For example, sponsoring employees and nonemployees in the pursuit of university degrees is a common practice. The focus is on leading Saudi universities and top-tier education institutions in the US, Europe, China, the Far East and Australia. Such investments help improve the quality of Saudi Aramco's workforce and help adapt employees' skills, knowledge and capabilities to the changing business needs of the company.

The investments support the company's participation in growing the local labor market and national economy – an important goal for this state-owned company. The company considers the value of learning not only to the firm itself, but also its impact on Saudi society at large. A vivid example is Ali Naimi, Minister of Petroleum and Minerals, a graduate of Saudi Aramco's apprentice training program. Similarly, there are many others who currently assume key positions in the Saudi public and private sectors who either are on loan or have retired from the company.

⁷ This case study is excerpted from the World Economic Forum/Mercer report, *Talent Mobility Good Practices: Collaboration at the Core of Driving Economic Growth*, Geneva: World Economic Forum, January 2012.

Saudi Aramco also engages in long-term collaborative partnerships with the government and key academic institutions to prepare the Saudi workforce for the competitive economy of the future. The company sponsors 11 chairs across Saudi universities. It collaborates with government institutions on vocational training covering a variety of engineering disciplines to ensure alignment of the academic curriculum of public schools and universities with Saudi Aramco's needs. It also provides subject-matter experts from its own oil and gas operations to teach courses in engineering, project management and business.

Saudi Aramco reaches down to the primary and secondary education levels. This is done through initiatives such as its popular Summer Student program, which draws nearly 2,000 students annually. This eight-week program provides students in the 10th and 11th grades and college students with interesting and challenging educational and work experiences to enhance their life skills and promote volunteerism and community values. The company uses the program to attract the best-performing students to the company and to encourage these students to apply for other work-study programs.

Out-of-company assignments are another key tool used to develop leadership and technical skills in the Saudi workforce. The company collaborates with its alliance partners throughout the world to place Saudi employees in their firms, exposing them to world-class practices and more diverse technology. Such assignments contribute a lot to internal mobility at all career levels to broaden experience, better match people to jobs, and strengthen engagement and motivation.

In addition to sending Saudis on international assignments, Saudi Aramco relies on seasoned professionals from around the world to come to the Kingdom and help with knowledge transfer on the latest technologies and management practices. About 12% of its workforce is non-Saudi, bringing experience in critical oil and gas skills, project management, construction, health care, finance, IT and HR. In managing this expatriate workforce,

Saudi Aramco is careful not to simply fill positions that cannot be filled by locals, but to ensure that expatriate professionals develop Saudis as well. "We make it clear to all expatriate employees that knowledge transfer is a key part of their job," said Al-Tubayyeb. "They are encouraged regularly and recognized for adhering to this strategy."

EVIDENCE-BASED METHODS FOR HUMAN CAPITAL MANAGEMENT

A critical element of the company's workforce planning and development practices is its strong adherence to evidence-based methods for measuring and monitoring the impact of human capital management practices. The company deploys sophisticated workforce metrics and analytics to optimize the return on HR investments and quickly adjust the investments to changing business needs. The system shows, by almost 400 job families, the number of fully qualified employees that each business line needs in each year going forward. The process allows leaders to test different alternatives for critical workforce gaps through redeployment, reskilling, recruitment of Saudis and expatriates or the use of contractors.

IMPACT

Saudi Aramco's workforce planning process is recognized internationally as one of the most sophisticated, far-reaching and reliable workforce planning models in use anywhere. Over the years, it has become pivotal to Saudi Aramco's staffing success. The CMPM elicits information from business lines on the level and mix of talent required to meet future needs. It also develops projections of internal and external supply. But it goes well beyond the norm in deploying sophisticated algorithms to show how the company's ILM can be equilibrated through shifts of talent from areas of excess supply to areas of excess demand.

The model helped the company manage its workforce in a time of surging demand and address concerns about its talent pipeline and a prospective retirement bulge. Through pre-emptive actions made possible by more precise forecasts of what drives early retirement and turnover generally, the anticipated spike in retirements and associated shortfalls in critical areas has not materialized.

Recent analysis suggests that the company is making highly efficient investments in training and education. Young Saudis who earn college degrees at the company’s expense under the careful preparation and support of the company, and return to work, tend to perform better than other employees over time, as measured by performance rating, career and pay progress. Comparisons of future pay trajectories show that it takes eight years for an employee who completes an advanced degree on the company’s expense to “catch up” with comparable employees who forgo that opportunity

and remain on the job. However, payoffs from higher education accrue over time as employees start to deliver value to the organization.

This is a textbook example of best practices for managing long-term investments in higher education. Similar positive returns are found with respect to overseas assignments, though this type of mobility comes with a relatively higher risk of talent loss. Using sophisticated workforce analytics, Saudi Aramco is able to spot the risk and take action to mitigate it.

Figure 16

Using ILM Analysis®, Saudi Aramco Was Able to Assess the Workforce Impact of Education and Overseas Assignments

	Promotion	Voluntary turnover	Normal retirement	Performance rating	Pay level	Pay growth
Master’s v s. bachelor’s degree	11%	No influence	No influence	3%	5%	No influence
Doctorate vs. bachelor’s degree	55%	No influence	-83%	No influence	10%	No influence
Ever did overseas assignment?	49%	41%	Not applicable	6%	-4%	.01%

KEY LEARNINGS

The overall success of Saudi Aramco’s approach to workforce planning and development is attributable to several factors:

- **Engagement and buy-in from senior leaders.** Workforce planning in the company is not an “HR thing” – it is a business priority and has the commitment of business leaders in each department. There is no ambiguity about the importance of workforce planning and employee development to the company’s success. It is perhaps significant that Saudi Aramco’s CEO, Khalid A. Al-Falih, was formerly the Chief HR Officer of the company and has a deep understanding of the critical role of talent in driving success – even in a natural resources company.
- **Scientific orientation and holistic thinking.** The company is, at its roots, an engineering-based organization that embraces technical know-how, systems thinking and fact-based approaches to problem solving. This makes it easy to deploy more scientific methods across the gamut of management activities in the organization.
- **Care in measuring the impact of talent mobility decisions.** The company is careful to not simply launch new programs, but instead to measure and understand the real impact of its talent practices and investments.
- **Leveraging its public standing in the industry, the country, the region and the world.** Saudi Aramco appreciates that its brand not only signifies financial strength, but also the propensity and ability to seek best-in-class solutions for all major business operations. Leadership actively deploys the power of its brand to secure productive partnerships with business and public institutions all over the world in ways that strengthen its own – and the country’s – workforce.

Saudi Aramco relies on rigorous workforce planning methods, substantial targeted investments in education and training, and expansive talent mobility programs that give its employees exposure to the management practices and tools used by other major firms around the world. By doing so, Saudi Aramco is ensuring not only that it has the workforce it needs to sustain its business, but also that the country has a competitive talent pool that will ensure growth for the society as a whole. Each of these mobility practices involves extensive collaboration across stakeholders within and outside the company. It is telling that an organization of such high standing that is endowed with extraordinary financial and human resources nonetheless recognizes that when it comes to talent mobility, collaboration delivers far better outcomes than doing it alone.

MOTIVATING AND ENGAGING THE WORKFORCE

Securing the right workforce is one thing. Engaging that workforce in a way that makes it productive, innovative and able to quickly adapt to changing market conditions is another matter entirely and certainly no less important to business success. Unfortunately, this has become an inordinately difficult task for almost all employers. Research shows that employee engagement took a hard hit during the financial crisis, with feelings of loyalty, commitment to the organization and trust in leadership dipping dramatically in many organizations. Changing this dynamic is no easy task and once again, there is a big payoff to organizations that operate from a strong base of evidence rather than relying on HR bromides, a gut feeling or a simple hope that the problem will go away. Getting the right facts about the state of engagement of your current and potential workforce and

what is most likely to strengthen it can help organizations get ahead of the curve and focus limited resources on what really matters to the employees they want to have.

A good place to start is reviewing some fresh data on what's inside employees' minds. The employer who has that knowledge can successfully engage the potential and current workforce and gain a competitive advantage in hiring and retaining scarce available talent.

UNDERSTANDING WHAT'S INSIDE EMPLOYEES' MINDS

Mercer's proprietary *What's Working*[™] survey, which examines employee views on work, was last conducted between the fourth quarter of 2010 and the second quarter of 2011 among nearly 30,000 workers in 17 markets worldwide. The survey includes more than 100 questions on a range of work-related topics and reflects the overall demographics of the workforce in each of the 17 markets in terms of age, gender and job level.

Not surprisingly, what is important to employees varies by geography and across generations. Mercer used conjoint analysis to determine a prioritized ranking for each of 13 key value propositions in each market.

GEOGRAPHIC VARIATIONS

Americas

In the Americas, five markets were surveyed:

- Argentina
- Brazil
- Canada
- Mexico
- US

In summary, the results revealed:

- Base pay ranks first or second in importance in all markets.
- Career advancement and training opportunities were highly emphasized in Latin America, but neither element ranks in the top six in Canada or the US.
- Canada and the US both rank having a retirement savings or pension plan as the second most important value proposition element.
- The type of work and bonus/other incentives factor highly in four out of five markets.
- Working for a respectable organization ranks the highest in Brazil and Canada.

Figure 17 provides a complete summary of the top six elements that employees value in each of the five markets in the Americas.

Figure 17
Most Important Value Proposition Elements: Americas

Rank	Argentina	Brazil	Canada	Mexico	USA
1	Career advancement	Career advancement	Base pay	Base pay	Base pay
2	Base pay	Base pay	Retirement savings or pension plan	Career advancement	Retirement savings or pension plan
3	Training opportunities	Training opportunities	Type of work	Training opportunities	Type of work
4	Type of work	Working for respectable organization	Working for respectable organization	Bonus/other incentives	Low health care costs
5	Health ins. with broad coverage	Type of work	Bonus/other incentives	Retirement savings or pension plan	Bonus/other incentives
6	Flexible work schedule	Bonus/other incentives	Flexible work schedule	Broad coverage medical ins.	Working for respectable organization

When energy-sector employers consider the labor market in the Americas with these results in mind, it is apparent that providing top-tier total remuneration, especially in North America, is critical for attraction and retention of talent, particularly for workers ages 50 and older.

Asia Pacific

In Asia Pacific, five markets were surveyed:

- Australia
- China
- Hong Kong
- India
- Singapore

The results of the conjoint analysis revealed:

- Base pay ranks first or second in importance in all markets.
- Bonus/other incentives ranks second in Hong Kong and Singapore and in the top six in the other three markets.
- Career advancement, type of work and training opportunities rate highly in four of the five markets.
- Australians value flexible work schedules more than workers in other markets.
- Paid time off ranks in the top six value propositions only in Hong Kong.

Figure 18 provides a complete summary of the top six elements in each of the five markets in Asia Pacific.

Figure 18
Most Important Value Proposition Elements: Asia Pacific

Rank	Australia	China	Hong Kong	India	Singapore
1	Base pay	Career advancement	Base pay	Career advancement	Base pay
2	Type of work	Base pay	Bonus/other incentives	Base pay	Bonus/other incentives
3	Flexible work schedule	Supplemental retirement savings plan	Career advancement	Training opportunities	Career advancement
4	Working for respectable organization	Training opportunities	Retirement savings or pension plan	Type of work	Type of work
5	Bonus/other incentives	Bonus/other incentives	Paid time off	Working for respectable organization	Flexible work schedule
6	Training opportunities	Supplemental medical ins. coverage	Type of work	Bonus/other incentives	Training opportunities

As employers seek to gain a competitive advantage for talent in this growing geographic region for the energy industry, the value proposition offered to employees beyond pay should be emphasized in order to achieve a high level of employee engagement.

Europe

In Europe, seven markets were surveyed:

- France
- Germany
- Ireland
- Italy
- Netherlands
- Spain
- UK

The results of the conjoint analysis revealed:

- Base pay ranks first in importance in all seven markets.
- Type of work ranks second in six markets.
- Bonus/other incentives ranks in the top six in five markets.
- Other highly valued elements of the deal are:
 - Career advancement
 - Training opportunities
 - Retirement or supplemental retirement plan.

Figure 19 provides a complete summary of the top six elements in each of the seven markets in Europe.

Figure 19
Most Important Value Proposition Elements: Europe

Rank	France	Germany	Ireland	Italy	Netherlands	Spain	UK
1	Base pay	Base pay	Base pay	Base pay	Base pay	Base pay	Base pay
2	Type of work	Type of work	Job security	Type of work	Type of work	Type of work	Type of work
3	Bonus/other incentives	Bonus/other incentives	Type of work	Career advancement	Retirement savings or pension plan	Flexible work schedule	Bonus/other incentives
4	Career advancement	Flexible work schedule	Good workspace	Bonus/other incentives	Working for respectable organization	Training opportunities	Retirement savings or pension plan
5	Supplemental retirement savings plan	Working for respectable organization	Career advancement	Retirement savings or pension plan	Paid time off	Career advancement	Flexible work schedule
6	Private medical insurance	Training opportunities	Bonus/other incentives	Training opportunities	Training opportunities	Paid time off	Paid time off

The implications of the European results when applied to the energy industry are twofold. Emphasis should be placed on the base pay portion of the total remuneration package, and providing a positive “work experience” is critical, especially for the younger portion of the workforce (which places a premium on satisfaction with their actual job).

GENERATIONAL VARIATIONS

The Paradox of the Millennials

While differences in the survey results by age group were seen in every one of the 17 markets, compared with the overall workforce in each market the youngest groups of workers (ages 16–24 and 25–34) are:

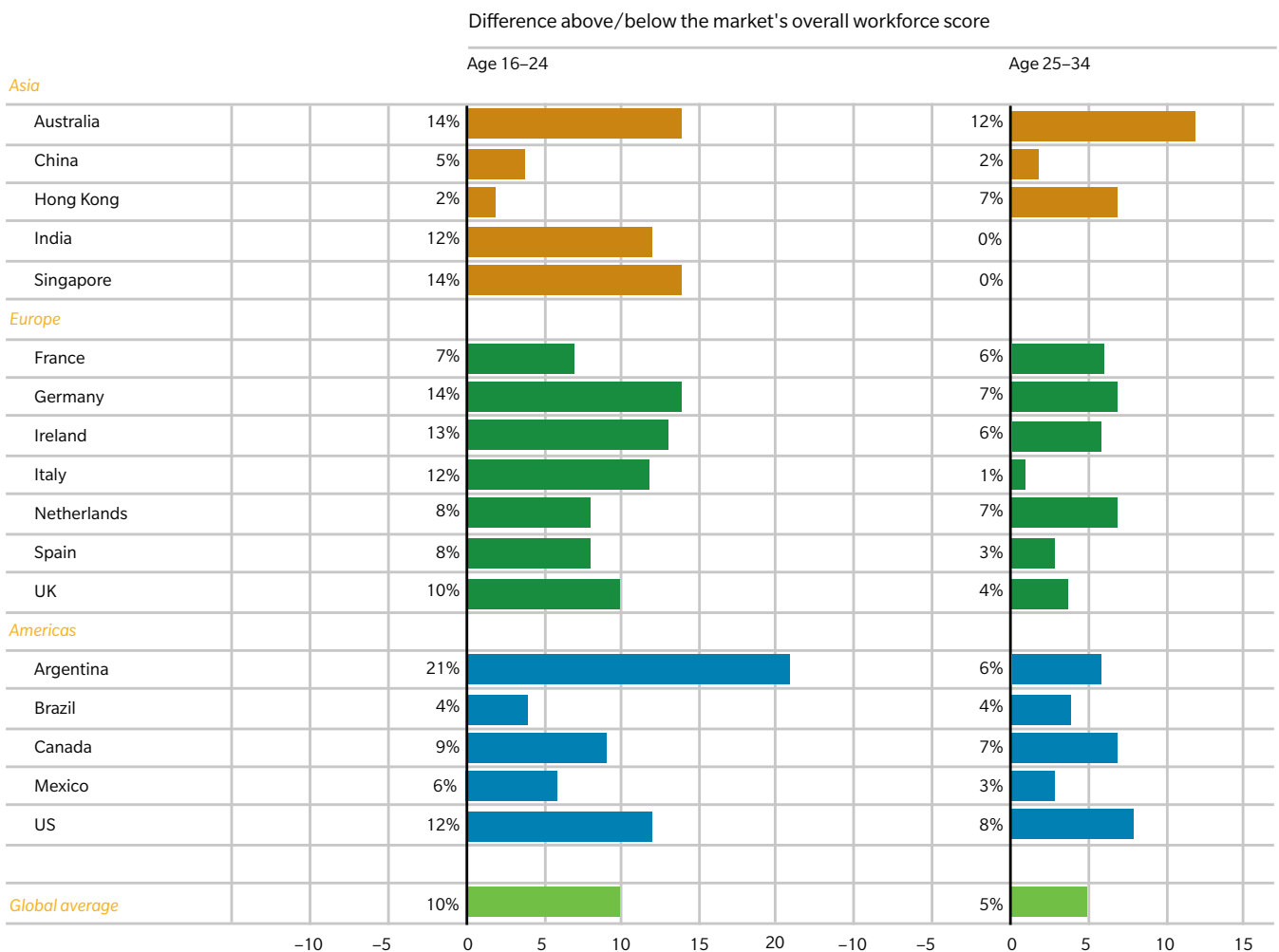
- More satisfied with their organizations
- More satisfied with their jobs
- More likely to recommend their organization as a good place to work
- Much more likely to be seriously considering leaving their organizations at the present time

Figure 20 provides a summary of this paradox, by market.

The dilemma for energy employers is to either accept the current situation (younger workers satisfied yet more likely to leave than the workforce at large) as *fait accompli* or try to change the perspective and employment habits of younger workers. Employers have a significant upfront investment in new employees in terms of onboarding, training and development. It is thus clearly in the organization's best interest to amortize these front-loaded costs over a reasonable period and not lose talent and investments to a competitor.

While the answer to the problem will vary by organization, it is essential for each to understand its own unique value equation and whether a business case can be made for taking steps to retain and extend the tenure of young workers.

Figure 20
At the Present Time, I Am Seriously Considering Leaving My Organization



*Youngest Workers Have More in Common
Across Borders*

Mercer's research also shows that 16–24-year-olds are the only age group more likely to think and act like their age-group peers around the world. All other ages are more likely to think and act within the established cultural norms of their country. This important distinction was not seen in previous Mercer *What's Working* survey data.

As energy employers increasingly move toward a globally mobile workforce, the organization that understands both the values and the mindset of its current and prospective employees, including recognizing the variations by age group, should enable modification or development of compensation and career development programs that will maximize the return on investment in human capital.



A FOCUS ON TOTAL REMUNERATION

While there are some distinctions by market, region and age group, it is not surprising that total remuneration (base pay, variable bonuses and benefits) ranks high around the world and across all age groups. Because typical mixes of remuneration packages vary widely by region, energy companies wishing to gain a competitive advantage should avoid a “one size fits all” approach to creating the right mix of remuneration elements.

Every year, Mercer takes a detailed look at compensation and benefit plans around the world. The 2011 study looked at close to 50 countries.

COMPENSATION PLANS AROUND THE WORLD

The compensation study examined the mix of total remuneration for two broad categories of employees – professional and management. The compensation results for all the countries studied were grouped into four regions:

- Americas
- Asia Pacific
- Eastern Europe, Middle East and Africa
- Western Europe

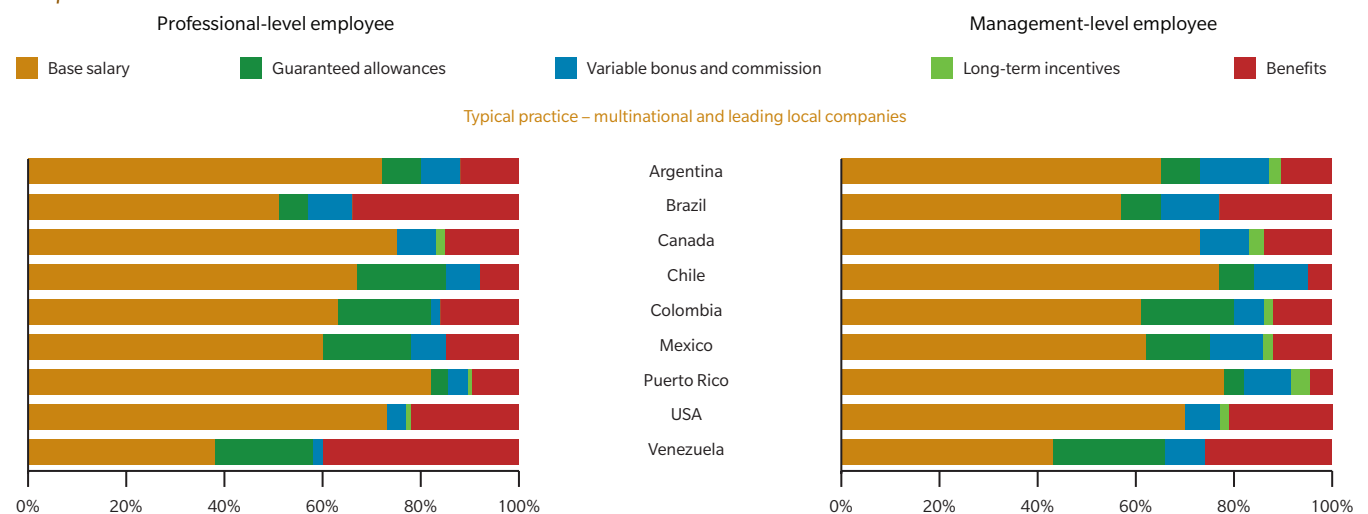
The results by region, with the understanding of what is inside employees’ minds in that region, allow the energy executive to adapt the makeup and mix of programs to gain a competitive edge.

Americas

- *Short-term incentives* are typically prevalent for professional-level employees and above in all of the countries in the region.
- *Vacation allowances and additional salary payments* are often mandated. Most of the countries have a mandated additional salary payment, such as a 13th-month salary payment, Christmas or holiday/vacation bonuses, or mandated profit sharing. The US, Canada and Puerto Rico do not have a mandated additional salary payment.
- *Annual salary reviews* are common in all of the countries.
- Use of formal *pay structures* is common – job evaluation, market data or both are typically used to develop the ranges.
- While financial circumstances differ across the region, the economic downturn has affected remuneration decisions – *salary freezes* or *below-average salary adjustments* were experienced in many locations in 2010.

Figure 21 provides a summary of the typical components of remuneration for nine select markets in the Americas.

Figure 21
Compensation Plans Remuneration Mix – Americas



Pay mix data from Mercer’s Total Remuneration Surveys and Mercer’s Total Employment Costs Around the World report (www.imercer.com).

Asia Pacific

- *Short-term incentives* are prevalent for professional-level employees and above throughout the countries of the region.
- *Additional salary payments, such as base pay delivered over more than 12 months, or Christmas/vacation allowances* are used frequently in Asia Pacific. These payments are prevalent or mandatory in more than half the countries surveyed in this region.
- *Transportation allowances* and *car benefits* are commonly provided by employers in most of these countries. These benefits are not typically mandated.

- *Annual salary reviews* are common in all of the countries.
- *Job evaluation* is the most popular process for developing pay structures – more than three-quarters of the countries reported using job evaluation to determine salary ranges and pay structures.
- More than half of the countries surveyed reported *cost-cutting measures* or *salary freezes* as a result of the economic downturn.

Figure 22 provides a summary of the typical components of remuneration for 13 select markets in Asia Pacific.

Figure 22

Compensation Plans Remuneration Mix – Asia Pacific



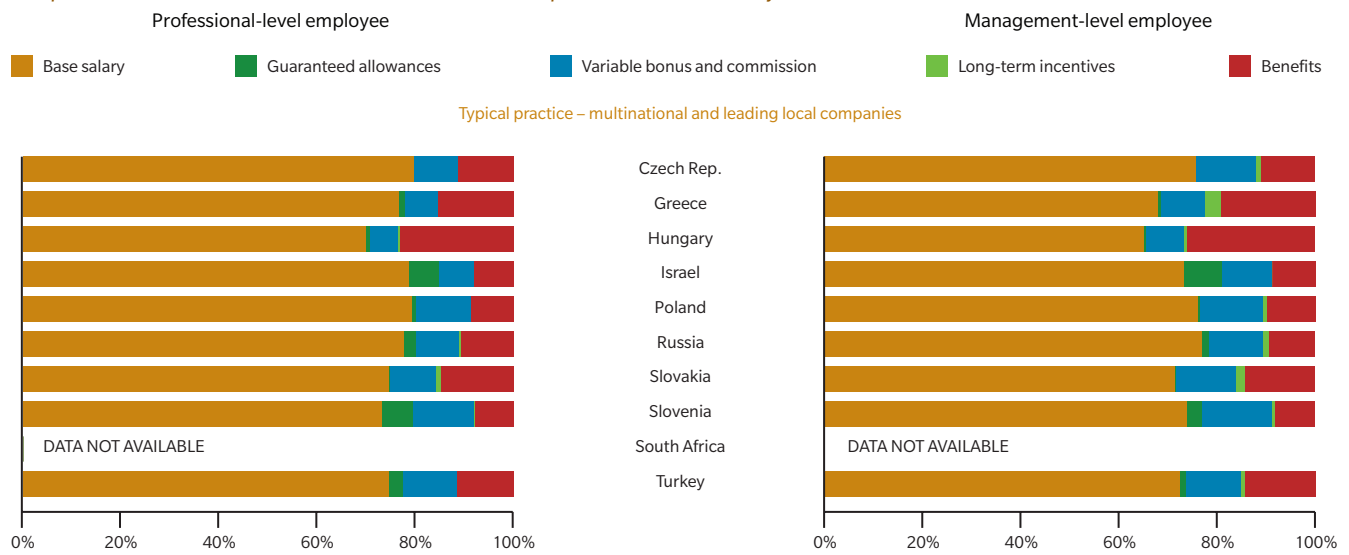
Pay mix data from Mercer's Total Remuneration Surveys (www.imercer.com/trs). Note that China's data are based on two cities – Beijing and Shanghai.

Eastern Europe, Middle East and Africa

- **Short-term incentives** are generally prevalent for professional-level employees and above among the countries covered for this region.
- Unlike the other regions in the survey, **additional salary payments** are not common in Eastern Europe, the Middle East and Africa. Additional salary payments are only mandated in Greece and are used occasionally in Russia (13th-month salary) and Turkey (13-, 14- and 16-month salaries are sometimes used).
- **Transportation allowances** are prevalent in one-third of the countries, are common in two of the countries and are mandated in one (Israel).
- **Car benefits** are prevalent in a majority of the countries and are common in one-third. Although a car benefit is prevalent in Israel, new tax legislation may significantly reduce the incidence.
- **Meal allowances** are prevalent in five of the countries and are common in approximately one-third. These allowances are typically provided as onsite dining facilities and in the form of meal vouchers for local restaurants and canteens.
- **Annual salary reviews** are common in all of the countries.
- A **job evaluation** approach to pay structures is common in seven of the countries. It is not common in Israel or South Africa.

Figure 23 provides a summary of the typical components of remuneration for 10 select markets in the Eastern Europe, the Middle East and Africa.

Figure 23
Compensation Plans Remuneration Mix – Eastern Europe, Middle East and Africa



Pay mix data from Mercer's Total Remuneration Surveys (www.imercer.com/trs).

Western Europe

- In all of the Western European countries, *short-term incentives* are typically prevalent for professional-level employees and above.
- A *vacation allowance* is legally mandated in 13 of the 14 countries. Spain is the only country without a mandated vacation allowance.
- Half of the countries in Western Europe provide prevalent or mandated *additional salary payments*.
- *Annual salary reviews* are common in all of the countries.
- Organizations in all but one country use *job evaluations* to develop and maintain pay structures. Some countries also use market data.
- In more than half of the Western European countries, *pay freezes, cost-cutting measures and more stringent reviews of incentive payouts* were experienced throughout 2010 as a result the economic conditions.

BENEFIT PLANS AROUND THE WORLD

While compensation programs for energy companies tend to evolve on a regular basis, the benefits area is heavily influenced by forces outside of the industry. As the energy industry places far more emphasis than industry in general on the benefit package provided to employees (especially due to the aging workforce challenge), it is important for employers to understand the global macro issues affecting benefit programs.

The five most important current benefit issues include:

- Reactions to changes in government policy
- Shift in focus to benefit cost efficiency
- Trend toward defined contribution (DC) plans
- Improving pension risk management
- Improving the global governance benefits framework

Figure 24 provides a summary of the typical components of remuneration for 15 select markets in Western Europe.

Figure 24
Compensation Plans Remuneration Mix – Western Europe



Pay mix data from Mercer's Total Remuneration Surveys (www.imercer.com/trs).

Reactions to Changes in Government Policy

Pension, health and welfare reform is gathering steam and is either in progress or planned in numerous countries around the world, such as France, the UK, Canada and the US. Drivers include aging populations and the increasing cost of providing an adequate retirement income and health service.

Changes vary per country and include increases in retirement ages, reductions in benefits and increases in contributions, as well as the introduction of mandatory programs. In many countries, governments aim to shift cost from the public sector to the private sector, creating an additional burden on employers to bridge any gaps. Energy employers can expect that such reform will continue to have a significant knock-on effect on the programs they provide.

Shift in Focus to Benefit Cost Efficiency

Moving out of the recession, budgets are still tight and energy companies are focused on ensuring cost efficiency and getting value for money. In some countries, companies are seeking to limit costs by various means – for example, by reducing benefits for new hires or introducing cost sharing.

Many companies are also looking to implement other cost control initiatives that may be less visible to employees – for example, by achieving global economies of scale through consolidation of third-party vendors and/or pooling of insurance risk.

Some energy companies are additionally introducing strategic innovations to benefit programs that may help with cost control in the longer term and may also be positively viewed by employees – for example, wellness programs and flexible benefits programs.

It seems that the recession has raised the profile of retirement, health and risk benefit programs among employees. Energy companies will need to take this into account as they formulate reward strategies for the recovery and beyond.

Trend Toward DC Plans

The trend for DC plans to be the primary employer-sponsored retirement program globally continues. However, next to managing legacy defined benefit (DB) plans, employers face specific DC challenges, including ensuring adequate retirement income and meeting employees' need for advice.

The recent global economic crisis has led to sponsor and employee concerns about the adequacy of DC plan benefits. For example, the generation of employees close to retirement may not be able to afford to retire as anticipated, leading to workforce planning issues.

Many companies have increased their focus on DC plan management, often at a global level with a view to ensuring cost efficiency (“value for money”) and ensuring that employees are empowered to make good decisions relating to retirement. More than one-third of sponsors plan to move to more centralization of DC plan oversight of plan design, financing, investment, administration and communication within the next two years.

While the energy industry still has a higher percentage of DB plans than overall industry, there is a growing trend toward DC plans as the primary vehicle for at least the younger part of the workforce.

Improving Pension Risk Management

A significant proportion of energy companies recognize the risk drivers embedded in retirement and benefit programs as a critical business issues, and they continue to focus on making informed decisions and improving risk management.

Many plan sponsors are still grappling with how to deal with the financial volatility inherent in legacy DB plans going forward. This is exacerbated in many countries where changes in funding levels (and resulting regulatory requirements) will have short- and long-term cash cost effects. Many sponsors are re-evaluating their financial management policies and are looking to keep tighter control over plans in order to quickly and appropriately react to market conditions and ensure that risk tolerance levels are met.

This will enable companies to adopt targeted solutions to mitigate cost and risk drivers that can be controlled, such as adjusting investment strategy to balance the allocation between growth assets and liability hedging, or formulating a funding and phased de-risking strategy to neutralize certain uncompensated risks being carried in a retirement plan.

For health and benefit plans, central oversight and monitoring of policy can help identify risks and issues and enable companies to react appropriately – for example, by encouraging behavioral change through a global health management program.

Improving the Global Governance Benefits Framework

Global energy organizations that sponsor retirement and other benefit plans around the world face the challenge of managing and overseeing those plans in a way that meets their global objectives. The increased visibility of retirement and benefit programs at board and senior management levels has encouraged a trend toward increased global oversight in the past several years.

Mercer's *Global Benefits Governance Survey 2009/2010* revealed:

- Only 16% of multinationals believe that their existing governance structures are robust and adequate enough to meet current and anticipated future needs.
- Half (50%) of respondents believe that better or timelier information is needed across various plan management activities.
- More than 80% of respondents believe that benefit plans have a material impact on group financials, and they are planning changes to governance structure to facilitate better management of financial risk and volatility globally.

As multinational energy companies often have fewer resources available on the ground to manage these programs locally and fewer headquarters resources available to oversee them centrally, the importance of having a robust global governance framework is greater today than it has ever been. Such a framework includes both the structure and the supporting processes needed to achieve the desired level of central oversight, and it frequently includes written policies on design, funding and investment; clear delegation of authority and assignment of responsibility related to benefit programs; and a defined approach to monitoring and mitigating risks.

With this foundation in place, a multinational is better able to examine substantive benefit issues in a strategic and proactive way and make sound decisions about solutions. This need may be even more acute for DC plans and nonretirement benefits where there is not the same rigorous funding review process as for DB pension plans. In the past, this has resulted in a multifocal decision-making approach. However, there is a strong trend for multinational energy employers to establish global guiding principles for these plans and to ensure adherence to these guiding principles.

CONCLUSION

Understanding the pattern and dynamics of total remuneration in different regions and talent markets is now an integral part of the workforce management and planning process in more sophisticated energy organizations. Getting the requisite data on these markets is a challenge. The demand is strong for better, more reliable data at an ever more granular job level.

However, as we have seen in our earlier discussion of evidence-based management, securing the right talent is not simply a matter of knowing and meeting the market price for the talent you need. Rather, it is about knowing what actually drives value in your organization, knowing what actually drives productive behavior among your current and desired workforce, and using that information to craft an employment proposition that aligns with your business and workforce needs.

The mix of pay, benefits, career opportunity and work environment that is optimal for your organization is likely considerably different from the mix that optimizes workforce and business outcomes in your competitors' organizations. Fixate on one element of the employment proposition, such as pay or even total compensation, and you are bound to get it wrong. When it comes to strategic workforce management and planning, there is no substitute for building a foundation of organization-specific evidence to support decision making.

In today's economy, organizations can no longer just give lip service to the idea that "people are our greatest asset." They need to start managing their workforces as if they are assets, applying the same discipline and quantitative mindset that they bring to other asset management decisions. Fortunately, the methods to accomplish this now exist and most organizations have all the data they need – from internal and external sources – to deploy an evidence-based approach and turn their workforce management and planning into a lasting source of competitive advantage.

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Mercer is a global leader in human resource consulting and related services. The firm works with clients to solve their most complex human capital issues by designing and helping manage health, retirement and other benefits. Mercer's 20,000 employees are based in more than 40 countries.

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