



UNCHANGING SALARY INCREASE BUDGETS HIGHLIGHT OPPORTUNITY TO MAXIMIZE ROI THROUGH BETTER DISTRIBUTION

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Current Situation

Annual compensation research from WorldatWork, The Conference Board, and Mercer Human Resources Consulting shows there has been little change in salary increase budget projections for the last three years. According to WorldatWork, even as the economy continues its slow recovery, salary increase budgets remain fairly steady at 3.0% and this continues to be “well below pre-recession level,” where the average budget was 3.9%. The Conference Board adds that with the labor market currently overcapacity and companies unable to raise prices, pressure is increasing to limit or even cut costs, especially labor costs.

In this environment, organizations can choose to accept the status quo and keep their compensation practices the same. However, Axiom believes organizations need to innovate in their compensation practices more so now than ever to attract and retain talent and save money simultaneously. There is an opportunity to be more strategic about how to distribute investments in compensation that can help the bottom line. Below are three ways we suggest organizations get more bang for their buck from their compensation programs.

Avenues for Optimization

Ensure Base Pay Increases Reflect True Performance Improvement

WorldatWork finds paying for performance through merit increases is three to five times more common than other types of pay increases. This type of salary increase results directly from performance management and assessment outcomes. Mercer asserts that salary increases for top-performing employees will typically be higher as organizations focus on retaining top talent.

WorldatWork survey data from the past four years shows that the difference between average performers and highly-rated performers is increasing; those that are highest rated on average received 152% more than mid-level performers. Subsequently, it is and will continue to be more difficult for organizations to appropriately compensate and retain top performers as organizations compete on salary for top talent. Organizations that are more stringent with their rating systems – that move away from a forced bell curve distribution of ratings – can be more selective about what qualifies as high-performing talent and are able to pay more than the mean for high performers (4.1%), at approximately 4.6% (Exhibit 4). Axiom believes that organizations that better delineate between performance levels and are more aggressive in reserving top ratings for truly exceptional performers may be able to more effectively redistribute their salary increase budgets. This redistribution can allow them to compensate talent at or above market level and reward high performers in critical roles with meaningful increases in pay. In addition, we also believe that annual performance standards may need to continuously increase; otherwise all employees will either be exited or rise to the top ratings, making performance differentiation difficult and potentially less meaningful and more difficult to reward.

Invest in Enhanced Financial and Non-Financial Reward Programs

Mercer asserts that organizations are beginning to invest more in employee engagement in an effort to target high potential candidates or those with critical skills. WorldatWork survey data shows that the percentage of organizations investing in these types of programs has been increasing since 2010 and continues to trend upward (Exhibit 5a & b). From a financial perspective, these programs include spot bonuses or project completion bonuses. Non-financial awards include sponsored conferences, professional development events, recognition awards and enriched job sharing/flexible hours. Variable pay budgets, often used to fund these programs, have also been on the rise since 2011 (more detailed information on variable pay budgets can be found through subscription to WorldatWork survey data). Axiom finds that incentives can be useful to reward employees for achieving excellent short-term results closer to the time of achievement, not necessarily when they materially increase an employee's level of capability or competence, as has been the traditional practice. As these programs become more prevalent, organizations can expect talent to look for rewards outside of base salary increases throughout the year as high-quality work is completed.

Link Pay to Significant Increases in Capability Rather Than Timing

According to WorldatWork, more than 95% of organizations report that pay increases are awarded every 12 months, with the average being close to 12 months. However, this historical trend has been changing. More organizations are reporting “15, 18 or 24 months between raises, causing the average time to increase” (Exhibit 6). A previous study released by Axiom in 2009 through WorldatWork's magazine *workspan* titled “Planning for the New Normal” foreshadowed organizations moving to a system where “salary adjustments... are linked to significant competency growth, promotion or significant labor market movement [and these adjustments will occur] less frequently than today's annual increases.” While organizations now seem to be moving in this direction, it is not yet the norm. However, Axiom believes that linking increases in pay to increases in capability or market value rather than timing should be considered in combination with other adjustments to compensation practices as a way to more closely link achievement of results to rewards. This may enable organizations to increase the amount of time between pay increases. Furthermore, with a redefined rating system, there may be cost savings available through base salary administration, even within today's limited budgets.

2014 Compensation Budget Projections

As a service to you, Axiom has aggregated recently released 2014 compensation planning data. We collected the latest data from WorldatWork, The Conference Board, and Mercer Human Resources Consulting studies, including projections for salary increase budgets, merit pay increase budgets, and salary structure movements for 2014. As this is early data, it is important to note that it is subject to change.

Salary increase budgets continue to remain relatively flat, on the trend of the past four years, at 3.0%. Organizations continue to emphasize pay for performance, or merit increases, as the largest allocation of the salary increase budget. However, organizations are showing indications of placing additional emphasis on targeting high potentials or those with critical skills by investing in employee engagement and rewards programs, both financial (spot bonuses, project completion bonuses) and non-financial (professional development, enriched job sharing/flexible hours).

Summarized below are actual 2013 and actual and projected 2014 salary increase budgets from three reputable survey sources. More detailed data are presented in the pages that follow.

Source	Actual 2013 Median Salary Increase Budget			Projected 2014 Median Salary Increase Budget		
	Non-exempt	Exempt Salaried	Executive	Non-exempt	Exempt Salaried	Executive
WorldatWork¹	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%
The Conference Board²	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%
Mercer³	2.8%			2.9%		

¹ "WorldatWork 2013-2014 Salary Budget Survey," July 2013. WorldatWork.

² "U.S. Salary Increase Budgets for 2014," June 2013. The Conference Board.

³ "Pay Increases for U.S. Employees Illustrate the "New Normal" by Staying the Course," July 2013. Mercer Human Resources Consulting.

WORLDATEWORK: 2013-2014 SALARY BUDGET SURVEY

1 | Salary Increase Budgets

- The median 2014 projected salary increase budget is 3.0% (includes companies who reported salary freezes) for all employee categories, showing no change from actual medians from 2012 or 2013.
 - 2013 is the fourth straight year the number of zero percent responses, or salary increase freezes, has declined.
 - Actual mean salary increase budgets by employee category have been increasing since 2011 and projections for 2014 show an increase for almost all categories from previous years' mean projections.

1a | 2012 – 2014 Salary Increase Budgets

U.S. Employee Category	Actual 2012		Projected 2013		Actual 2013		Projected 2014	
	Mean	Median	Mean	Median	Mean	Median	Mean	Median
Non-exempt Hourly	2.8%	3.0%	2.9%	3.0%	2.9%	3.0%	3.0%	3.0%
Non-exempt Salaried	2.9%	3.0%	3.0%	3.0%	2.9%	3.0%	3.1%	3.0%
Exempt	2.9%	3.0%	3.0%	3.0%	2.9%	3.0%	3.1%	3.0%
Executive	2.8%	3.0%	3.0%	3.0%	2.9%	3.0%	3.1%	3.0%

1b | Salary Increase Budgets by Location

- Median salary increase budgets do not deviate by metropolitan location. Additional location data is available through subscription to survey data through WorldatWork.
 - Mean salary increase budgets in Boston, Dallas, Los Angeles, and San Francisco have increased notably from 2012 to 2013 and are projected to remain constant or continue to grow in 2014.

Location	Actual 2013		Projected 2014	
	Mean	Median	Mean	Median
Atlanta	2.9%	3.0%	3.0%	3.0%
Boston	2.9%	3.0%	3.1%	3.0%
Chicago	2.9%	3.0%	3.1%	3.0%
Dallas	3.0%	3.0%	3.1%	3.0%
Houston	3.1%	3.0%	3.2%	3.0%
Los Angeles	3.1%	3.0%	3.2%	3.0%
New York	2.9%	3.0%	3.0%	3.0%
San Francisco	3.1%	3.0%	3.1%	3.0%
Washington, D.C.	2.9%	3.0%	3.0%	3.0%

2 | Median Salary Structure Adjustments

- The projected median salary structure movement is 2.0% for all employee categories for 2014.
- Projected medians have remained constant from 2012-2014.
- Mean salary structure adjustments have been increasing (with the exception of non-exempt salaried from 2012-2013) and are projected to continue to grow. (Detailed information from the “WorldatWork 2013-2014 Salary Budget Survey” is available at www.worldatwork.org.)

3 | Variable Pay

- 2014 projected median variable pay budgets as a percent of total payroll vary by employee category and are as follows:
 - Non-exempt Hourly and Non-exempt Salaried Employees: 5.0%
 - Exempt Employees: 12.0%
 - Executives: 35.0%
- These projections have remained steady since 2012 (2011 for non-exempt salaried employees).

4 | Pay Increases by Percentage of Employees Rated as High Performers

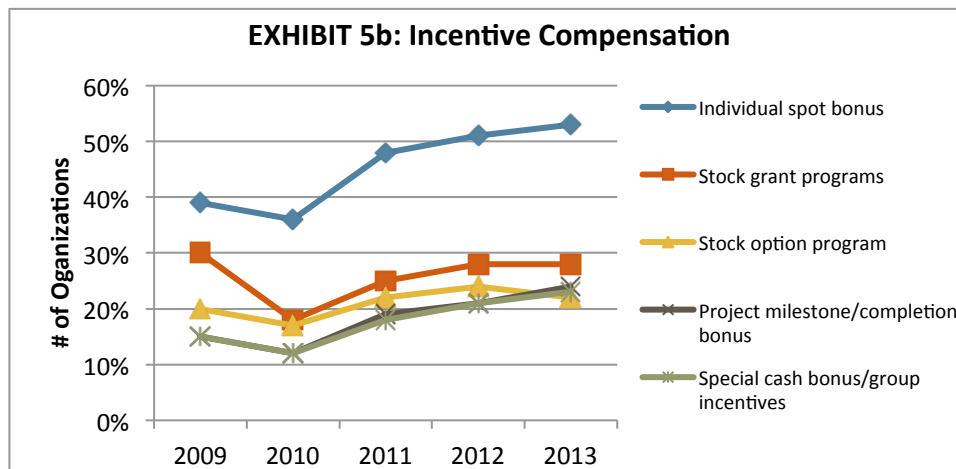
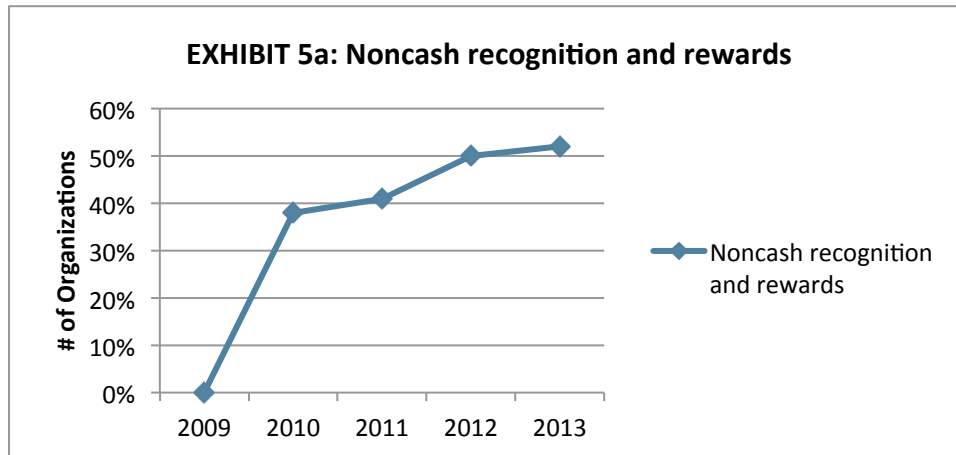
- High performers typically have pay increases 1.5x greater than middle performers. (Detailed information from the “WorldatWork 2013-2014 Salary Budget Survey” is available at www.worldatwork.org.)
- Organizations with a more concentrated percentage of high-rated employees can offer those high performers higher median pay increases.

Percent of employees rated as high performers in 2012	N	Mean	Median
Up to 10% of employees	311	4.6%	4.5%
11 to 15% of employees	164	4.3%	4.0%
16 to 24% of employees	227	4.3%	4.0%
25 to 29% of employees	139	4.2%	4.0%
30% or more of employees	483	3.8%	3.7%

5 | Noncash Rewards

Noncash rewards and incentive compensation for short-term results are on the rise while non-performance based compensation shows modest increases.

- Detailed information on incentive programs, including data on non-performance based compensation, is available through WorldatWork's subscription service.



6 | Number of Months between Pay Increases

- While the median number of months between pay increases remains constant, the mean is coming in higher than projected.

U.S. Employee Category	Actual 2012		Projected 2013		Actual 2013		Projected 2014	
	Mean	Median	Mean	Median	Mean	Median	Mean	Median
Non-exempt Hourly	12.7	12.0	12.3	12.0	12.6	12.0	12.1	12.0
Non-exempt Salaried	12.4	12.0	12.4	12.0	12.6	12.0	12.3	12.0
Exempt	12.7	12.0	12.4	12.0	12.6	12.0	12.2	12.0
Executive	13.1	12.0	12.7	12.0	12.9	12.0	12.4	12.0

THE CONFERENCE BOARD: “U.S. SALARY INCREASE BUDGETS FOR 2014”

7 | Salary Increase Budgets

- The median 2014 projected salary increase budget is 3.0% for all employee categories (includes companies who reported salary freezes).
- Median and 75th percentile projections for all employee categories remains almost the same as the 2013 increases, whereas the 25th percentile forecasts are slightly higher for each category.

7a | 2013 – 2014 Salary Increase Budgets by Employee Category

U.S. Employee Category	Actual 2013 Median Salary Increase Budget			Projected 2014 Median Salary Increase Budget		
	Median	25th Percentile	75th Percentile	Median	25th Percentile	75th Percentile
Non-exempt Hourly	3.0%	2.5%	3.0%	3.0%	2.75%	3.0%
Non-exempt Salaried	3.0%	2.6%	3.33%	3.0%	3.0%	3.3%
Exempt	3.0%	2.7%	3.3%	3.0%	3.0%	3.3%
Executive	3.0%	2.5%	3.25%	3.0%	3.0%	3.5%

- Salary increase budgets are composed of several compensation budget components such as merit, “across the board”/cost of living, and/or promotion and market adjustments.

7b | 2014 Salary Increase Budgets by Increase Type

U.S. Employee Category	2014 Projected Merit Increase Budget			2014 Projected General Increase Budget			2014 Projected Other Increase Budget (e.g. Promotions, Market Adjustments)		
	Median	25th Percentile	75th Percentile	Median	25th Percentile	75th Percentile	Median	25th Percentile	75th Percentile
Non-exempt Hourly	3.0%	2.5%	3.0%	0.25%	0.0%	2.65%	0.5%	0.0%	1.0%
Non-exempt Salaried	3.0%	2.5%	3.0%	0.0%	0.0%	3.0%	0.5%	0.0%	1.0%
Exempt	3.0%	2.5%	3.0%	0.0%	0.0%	2.75%	0.5%	0.0%	1.0%
Executive	3.0%	2.5%	3.0%	0.0%	0.0%	3.0%	0.5%	0.0%	1.0%

- These results suggest that most organizations are not making significant changes to their allocations, except in the general increase budget, where the median for non-exempt hourly employees has been unfrozen to 0.25% and across all employee categories in the 75th percentile.

8 | Salary Structure Movement

- Projections for 2014 salary structure movements are at a median of 2.0% for all employee groups, which was the same as the actual movement in both 2012 and 2013 for all groups.
- While these improvements have been modestly positive since 2010 (from 1.0% in all employee categories in 2010 but for Executives, which was 0.0%), it has and will continue to level off into 2014.

8a | 2013 – 2014 Salary Structure Movements by Employee Category

U.S. Employee Category	Actual 2013 Median Salary Increase			Projected 2014 Median Salary Increase		
	Median	25 th Percentile	75 th Percentile	Median	25 th Percentile	75 th Percentile
Non-exempt Hourly	2.0%	0.0%	2.0%	2.0%	1.6%	2.05%
Non-exempt Salaried	2.0%	0.0%	2.3%	2.0%	1.5%	2.2%
Exempt	2.0%	1.0%	2.25%	2.0%	1.7%	2.2%
Executive	2.0%	0.0%	2.25%	2.0%	1.5%	2.5%

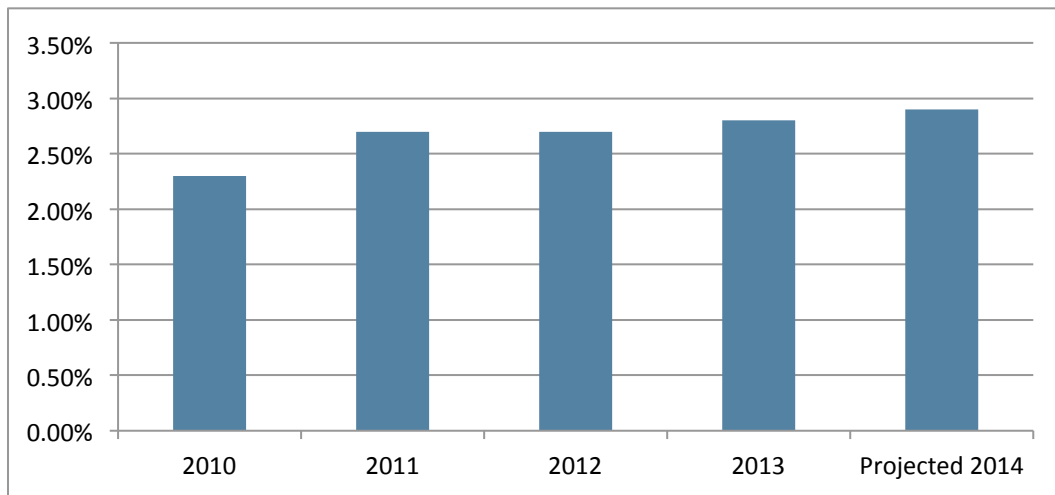
- 2013 salary structure movement projections and actuals at the median align at 2.0% while projections at both the 25th percentile and the 75th percentile came in lower (more so in the 25th percentile).
 - Projections for 2014 remain ambitious in the 25th percentile while the 75th percentile is more aligned with 2013 actuals.

MERCER: “PAY INCREASES FOR U.S. EMPLOYEES ILLUSTRATE THE ‘NEW NORMAL’ BY STAYING THE COURSE”

9 | Salary Increase Budgets

- The Projected Salary Increase Budget for 2014 is 2.9%, rising from 2.8% in 2013, and up from 2.7% in 2011 and 2012 (includes companies who reported salary freezes).
- Mercer indicates that salary increases for top-performing employees (7% of the workforce) will be higher as organizations focus on retaining top talent.

9a | 2010 – Projected 2014 Salary Increase Budgets



9b | Base Pay Increases as a Function of Performance

Rating	Percent of Workforce	Average Pay Increase
Highest-rated	7%	4.6%
Next highest-rated	30%	3.5%
Middle-rated	54%	2.6%
Low-rated	7%	0.9%
Lowest-rated	2%	0.2%

10 | Pay for Performance

- Organizations continue to invest in pay for performance; however, they are looking for ways to not only reward high performers but also high-potential employees or employees with critical skills.
 - Investing in employee engagement through enhanced reward programs is becoming a larger part of regular compensation practices (e.g., sponsored conferences, professional development events, additional non-financial recognition awards, and enriched job sharing/flexible hours) throughout the year.

About Axiom Consulting Partners

Axiom Consulting Partners works side-by-side with leaders to deliver pragmatic solutions that drive results. Our services help clients clarify strategy, focus on the highest priority sources of value and align their capabilities, processes and people to deliver sustainable, profitable growth. We always look at a client's challenges through the lenses of business strategy, organization design and talent management – it's why they choose us over firms that operate in just one of these disciplines.

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