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Managing Expatriate Compensation: The Currency and Inflation Challenge

Managing Expatriate Compensation: The Currency and Inflation Challenges



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Today's agenda

1. Expatriate Allowance Trends

2. Assessing expatriate allowances

3. Determining cost of living allowances

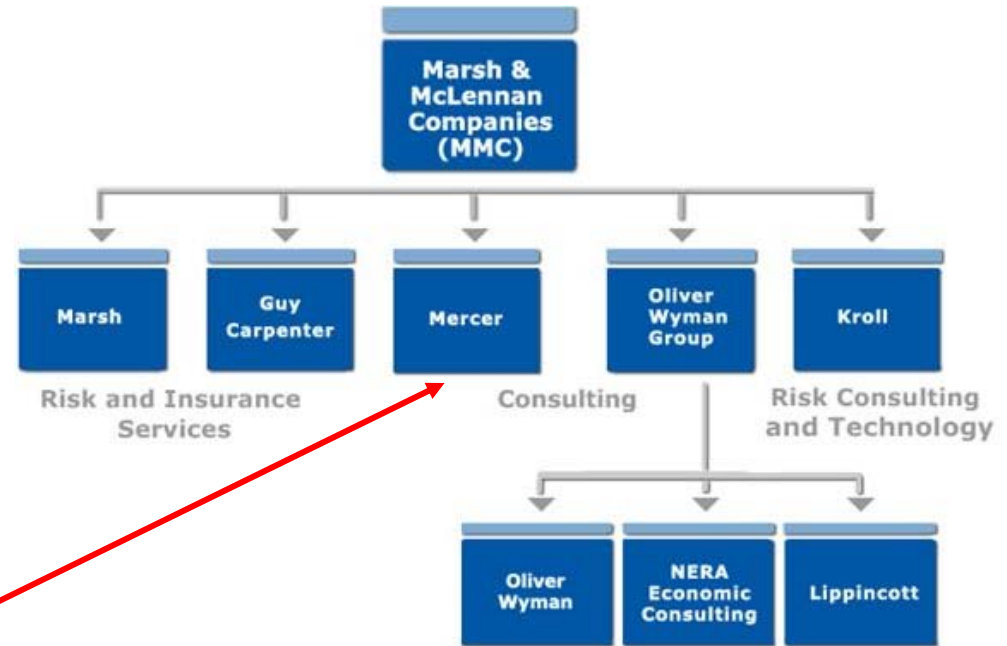
**4. Understanding and communicating changes caused
by exchange rate fluctuations**

About Mercer ©

The largest HR Consulting Company in the world with over 17,000 employees in 42 countries (180 cities)

Recent industry recognitions:

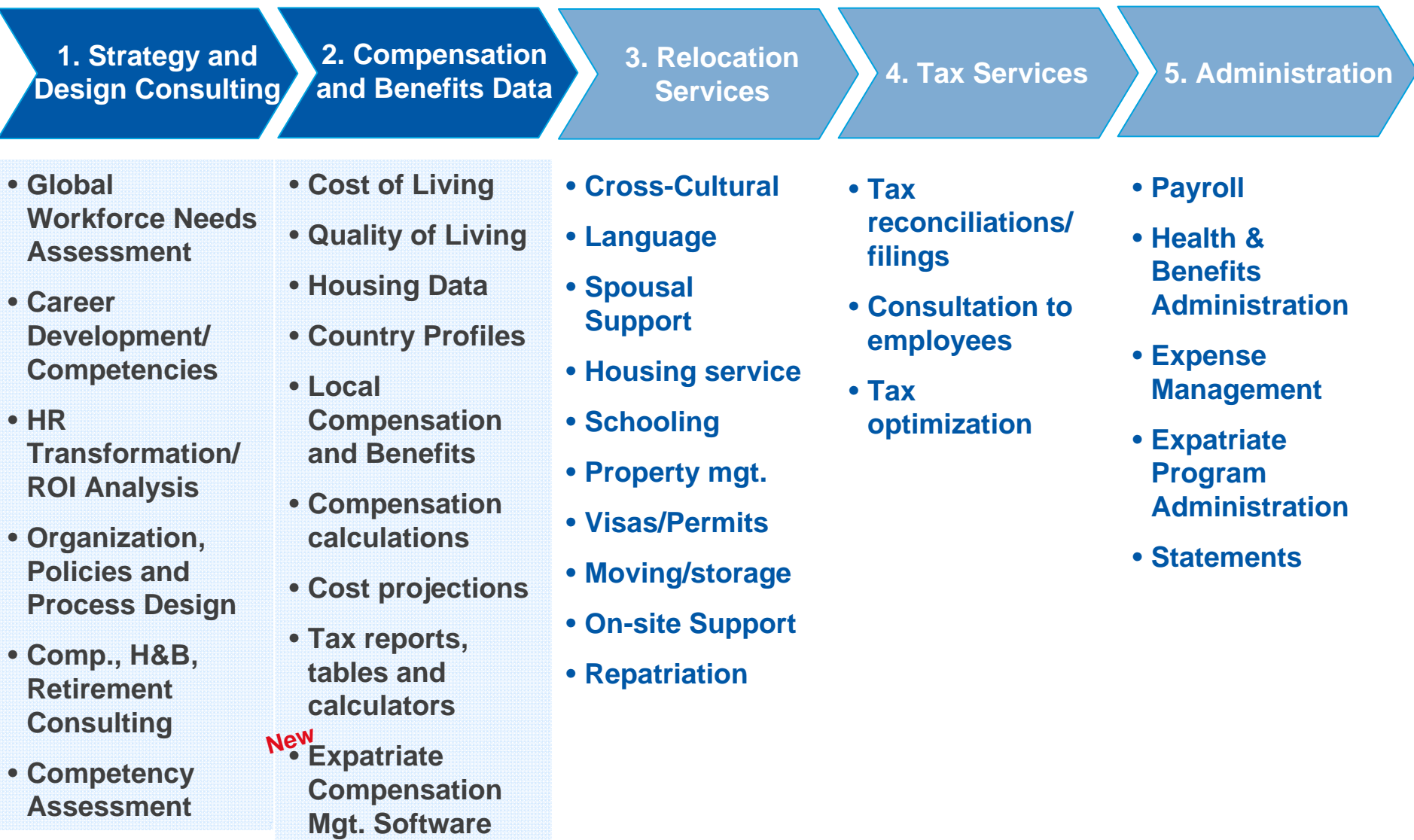
- Voted the "Best Employee Benefits Consulting Firm" by readers of Business Insurance magazine
- Voted the "Consulting Firm for HR Strategy and Management" in China by *China Staff*



Mercer worldwide countries

Argentina	Denmark	Malaysia	Taiwan
Australia	Finland	Netherlands	Thailand
Austria	France	New Zealand	Turkey
Belgium	Germany	Norway	UAE
Brazil	Hong Kong	Philippines	United Kingdom
Canada	Hungary	Poland	United States
Chile	India	Portugal	Venezuela
China	Indonesia	Singapore	
Colombia	Ireland	South Korea	
Czech Republic	Italy	Spain	
	Japan	Sweden	
		Switzerland	

Global Mobility Value Chain – Our Global Mobility Services



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The overall trends



**Managing expatriates
in unprecedented times – containing
international assignment costs**

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Webinar 9th & 12th & 25th of February 2009 Mini Survey Results with 960 total survey participants

In today's global economic downturn, is your company currently or in the near future looking to revise your international assignment policy and management process?

	European Participants	North American Participants	Latin American Participants	APAC Participants
Not sure yet	41.1%	48.7%	42.2%	55.4%
Yes	44.6%	36.4%	44.4%	36.7%
No	14.9%	15.2%	11.1%	7.9%

Main findings (1)

As a result of economic conditions, do you envisage any of the following taking place?	European Participants	North American Participants	Latin American Participants	APAC Participants
Avoid policy exceptions	31.0%	36.1%	26.7%	32.7%
Localize more expatriate compensation packages (where possible)	32.1%	28.8%	35.6%	51.6%
Reduce the number of medium – long term international assignees (2 to 5 years)	20.8%	32.3%	26.7%	28.6%
Reduce the number of overseas assignments	24.4%	23.7%	31.1%	12.8%
Consider reduction of expatriate allowance and perquisites	24.4%	21.5%	24.4%	32.7%
Favor short term assignments over long term assignments	13.7%	22.2%	8.9%	23.9%
Reduce the number of short term assignees (2 to 18 months)	6.5%	14.4%	20.0%	12.5%
Outsource various components of expatriate management	3.6%	9.3%	11.1%	6.4%
Lower the level of foreign investments	3.0%	2.3%	11.1%	5.2%
Bring the expatriate management process in-house	2.4%	2.5%	6.7%	9.6%

Main findings (2)

Are companies currently or in the near future looking to revise any of the following Allowances for medium to long term assignments?	European Participants	North American Participants	Latin American Participants	APAC Participants
	<i>(% of companies reporting no change at all)</i>			
Goods & Services Allowances	48.8%	56.3%	55.6%	52.5%
Housing Allowances	60.7%	62.1%	66.7%	54.5%
Education Allowances	67.9%	66.9%	57.8%	65.0%
Hardship Allowances	66.7%	64.1%	64.4%	71.4%
Mobility Premium (Foreign Service) Premium	51.8%	52.0%	53.3%	52.2%
Spouse Support	62.5%	64.4%	62.2%	68.5%
Pre Assignment Visit	66.7%	64.9%	44.4%	59.8%
Home Leave	62.5%	61.6%	46.7%	69.7%

Today's agenda

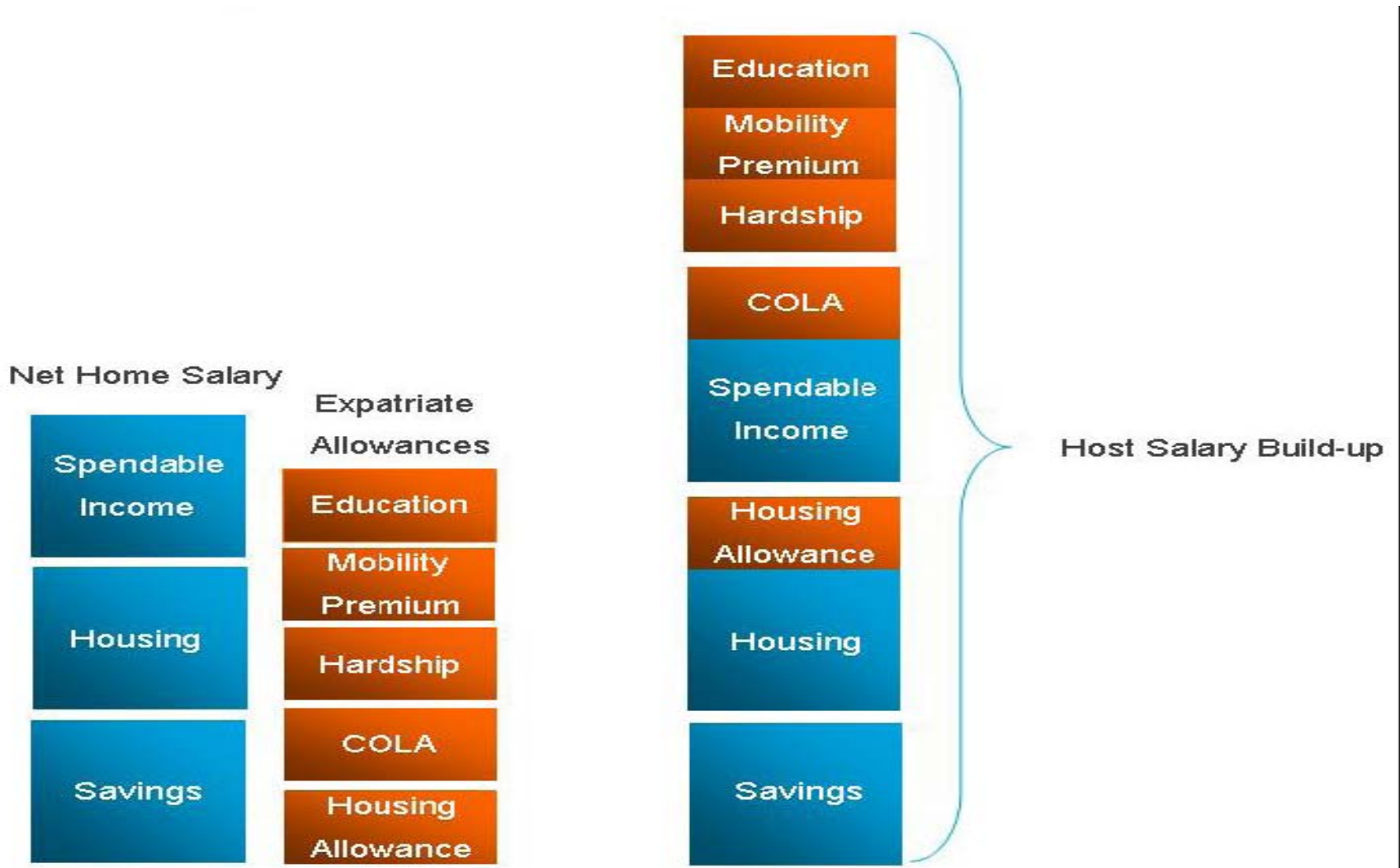
1. Expatriate Allowance Trends

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The classic balance sheet model



The options

- **Cost of living allowance**
 - Choice of spendable income
 - Choice of index
 - Negative indices
- **Accommodation**
 - Home housing norm
 - Utilities allowance
- **Education**
 - Choice of schools
 - Choice up to employee
- **Mobility premium**
 - Annual vs. one time or two times
 - Eliminate?
- **Hardship premium**
 - Review the list
- **Pre assignment visit**
 - Exclude family members
- **Transportation**
 - Norm or no norm
- **Home leave**
 - Leave or no leave

Case example – balance sheet calculation

Atlanta to Tokyo, M+2, March 2009 – amounts in USD

	Standard Calculation	Premium Calculation
Gross base salary	150'000	150'000
Net base salary	109'663	109'663
Spendable income	50'938	75'776
COL index	166	203
Exchange rate USD 1: JPY 92.30		
Host build-up		
COLA	33'619	78'050
Housing allowance	127'153	143'527
Mobility premium	15'000	15'000
Education allowance	41'538	41'538
Total	326'973	387'778
as a factor of the net home base salary	2.98	3.54
Potential savings net of tax		
One year		60'805
Two years		121'610
Three years		182'415

A quick look at Goods and Services (G&S) or Cost of Living allowances (COLA)*

Mercer findings

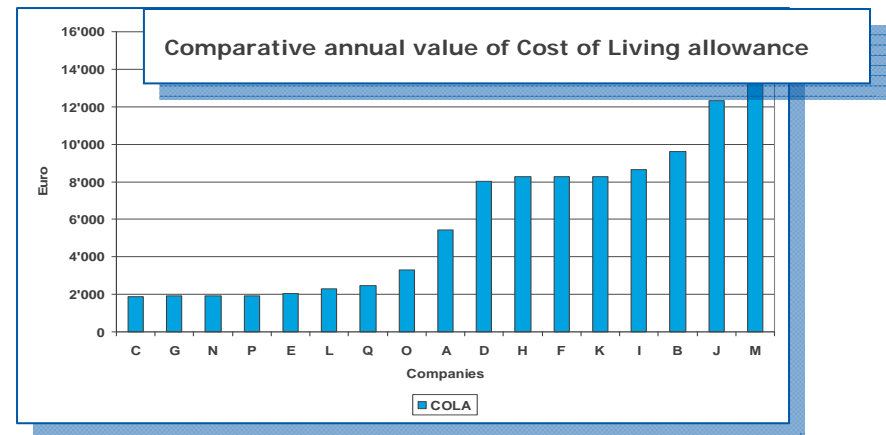
Mercer recently **measured the actual G&S allowance or COLA** among a group of the world's leading multinational firms in the US and Europe

1:10

Variation in net value of COLA

Based on:

- same salary
- same host / home combination
- same family size

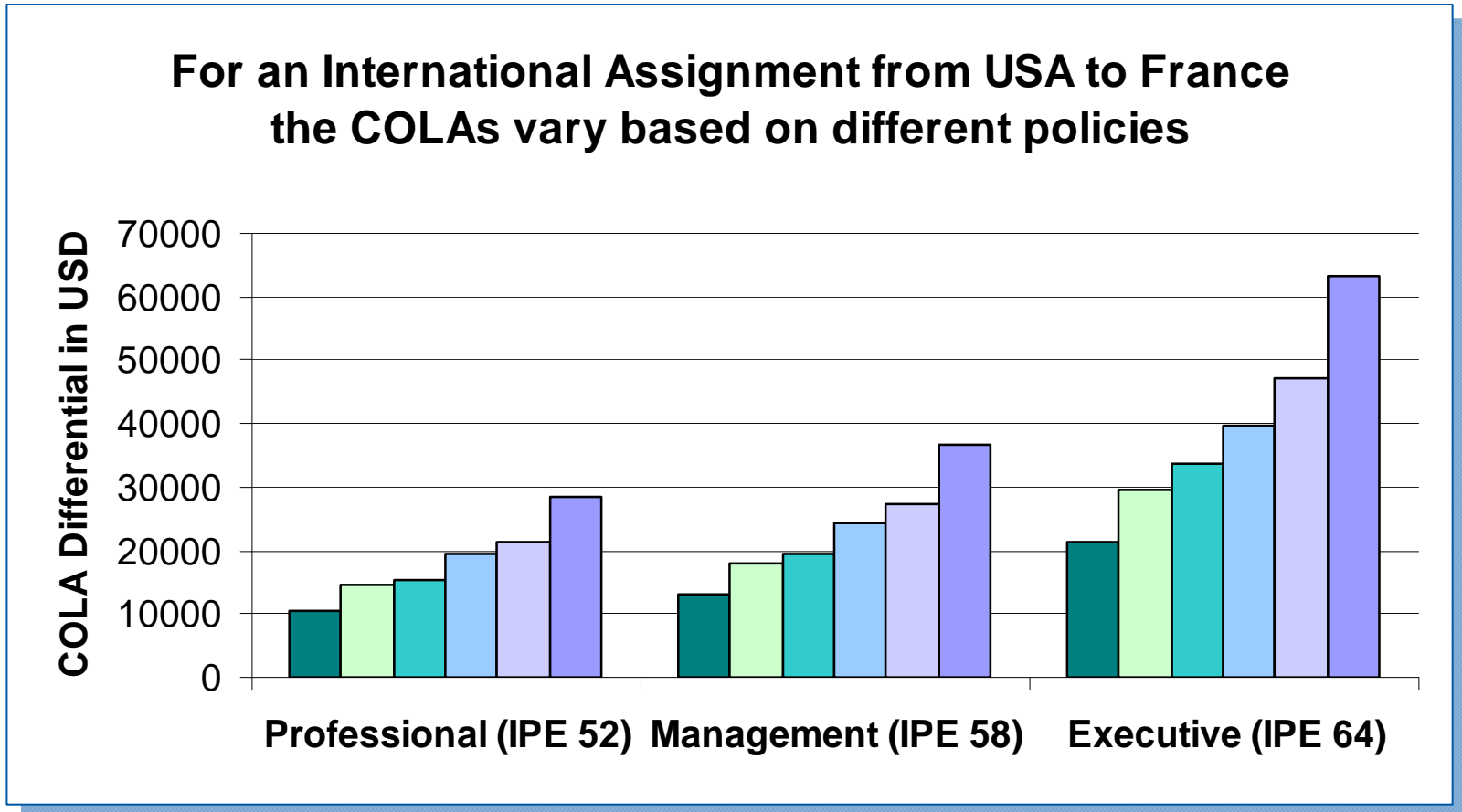


Based on a Frankfurt to Paris, €100,000 gross base salary and family of four

*In this document, we use indifferently “Cost of Living allowance (COLA)” and “Goods and Services (G&S) allowance” to design the same thing.

A quick look at Goods and Services (G&S)/Cost of Living allowances (COLA)

Comparison of the potential differences



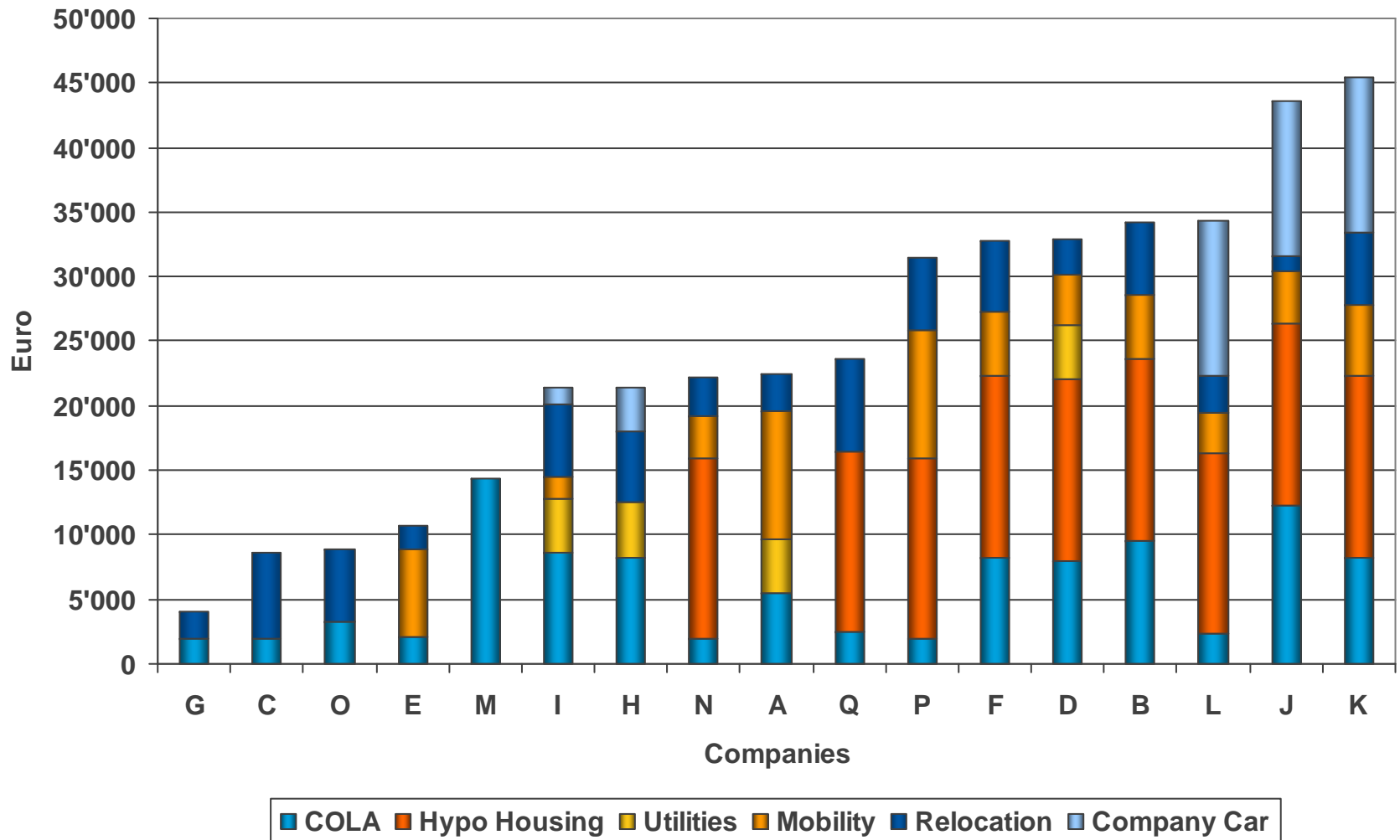
Our audit proposal

Your current COLAs vs. Mercer options

Home city	Host city	Position ID	Status	Your current COLA	Mercer COLA 1	Mercer COLA 2	Mercer COLA 3	Mercer COLA 4	Mercer COLA 5	Mercer COLA 6
Detroit	London	1	M 1	12'000	2'400	3'600	4'800	7'200	8'400	12'480
Detroit	London	2	S	9'000	1'800	2'700	3'600	5'400	6'300	9'360
Detroit	London	3	S	9'000	1'800	2'700	3'600	5'400	6'300	9'360
Detroit	London	4	M 4	24'000	4'800	7'200	9'600	14'400	16'800	24'960
Detroit	Paris	5	M 2	12'000	2'400	3'600	4'800	7'200	8'400	12'480
Detroit	Paris	6	M 2	12'000	2'400	3'600	4'800	7'200	8'400	12'480
Detroit	Paris	7	S	5'000	1'000	1'500	2'000	3'000	3'500	5'200
Detroit	Paris	8	S	2'000	400	600	800	1'200	1'400	2'080
Detroit	Mexico	9	M	2'000	400	600	800	1'200	1'400	2'080
Detroit	Mexico	10	M	10'000	2'000	3'000	4'000	6'000	7'000	10'400
Detroit	Mexico	11	M 2	15'000	3'000	4'500	6'000	9'000	10'500	15'600
Detroit	Mexico	12	M 3	3'000	600	900	1'200	1'800	2'100	3'120
Detroit	Mexico	13	M 3	12'000	2'400	3'600	4'800	7'200	8'400	12'480
Detroit	Tokyo	14	S	24'000	4'800	7'200	9'600	14'400	16'800	24'960
Detroit	Tokyo	15	M 3	36'000	7'200	10'800	14'400	21'600	25'200	37'440
Detroit	Milan	16	M 2	24'000	4'800	7'200	9'600	14'400	16'800	24'960
Detroit	Milan	17	S	24'000	4'800	7'200	9'600	14'400	16'800	24'960
Detroit	Shanghai	18	S	36'000	7'200	10'800	14'400	21'600	25'200	37'440
Paris	Detroit	19	M 3	36'000	7'200	10'800	14'400	21'600	25'200	37'440
Paris	Shanghai	20	S	12'000	2'400	3'600	4'800	7'200	8'400	12'480
Paris	Shanghai	21	S	15'000	3'000	4'500	6'000	9'000	10'500	15'600
Paris	Paris	22	M 2	9'000	1'800	2'700	3'600	5'400	6'300	9'360
Paris	London	23	M 3	9'000	1'800	2'700	3'600	5'400	6'300	9'360
Paris	Milan	24	M 3	24'000	4'800	7'200	9'600	14'400	16'800	24'960
Pans	Milan	25	S	12'000	2'400	3'600	4'800	7'200	8'400	12'480
Singapore	Paris	26	M 3	12'000	2'400	3'600	4'800	7'200	8'400	12'480
Singapore	Shanghai	27	M 2	5'000	1'000	1'500	2'000	3'000	3'500	5'200
Singapore	Shanghai	28	M 2	2'000	400	600	800	1'200	1'400	2'080
Singapore	Bombay	29	M 2	2'000	400	600	800	1'200	1'400	2'080
Singapore	Sydney	30	M 2	10'000	2'000	3'000	4'000	6'000	7'000	10'400
Mexico	Bogota	31	S	15'000	3'000	4'500	6'000	9'000	10'500	15'600
Mexico	Detroit	32	M 2	3'000	600	900	1'200	1'800	2'100	3'120
Mexico	Paris	33	M 2	12'000	2'400	3'600	4'800	7'200	8'400	12'480
Mexico	London	34	S	9'000	1'800	2'700	3'600	5'400	6'300	9'360
TOTAL				458'000	91'600	137'400	183'200	274'800	320'600	476'320
Potential Savings					366'400	320'600	274'800	183'200	137'400	-18'320
Mercer 1	Mean to mean index with index related spendable income									
Mercer 2	Mean to mean index with total spendable income									
Mercer 3	Efficient with index index related spendable income									
Mercer 4	Efficient index with total spendable income									
Mercer 5	Convenience index (Expatriate) with index related spendable income									
Mercer 6	Convenience index (Expatriate) with total spendable income									

(Amounts in \$USD)

Comparative annual value of allowances – with car



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What are the options?

Which portion of the salary to apply the cost of living index?

Annual gross base salary

- Hypothetical personal income tax
- Hypothetical social security contributions

= Annual net base income

- Housing (Home Housing Norm)
- Savings

= Annual net total spendable income

- Medical insurance
- Education, hobbies
- Furniture, vacation

= Annual net spendable income index related

Mercer's 10 categories of daily goods and services:

Food at home, food away from home, alcohol & tobacco, domestic Supplies, personal care, clothing & footwear, home services, utilities, transportation, sports & leisure

How to define the cost of living index

December 2008: Asian Efficient COL index, Local Mumbai to Singapore

Basket	Base City	Host City
Mercer International Asian Basket	MUMBAI LOCAL (IN)	SINGAPORE (SG)
Date of Price Survey	01/09/2008	01/09/2008
Date of Exchange Rate	01/09/2008	01/09/2008
Exchange Rate	EUR 1 = INR 64.405361	EUR 1 = SGD 2.102485
Cross Rate	INR 1 = SGD 0.03264	SGD 1 = INR 30.63297
Previous 6 months inflation	3.75%	2.00%
Previous 12 months inflation	8.16%	4.81%

* Index Categories	Base City	Host City		
		M / M	Efficient	Convenience
<input checked="" type="checkbox"/> 1) Food at Home	100	235	260	294
<input checked="" type="checkbox"/> 2) Alcohol and Tobacco	100	262	276	296
<input checked="" type="checkbox"/> 3) Domestic Supplies	100	142	156	157
<input checked="" type="checkbox"/> 4) Personal Care	100	174	192	213
<input checked="" type="checkbox"/> 5) Clothing and Footwear	100	320	360	360
<input checked="" type="checkbox"/> 6) Home Services	100	356	376	444
<input checked="" type="checkbox"/> 7) Utilities	100	215	227	262
<input checked="" type="checkbox"/> 8) Food away from home	100	280	321	378
<input checked="" type="checkbox"/> 9) Transportation	100	198	217	221
<input checked="" type="checkbox"/> 10) Sports and Leisure	100	174	193	198
Total Index	100	227	251	273
A) Excluding Utilities	100	229	253	274
B) Excluding Transportation	100	234	259	285
C) Excluding both above	100	236	263	288

How to define the cost of living index

December 2008: **International** Efficient COL index, Mumbai to Singapore

Basket	Base City	Host City
Mercer International Basket	MUMBAI (IN)	SINGAPORE (SG)
Date of Price Survey	01/09/2008	01/09/2008
Date of Exchange Rate	01/09/2008	01/09/2008
Exchange Rate	EUR 1 = INR 64.405361	EUR 1 = SGD 2.102485
Cross Rate	INR 1 = SGD 0.03264	SGD 1 = INR 30.63297
Previous 6 months inflation	1.75%	2.00%
Previous 12 months inflation	5.31%	4.81%

* Index Categories	Base City	Host City		
		M / M	Efficient	Convenience
<input checked="" type="checkbox"/> 1) Food at Home	100	171	192	218
<input checked="" type="checkbox"/> 2) Alcohol and Tobacco	100	124	133	143
<input checked="" type="checkbox"/> 3) Domestic Supplies	100	112	123	126
<input checked="" type="checkbox"/> 4) Personal Care	100	140	156	177
<input checked="" type="checkbox"/> 5) Clothing and Footwear	100	143	157	157
<input checked="" type="checkbox"/> 6) Home Services	100	198	229	270
<input checked="" type="checkbox"/> 7) Utilities	100	165	180	223
<input checked="" type="checkbox"/> 8) Food away from home	100	155	170	203
<input checked="" type="checkbox"/> 9) Transportation	100	165	189	194
<input checked="" type="checkbox"/> 10) Sports and Leisure	100	124	138	142
Total Index	100	150	167	182
A) Excluding Utilities	100	148	165	179
B) Excluding Transportation	100	146	161	180
C) Excluding both above	100	143	159	174

How to define the cost of living index

March 2009: Efficient COL index, Mumbai to Singapore

Basket Mercer International Basket	Base City MUMBAI (IN)	Host City SINGAPORE (SG)
Date of Price Survey	01/03/2009	01/03/2009
Date of Exchange Rate	01/03/2009	01/03/2009
Exchange Rate	EUR 1 = INR 63.332172	EUR 1 = SGD 1.942432
Cross Rate	INR 1 = SGD 0.03067	SGD 1 = INR 32.60458
Previous 6 months inflation	0.75%	0.25%
Previous 12 months inflation	<u>2.51%</u>	<u>2.26%</u>

The Cost of living index is impacted by 2 variables:

Exchange rate

Prices movements in the home and host cities

* Index Categories	Base City	Host City Efficient
<input checked="" type="checkbox"/> 1) Food at Home	100	199
<input checked="" type="checkbox"/> 2) Alcohol and Tobacco	100	138
<input checked="" type="checkbox"/> 3) Domestic Supplies	100	134
<input checked="" type="checkbox"/> 4) Personal Care	100	165
<input checked="" type="checkbox"/> 5) Clothing and Footwear	100	167
<input checked="" type="checkbox"/> 6) Home Services	100	243
<input checked="" type="checkbox"/> 7) Utilities	100	194
<input checked="" type="checkbox"/> 8) Food away from home	100	180
<input checked="" type="checkbox"/> 9) Transportation	100	202
<input checked="" type="checkbox"/> 10) Sports and Leisure	100	145
Total Index	100	177
A) Excluding Utilities	100	175
B) Excluding Transportation	100	170
C) Excluding both above	100	167

The COL survey shows price increases over the 12 months of +2.51% in Mumbai and +2.26% in Singapore.

How to define the cost of living index

March 2009: Efficient COL index, Mumbai to Singapore
Updated with exchange rate May 2009

Basket Mercer International Basket	Base City MUMBAI (IN)	Host City SINGAPORE (SG)
Date of Price Survey	01/03/2009	01/03/2009
Date of Exchange Rate	<u>01/05/2009</u>	01/05/2009
Exchange Rate	EUR 1 = INR 66.544709	EUR 1 = SGD 1.988254
Cross Rate	<u>INR 1 = SGD 0.02988</u>	SGD 1 = INR 33.46892
Previous 6 months inflation	0.75%	0.25%
Previous 12 months inflation	2.51%	2.26%

* Index Categories	Base City	Host City Efficient
<input checked="" type="checkbox"/> 1) Food at Home	100	204
<input checked="" type="checkbox"/> 2) Alcohol and Tobacco	100	141
<input checked="" type="checkbox"/> 3) Domestic Supplies	100	137
<input checked="" type="checkbox"/> 4) Personal Care	100	169
<input checked="" type="checkbox"/> 5) Clothing and Footwear	100	171
<input checked="" type="checkbox"/> 6) Home Services	100	250
<input checked="" type="checkbox"/> 7) Utilities	100	199
<input checked="" type="checkbox"/> 8) Food away from home	100	185
<input checked="" type="checkbox"/> 9) Transportation	100	207
<input checked="" type="checkbox"/> 10) Sports and Leisure	100	149
Total Index	100	181
A) Excluding Utilities	100	179
B) Excluding Transportation	100	175
C) Excluding both above	100	171

The COL index is recalculated based on the May 2009 exchange rate of 1 INR = 0.02988 SGD (SGD gain strength by 2.6% since March 09 and by 8.5% since Sept 08).

The COL index increases to compensate the potential loss in currency conversion.

Mercer Global HRMonitor Web tool allows companies to adjust the Cost of Living index with the latest exchange rate instantly.

How to define the Cost of Living Allowance

- Management Level IPE 52 – Transfer from Mumbai to Singapore
- From September 2007 to March 2009, with a salary increase +12.7%
- Family status: Married couple + 2 children

Survey Dates	Exchange Rate Date	Annual Gross Base salary (INR)	Total Spendable Income Net (INR)	COL Index Efficient	Exchange rate 1 INR = SGD	Exchange rate Variation (%)	COLA (INR)	Spendable Income adjusted by COLA & exchange rate (SGD)	Variation (%)
September 2007	Sept.07	890'000	545'251	146	0.03746		250'815	29'821	
September 2008	Sept.08	890'000	545'251	167	0.03264	-12.9%	365'318	29'721	-0.33%
March 2009	March 09	1'003'030	589'349	177	0.03067	-6.0%	453'799	31'993	7.65%

COL Index increases to adjust for the currency & inflation fluctuations

Goods and Services Allowance guarantees a sufficient purchasing power in Singapore

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Understanding and communicating changes caused by exchange rate changes

- In high currency fluctuations economy, expatriates tend to start to question their COLA's and overseas purchasing power. It is important to even more **communicate** with your expatriates.
- It is possible that the expatriates are **not actually spending** the whole host part of the salary in the host location; they are saving more than expected and are sending more money back home.
- Consequently when the **currency devalues strongly** such as the Russian Rubles, Polish Zloty, South Korean Won, Japanese Yen, British pounds, the Brazilian Real, Mexican pesos have against the USD, the expatriates are losing on the additional saving opportunity of the salary.
- Therefore the discussion about the COL index evolution with your expatriates may not be a true concern about their COLA's but in reality a concern about their **additional savings opportunity**.

Challenges of companies paying expatriate compensation packages in **home** currency (INR), Mumbai to Singapore

Marital Status: Married with 2 children Transfer from Mumbai to Singapore	INR
Annual Gross home country reference salary	890'000
Annual Net home country pay	703'480
Non-Spendable income: Hypothetical Home Housing Costs, Savings and Other expenses	158'229
Total Spendable income (daily basket of goods and services)	545'251
Cost-of-Living Allowance (COLA): COL Efficient 167 Exchange rate: 1 INR = SGD 0.03265	365'318
Housing Allowance	3'694'507
Expatriation premiums - Mobility premium based on 5% of Gross - Education allowance	44'500 1'102'603
Total annual net host country pay	5'910'408

	INR	SGD value in Sept 08	SGD value in March 09
Saving Part	202'729		
Spending Part	5'707'679	186'356	175'05
Currency fluctuation INR & SGD September 08 to March 09	-6.1%		-11'30
Loss of the spending part when converted in SGD by - 6.1%			

Full salary paid in Home Currency INR Currency protection needed for the spending part

Challenges of companies paying expatriate compensation packages in **host** currency (SGD), Mumbai to Singapore

Marital Status: Married with 2 children Transfer from Mumbai to Singapre	SGD
Annual Gross home country reference salary	29'059
Annual Net home country pay	22'969
Non-Spendable income: Hypothetical Home Housing Costs, Savings and Other expenses	5'166
Total Spendable income (daily basket of goods and services)	17'802
Cost-of-Living Allowance (COLA): COL Efficient 167 Exchange rate: 1 INR = SGD 0.03265	11'928
Housing Allowance	120'607
Expatriation premiums	
- Mobility premium based on 5% of Gross	1'453
- Education allowance	36'000
Total annual net host country pay	192'956

	SGD	INR value in Sept 08	INR value in March 09
Saving Part	6'619	202'729	215'817
Spending Part	186'337		
Currency fluctuation INR & SGD September 08 to March 09	-6.1%		13'088
Gain of the saving part when converted back in INR by + 6.1%			

Full salary paid in Host Currency SGD Currency protection needed for the saving part

Challenges of companies paying expatriate compensation packages in **Third** currency (USD), Mumbai to Singapore

Marital Status: Married with 2 children Transfer from Mumbai to Singapore		USD
Annual Gross home country reference salary		20'716
Annual Net home country pay		16'374
Non-Spendable income: Hypothetical Home Housing Costs, Savings and Other expenses		3'683
Total Spendable income (daily basket of goods and services)		12'691
Cost-of-Living Allowance (COLA): COL Efficient 167 Exchange rate: 1 INR = SGD 0.03265		8'503
Housing Allowance		85'981
Expatriation premiums		
- Mobility premium based on 5% of Gross		1'036
- Education allowance		25'665
Total annual net host country pay		137'559

	USD	INR value in Sept 08	INR value in March 09
Saving Part	4'719	202'766	233'222
Currency fluctuation USD & INR September 08 to March 09	-13.1%		30'456
Gain of the saving part when converted back in INR by 13.1%			
		SGD value in Sept 08	SGD value in March 09
Spending Part	132'840	186'337	201'364
Currency fluctuation USD & SGD September 08 to March 09	-7.5%		15'027
Gain of the spending part when converted back in SGD by 7.5%			
Full salary paid in Third Currency USD Currency protection needed for the saving & spending parts			

Split payment of expatriate compensation package Mumbai to Singapore summary INR vs. SGD

Marital Status: Married with 2 children	Home City Mumbai (INR)	Host City SINGAPORE (SGD)
Annual Gross home country reference salary	890'000	29'059
Annual Net home country pay	703'480	22'969
Non-Spendable income: Hypothetical Home Housing Costs, Savings and Other expenses	158'229	5'166
Total Spendable income (daily basket of goods and services)	545'251	17'802
Cost-of-Living Allowance (COLA): COL Efficient 167 Exchange rate: 1 INR = SGD 0.03265	365'318	11'928
Housing Allowance	IND	SGD
a) Host location expatriate accommodation costs	3'816'694	124'596
b) Hypothetical home country housing costs	122'187	3'989
c) Housing allowance	3'694'507	120'607
Expatriation premiums		
- Quality of Living allowance	-	-
- Mobility premium based on 5% of Gross	44'500	1'453
Other allowances (according to company policy)		
- Education allowance	1'102'603	36'000
Total annual net host country pay	5'910'408	192'956
Split payment	202'729	186'337

Recommendations

It is very difficult to estimate which part of the salary will be really spent in the host country and which part will be kept in the home country

Most companies will leave the decision on the split with a certain limit to the expatriate

This approach prevents any future discussion with the expatriate

The responsibility is put on the expatriate's shoulders

Questions/Answers

MERCER



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2008/2009 Edition

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Survey of expatriate housing costs and practices in major cities worldwide



Current housing information around the world

Accommodation information across 50 cities to aid your expatriate housing decisions

Housing remains one of the most sensitive issues in the expatriate package negotiation process, primarily because of its cost but also because of its significant impact on the assignee and family. Mercer's expatriate accommodation costs information can help you make better-informed expatriate housing decisions.

Mercer's new report, *Survey of expatriate housing costs and practices in major cities worldwide*, presents housing policies and practices as well as complete, current housing-related cost survey data to help you apply them. The report will help both decision makers and assignees with information on pricing and availability for preferred expatriate neighbourhoods in each city covered.

This 2008/2009 survey provides essential information to help you design your expatriate compensation packages. It can also help your employees relocate with confidence that housing issues will be handled effectively and fairly.



How do housing policies vary from one global region to another?

What housing-related costs do companies usually cover?

How do employers handle expatriates' purchase of accommodations?

What are the tax implications of expatriate housing for employers and employees?

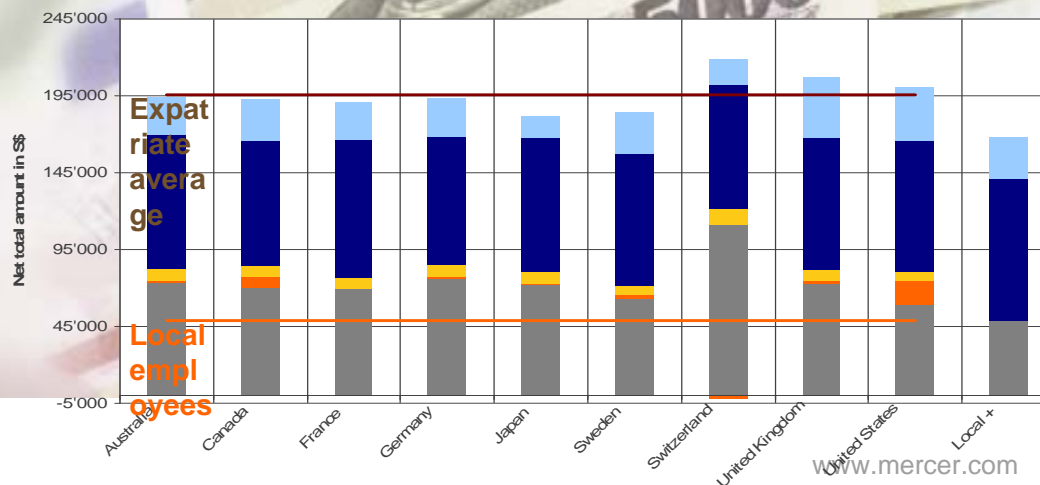


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