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Compensation 2011: Global strategies for five critical planning questions

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Compensation 2011: Global strategies for five critical planning questions

The global recession is morphing into a global recovery – some countries are already there while others are cautiously optimistic. When it comes to setting compensation strategy for next year, one equally powerful message throughout all regions shines through: Talent reigns supreme.

Around the world, organizations are focused on engaging key talent through thoughtful spending – a back-to-basics approach, if you will – to quickly spur growth and gain a competitive advantage. Many, however, are struggling with decisions about where to invest – whether to focus more on base pay, funding the incentive pool, or training and career planning programs.

Mercer insight from around the world

To help you with planning a 2011 compensation strategy and remaining globally competitive, we asked our compensation experts around the world to provide Mercer survey data and insight into compensation trends. Our objective is to help you design and implement a compensation program that aligns with current business strategy, is affordable and sustainable, drives productivity, engages key talent and minimizes the chance for pay inequity.

Five critical planning questions for 2010

1. What is the current mindset regarding base pay increases for 2011?
2. What is the status of pay for performance?
3. How are companies managing employee expectations for 2011?
4. How are employers incentivizing and engaging high-potential employees?
5. Where will employers place their compensation investment bets in 2011?

1. What is the current mindset regarding base pay increases for 2011?

Summary:

Around the world, generally speaking, the mindset is cautious optimism. Still, there is a growing reluctance in parts of Asia and the Middle East to sustain double-digit base pay annual increases. In countries that were more affected by the economic downturn, organizations are weighing restraint regarding base salary increases against playing “catch-up” after a year or two of frozen salaries. Yet, in both situations, employers are concerned about retaining talent and the tug of war between cash, career programs and retention.

Actions to consider:

- Determine the distinct employee groups or workforce segments (for example, business units, job functions or geographies) that are most critical in creating value for your organization.

- Differentiate the reward types and opportunities for these “performance drivers.”

- Help your line managers understand how segmentation helps them deliver better business results.

Country/region specifics:

ASEAN: In this region, Singapore has had a strong economic rebound, and most of the countries are most concerned about retaining talent. This is causing pressure on salary increases and retention strategies.

Australia: The mindset here is to stay with the market. Fiscal years 2008 and 2009 had some salary freezes (mostly at the executive and management levels and, in some organizations, at the salaried staff level), but this has not been evident in 2009 and 2010. Affected organizations are now considering "catch-ups," and some sectors, such as Resources, are likely to have larger increases.

Canada: We are seeing a generally positive mindset regarding base pay increases for 2011. Significantly fewer salary freezes are anticipated, indicating that overall confidence in the strength of the economy has increased. The public sector stands out, however, because it is projected to have the lowest increases as governments struggle to recover from budget deficits created in the past year.

China: Given the quick recovery and expansion of business to capture the benefits of the economic recovery, the competition in the talent market has been picking up more quickly than expected. Many organizations experienced higher turnover in the first half of this year than they had a year ago and are now in hiring mode; however, it is hard for them to find the appropriate talent at an ongoing market rate. We expect pay increases will be in high single digits and maybe 50 to 75 base points higher than this year, with significant industry differences. The electronics and mechanics industries may stand out as the highest pay increase industries. Also, local companies may have pay increases 50 to 100 base points higher than those for multinational companies. Given the double-digit minimum wage increase in most provinces this year, we expect a much higher pay increase for this segment of employees than others.

France: Unpredictability is the current mindset here. For 2010, we anticipated 2.5% increases, but the actual increase was only 1%–1.5%.

Germany: After salary freezes, mainly for executives in 2009, a moderate average base pay increase of around 2.5%–3% is expected. Nevertheless, some companies have been more affected by the economic downturn than others – as such, this will define the appropriate increase factor for each company.

GCC: Since the financial crisis of 2008, much has changed in the Gulf Cooperation Council (GCC) region (Saudi Arabia, United Arab Emirates, Qatar, Kuwait, Oman and Bahrain). Many companies downsized, inflation rates slowed to single digits, and compensation increases underwent careful consideration. Although most companies reported targeting higher increases (8%), in reality these numbers weren’t reached. In the coming years, we expect average growth in compensation to vary around 5%–6% annually for the region – Qatar and the United Arab Emirates may have slightly higher percentages, and the remaining countries may have slightly lower percentages.

India/Sri Lanka/Bangladesh: Drastic changes to the current trend in salary increases are not expected for 2011 in these countries. In fact, budgets for salary increases might be slightly tightened as companies deal with other aspects of rewards. In India, many multinationals are reluctant to continue granting double-digit increases in the future. Meanwhile, the talent market is getting hot with an increase in hiring and growing attrition. There is also concern that the high rate of salary increases will severely hamper the attractiveness of India as a destination for business, particularly for outsourcing and software development. Mercer's salary increase forecasts for 2011 for India, Sri Lanka and Bangladesh are 11%, 11% and 12%, respectively.

Japan: Companies are still very cautious about granting base pay increases for domestic employees. Overall corporate financial performance has improved since 2009, but many of our clients are fully aware that profits have come from overseas operations that are growing – not from domestic operations that are shrinking.

Mexico: We have seen relatively flat annual salary increases in the last few years. Next year, the forecast is a 5% annual increase, whereas 2009 actual and 2010 projected increases were 4.7%.

UK: Few organizations have frozen pay in 2010 or anticipate freezing pay in 2011. In terms of compensation, there has been some re-emphasis on the total value of the package (that is, stressing the intangible elements because organisations can't afford tangible increases in cost).

US: Organizations plan to adjust their remuneration practices for 2011 in response to concern about losing top talent after the past year of pay freezes and, for some, signs of economic recovery. According to Mercer data, more than 98% of companies plan to award base pay increases in 2011. Moreover, there should be a clear decrease in the number of companies freezing pay – only 2% of companies are planning across-the-board salary freezes next year, compared with 13% in 2010 and 31% in 2009. Of the employers planning to grant base pay increases, the average increase is expected to be 2.9% in 2011, up from an actual 2.7% in 2010 but down from 2009 levels (3.2% on average). This indicates that the US is not back to pre-recession pay increase levels

2. What is the status of pay for performance?

Summary:

For many organizations, paying for performance is easier said than done. The many roadblocks in place include cultural (more focus on team), financial (not enough funding of the pool), target setting (defining performance parameters) and pay equity. Yet, when done right, pay for performance effectively allocates limited rewards investments and retains top performers. It is a back-to-basics approach to pay strategy that results in thoughtful spending.

Actions to consider:

- Many business strategies have changed the last 12–24 months. If so, it's time for new performance measures. Select targets that are meaningful (an outcome that results in corporate value) and relevant (a set of results that appropriately reflects short- and long-term performance, and individual or team contributions).

- Don't jump back into business as usual. The recession led your organization to new strategies and tactics, so consider which ones should remain and which ones should not, such as putting more pay at risk or making base pay increases only every two to three years as job responsibilities change.

Country/region specifics:

ASEAN: A number of the ASEAN countries have displayed a continuing drive for performance pay, and this can be expected to continue if the outlook remains positive.

Asia Pacific: While every country and industry sector in Asia Pacific is diverse in terms of its economy and human capital planning and reactions, for most, skill acquisition and retention are essential to capturing the opportunities open to Asia. Pay for performance is a smaller priority, especially in rapidly growing markets such as China, India, Indonesia and Vietnam.

In addition, the pay-for-performance agenda can be influenced by cultural factors, including:

- Communist background (Vietnam), where performance pay is viewed somewhat skeptically

- More emphasis on team-based culture (Japan)

- Progression focused more around the individual than the job (Japan and Korea)

- Different dynamics between multinational and local companies in terms of compensation planning and reactions to market needs (even in China)

Australia/New Zealand: Pay for performance in these regions has largely been unchanged the last two to three years. Short-term incentive payouts were consistently lower in 2009 and 2010 than in previous years. Some concerns about corporate results in 2011 may affect bonuses.

Canada: We have not seen any change in the commitment to pay for performance in the Canadian market. Perhaps a year of weaker performance will reinforce the link between rewards and organizational performance in the market. Establishing reasonable and meaningful objectives will be critical to maintaining confidence in pay for performance – particularly in sectors such as manufacturing, where the recovery is occurring more slowly.

China: Differing from many other countries, organizations here have very aggressive expansion plans for their business in China. Leadership development is one of the top themes, because China lacks qualified leaders and talent. Another theme will be total rewards, which will focus more on non-cash components such as work/life balance and development and learning.

Japan: The pay-for-performance boom is over. The introduction of pay for performance was widely criticized, as it was perceived to have ruined the team-based culture that many Japanese companies believe is one of their core strengths.

France: The expected growth is 1.2%, and pay for performance can be applied only if it is associated with two other key elements: pay equity and collective increases of the lowest salaries. Pay allocations in general – and merit increases in particular – are functions of three elements together: pay equity, pay for performance and collectively low salary increases. Pay equity is going to be an even stronger theme in 2011 – the same level of pay will have to be ensured for the same levels of position, skills (knowledge), responsibility and exposure to stress.

Germany: Employers are struggling to find the balance between bonus funding and target setting. Companies have reviewed their performance management systems and aligned them better to the overall company goals. For top management, a focus on more sustainable growth was introduced by the amended stock corporation law. Listed companies have increasingly introduced this focus in their business practices, in addition to the long-term incentive bonus deferrals or midterm incentives that measure performance on a three-year basis.

GCC: Pay for performance has become an important theme for most companies in this region, where the focus is on talent development and performance-driven compensation. Most of our clients are making it very clear to their employees that the future is for those who perform.

Mexico: Roughly one in three companies is planning to modify the design of its pay-for-performance program, mainly by fine-tuning financial measures and increasing the weighting of the company's performance versus individual performance.

UK: Pay for performance is certainly a visible theme, but many organizations are finding it difficult to identify performance measures and targets in light of the economy.

US: There is a tug of war between limited resources and the need to retain critical employees – recognizing top performance is still clearly a driving factor. Differentiating salary increases among employee groups is a necessity, as it allows employers to make investments in those employees who will advance the organization. To that end, the gap between high-performing employees and those in the lower performing categories is widening significantly. The highest-performing employees (14% of the workforce) are expected to receive average base pay increases of 4.3% in 2010, compared with 2.6% for average performers (35% of the workforce) and 0.5% for the weakest performers (7% of the workforce).

3. *How are companies managing employee expectations for 2011? What are the key messages?*

Summary:

Managing expectations and facilitating frequent communication are essential ingredients for employee engagement – a top concern of many organizations. But what and how are employers communicating about their compensation programs these days? For the most part, the channels of communication are as diverse as the messages, which include discussion of the business situation, total rewards concepts, career development, job mobility opportunities and pay for performance.

Actions to consider:

- Has your employee value proposition changed? Maybe you are keeping more pay at risk or focusing less on pay and more on employee training and development. Articulate the new value proposition, moving from tactical employee communications to more strategic total rewards discussions.

- Equip managers with talking points to help with such discussions.

- Tailor the messaging to your current and future workforce values; consider generational differences.

- Be realistic and straightforward in your messaging; do not overpromise and under deliver.

- Vary the communication medium to include in-person, video, online and e-mail.

Country/region specifics:

Australia/New Zealand: In Australia and New Zealand, the main theme is maintaining variable pay that is linked to performance.

Canada: Most employers in Canada have found that taking a clear, straightforward approach to communicating compensation adjustments is received best by employees. Communicating the organization's business situation along with a view of the market (based on credible data sources) is most effective.

China: Managing employee expectations is going to vary by sector and location. In the high-growth market, it will be difficult to restrain expectations. Many companies are in this mode already; their key communication messages include:

- Focus on people's efforts and the company's bright future

- Emphasize productivity and pay for performance

- Introduce the total rewards concept and the focus on talent development

France: Communication of the compensation philosophy, policies and rules to all employee remuneration committees and work councils is going to be instrumental in managing expectations and avoiding tensions. In 2011, organizations will rely even more on practical tools, such as compensation management guides, that include clear definitions of key talent and precise rules of how pay funds are allocated and distributed.

GCC: In this region, the communication focus varies based on the workforce mix. For example, in Qatar and the United Arab Emirates (Abu Dhabi), the key challenge is to induct local nationals into the workforce. The number of local nationals available for recruitment is still low, and the quantity coming out of schools, colleges and universities is not sufficient to meet market demands. As a result, there is a race for local talent, leading companies to offer more competitive packages along with career growth and talent-development opportunities. In Saudi Arabia, Oman, Kuwait and Bahrain, the picture is slightly different. In these countries, local nationals comprise a considerable size of the workforce; thus, the challenge is to develop existing employees through training and career planning without offering very large compensation packages.

Germany: Employers will focus on company performance and the impact of individual contributions in employee communication. They will also look to total rewards messages such as career and personal development.

Japan: Key messages from companies are "job security" for average performers and "development opportunities" for high performers. Employees will not expect significant pay increases if the economic landscape continues to be weak in 2011.

Mexico: Because annual salary increases have been relatively flat for the last two years and the same is anticipated for next year, messaging will focus on a total rewards theme of skill building, career development, work/life balance and variable compensation.

UK: There is widespread focus on transparency, as well as fine-tuning and communicating the reward philosophy, which most companies have reviewed in the last 12 months.

US: Now more than ever, employees desire a straightforward message about their company's business prospects and their role in its success. Companies need to remain realistic, deliver simple messages and use all of the communication tools available to rebuild engagement. Both cash and non-cash (career planning, training, work/life) communication messages will help reduce post-recessionary flight.

4. How are employers incentivizing and engaging high-potential employees?

Summary:

As they say, cash is king … at least for areas least affected by the economic downturn, for companies able to play "catch up" and for workforce segments offering high-growth potential for their company. But cash – in the form of base and incentive pay – can only go so far. Many organizations around the world are using a total rewards philosophy and are fine-tuning and communicating their employee value proposition.

Actions to consider:

- Use all reward levers available; cash compensation is not the only way to encourage employee engagement.

- Consider creating career paths to provide development opportunities. Alternatively, employ special project opportunities that elevate an employee's corporate visibility and develop new skills that enhance employment security.

- Fine-tune your performance management program, through manager training and technology, to enhance processes and analytics.

- Implement an employee communication plan to minimize distractions and increase productivity.

Country/region specifics:

Asia: For much of Asia, cash remains king. There will be a strong focus on the overall value proposition to support retention, and high potentials will be the subject of increasingly targeted strategies.

Australia/New Zealand: There is an increasing and genuine consideration given to creating and communicating the employee value proposition. Total reward strategies are being reviewed, now that the tax benefits of packaging are extremely limited.

Canada: Increasingly, employers are assessing both their workforce requirements and their people to ensure that they have a clear view of which jobs are critical and exactly which employees are key (critical role, top performer, high potential). We see greater thought and structure around development programs and mentoring programs for high-potential employees. We believe that more organizations should be directing salary dollars to key talent, demonstrating to those employees that they are highly valued.

China: Cash is first, such as retention and deferred bonuses. Also popular are career planning, including job rotation and leadership development programs, and supplemental medical and pension plans; other benefits, such as education and car benefits, are also on the rise.

Japan: Companies are incentivizing and engaging high-potential employees mainly through non-monetary measures, such as training and career opportunities. Overseas assignments can be an effective way to develop global leaders, who are scarce resources, to achieve a company's global strategies.

France: High-potential employees are nurtured – in ways other than pay – mainly through career pathing and global mobility. For example, in addition to a 5% pay increase, a high-potential employee will also be offered career development and national/international mobility opportunities.

Germany: The focus is on total rewards, especially increased job responsibilities, career development and, if possible, career opportunities.

GCC: In this region, trends are changing for the longer-term retention of employees. The primary focus is on investing in people through talent development – that is, offering employees opportunities for development and growth. At the same time, there is a growing trend toward short- and long-term incentives, with companies creating or seriously considering schemes (primarily cash-based). Also, the trend of not offering expatriate employees any form of pension benefits may change in the years ahead to help retain certain categories of employees.

Mexico: The most common practice used to retain high-potential employees is positioning them above the midpoint of the salary structure. In addition, we find that proportioning international assignments and providing accelerated career plans are common company practices.

UK: Businesses want to laser-guide money to the most deserving, such as high performers or those who are not paid competitively. There is pressure on income, given increased taxes for most and high inflation, although it's due to drop.

US: The risk of losing key employees is top of mind as the economy recovers and certain labor markets improve. And while non-monetary awards such as career development and training are effective in retaining employees, employers realize that top-performing employees may resent going another year without a pay increase. Companies will do well to balance all levers of total rewards and deliver holistic value propositions to their employees.

5. *Where will employers place their compensation investment bets in 2011?*

Summary:

Ensuring that people resources are optimized is a top priority for many organizations around the world. In response, careful and direct investments are being made in talent development, including training and career planning, and infrastructure – that is, processes to ensure equitable pay, track return on investment and assist line managers with decision making and employee conversations regarding remuneration.

Actions to consider:

- Ensure that your rewards strategy aligns with your business strategy.

- View your compensation program holistically to include career development, training and other intrinsic work factors (for example, work-life balance).

- Focus on retaining mission-critical talent and reward the talent most responsible for creating value for your organization.

- Use analytics to support human capital decision making; combine multiple sources of financial and HR data from systems, surveys and external benchmarks into a single view to help track, measure and monitor internal and external workforce trends and reward program effectiveness.

Country/region specifics:

Australia/New Zealand: Companies primarily want to maintain their market positioning through retaining and developing staff. Some are focusing additional spending on employee learning and development.

Canada: We expect that most leading employers will continue to spend more of their remuneration budgets on top performers. We also believe that 2011 should be the year to reassess base salary programs to ensure that the objectives are clear and that the salaries delivered are competitive and fair. After all, for most employees, their regular paycheck is the most immediate and tangible indication of how much their employer values them.

China: Organizations, including both multinationals and local companies, are funding leadership and talent development, and more are beginning to show interest in flex benefits and employee annuities (supplemental pension plans).

France: Smart investments are likely to be made in career planning and in short-term and long-term incentive pools.

Germany: Companies are focusing on job grading and market benchmarks to more effectively create a base pay budget. Many organizations also review their target-setting and bonus-allocation processes.

GCC: Companies are investing heavily in talent management, pay for performance and initiatives to develop the local workforce. By law, companies in Qatar or Abu Dhabi, for example, have to hire local nationals up to a certain percentage of their total workforce – which continues to increase. This is leading to competition for local talent and forcing companies to institute plans for development opportunities for such categories of employees. Meanwhile, the expatriate workforce is still abundant.

Japan: Companies are focusing on acquiring management talent for overseas operations. They are also investing more in leadership development for selected high-potential employees.

Mexico: We anticipate that employers will focus on high-potential employees, building critical skills, career development, work/life balance and variable compensation.

UK: Many organizations will focus on correcting a growing issue – inconsistent application of compensation budgets, a product of years of larger budgets and poor pay governance. Inconsistency means over and under spending, and both have a cost. It's also a significant barrier to increased transparency, which is a real goal for most companies. Many are showing a strong interest in emphasizing that HR\reward has a major role to play in managing expenses and risk.

US: In the US, it looks like the use of salary increases are back. However, employers will remain cautious about this investment, wisely focusing on salary increases as well as short- and long-term incentives for top performers and critical workforce segments. A cautious mindset regarding the economic recovery will continue to influence actions of both employers and employees in 2011. We continue to see the use of contract, part-time employees, and a trend in reduced hiring levels.


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