

Pay Compression – What Did You Expect?

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Presented by
Effective Resources, Inc.

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The situation ...

- The economy is getting stronger
- Business is gaining momentum
- Competition for good employees remains strong – and will likely worsen in the years to come
- High uncertainty remains with minimum wage, indexing, and FLSA changes
- Salaries are growing at close to 3% - with some jobs moving much faster

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Salary trends ...

- Sign-on bonuses where there were none
- Employee referral bonuses where there were none
- Pay structures responding to both legal (min wage) and competitive pressures
- New employees hired at higher salaries than current employees

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The results ...

- Longer-term employees feel cheated and unappreciated
- Employees lose faith in management and find jobs elsewhere
- Or worse ... employees lose faith in management and stay
- Costs increase, morale drops, customer service falters, business suffers

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Expect pay compression ...

- If you hire without regard to current incumbents
- If you think your policies on privacy will hide salary decisions
- If you fail to routinely monitor salaries against an objective model
- If you believe your long-term employees won't move to a competitor

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Staying in control ...

- Do not hire an employee for more than the lowest paid competent performer
 - Exception: If the new hire will be clearly recognized by peers as superior, can hire at more than current employee(s)
- Note: Current employees hardly ever recognize superior talent ... and when they do, they seldom acknowledge it*

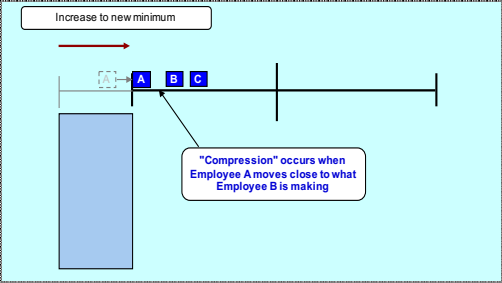
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Long-term best practices ...

- Method 1 (to address structure changes): The Wage Compression Triangle – simple, easy to understand, easy to administer
- Method 2 (to address wage compression from any cause): The 'Expected Rate' calculation – more demanding to calculate, more difficult to communicate, but more accurate when considering all factors

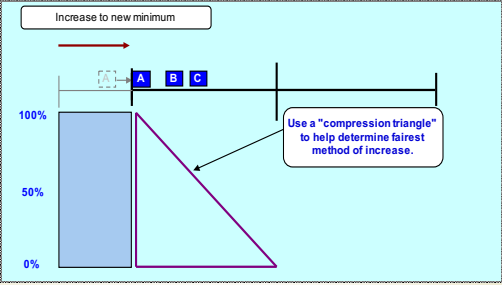
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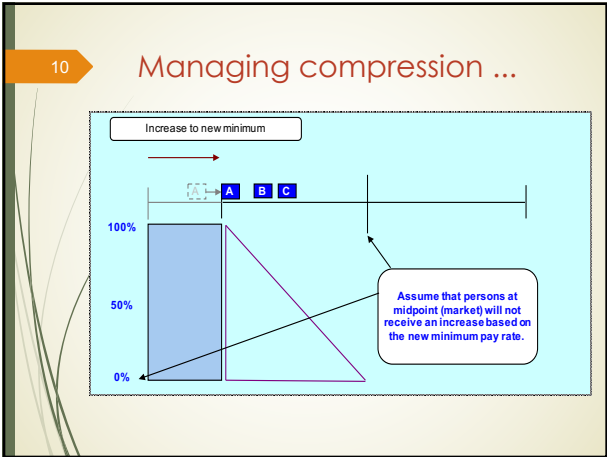
Lookout for compression ...

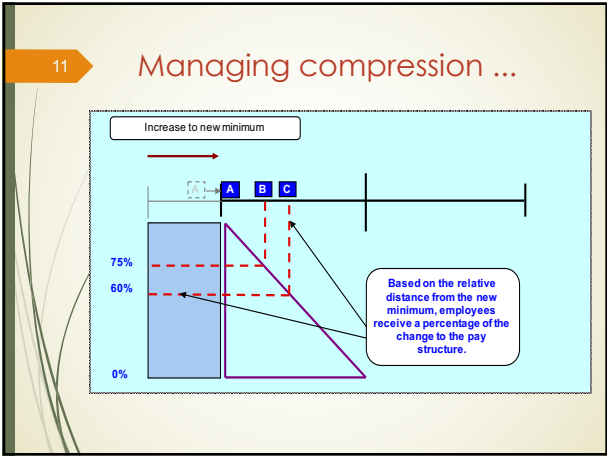


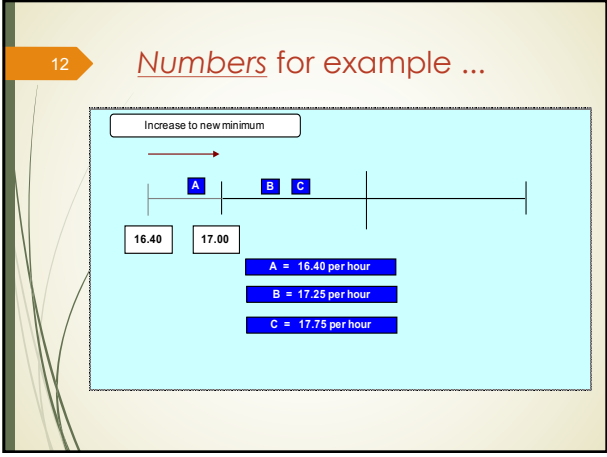
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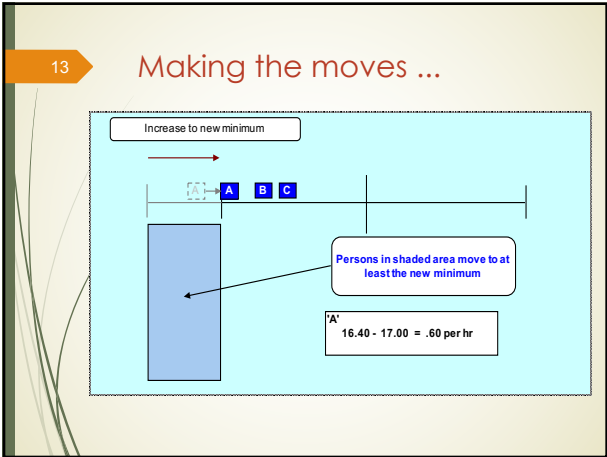
Managing compression ...

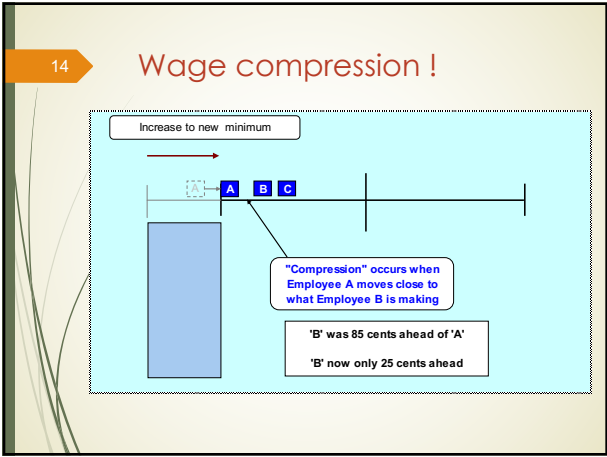


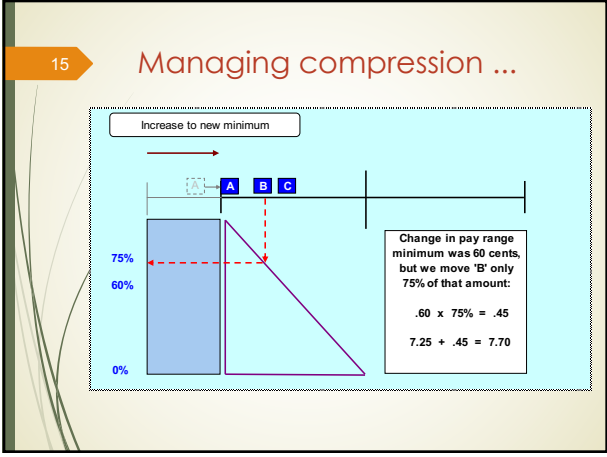


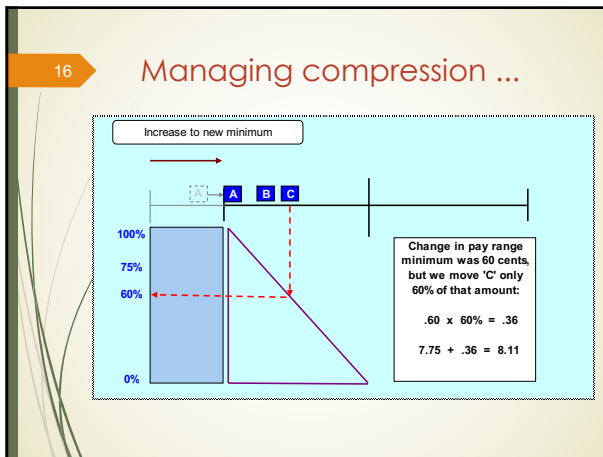


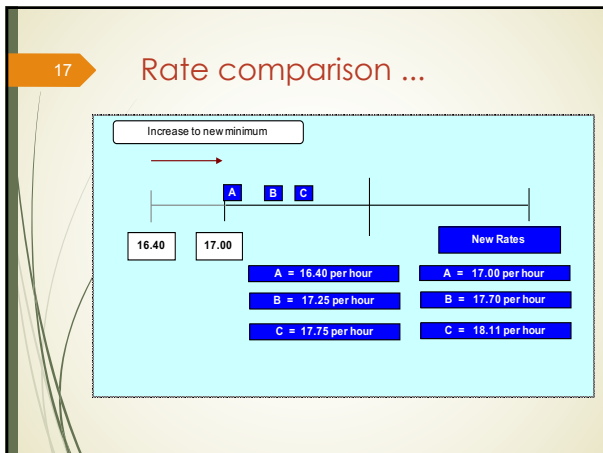


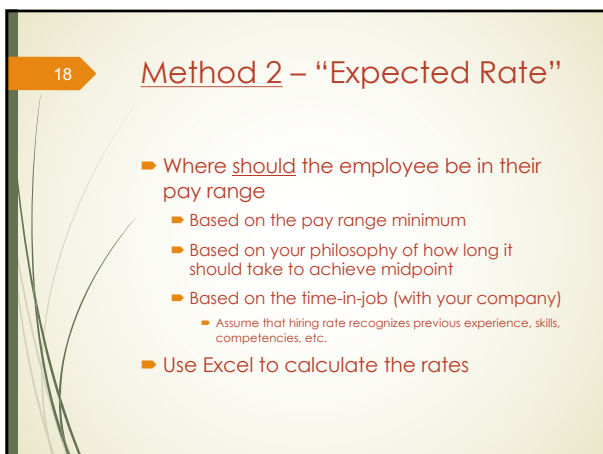












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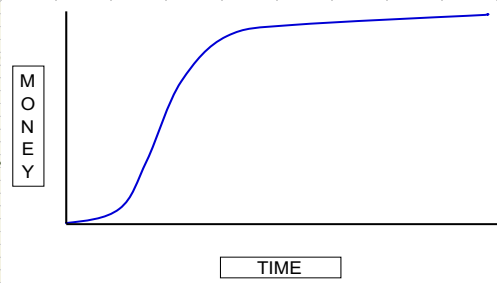
How long to midpoint ...

Question 1: "How long does it take for a qualified person to become fully competent in a given job?"

Question 2: "How long does it take to move from the hiring rate to the midpoint of your pay grade (or market)?"

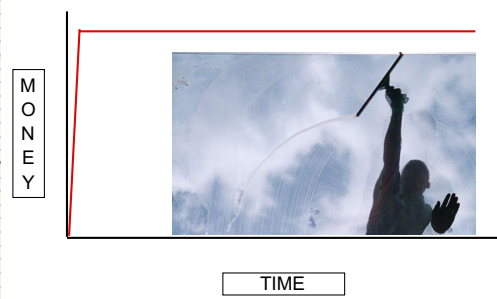
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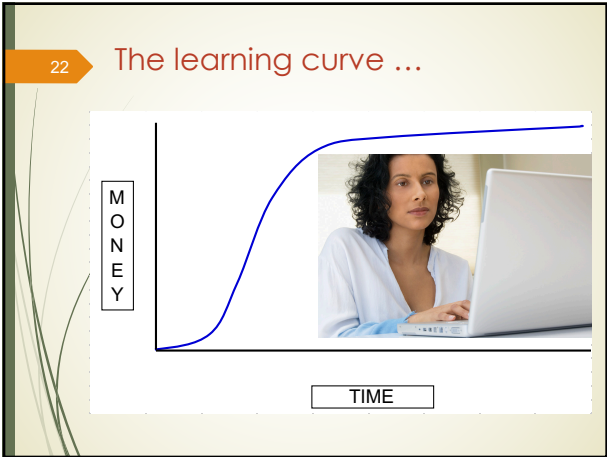
The learning curve ...

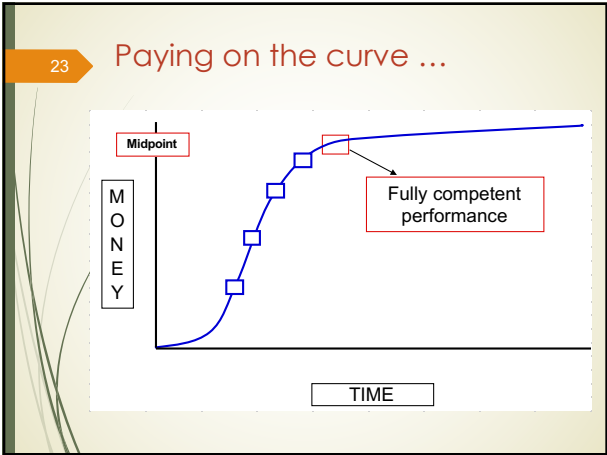


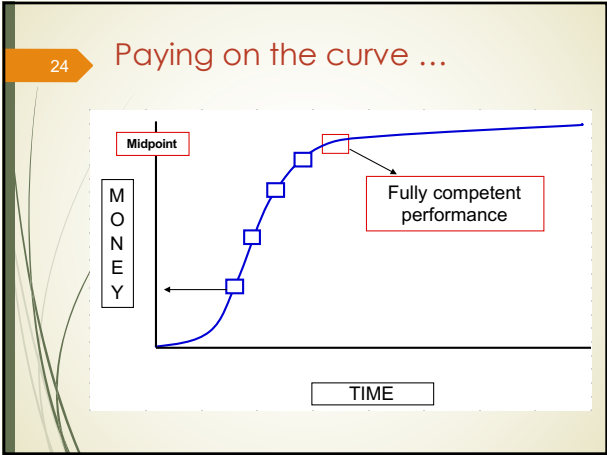
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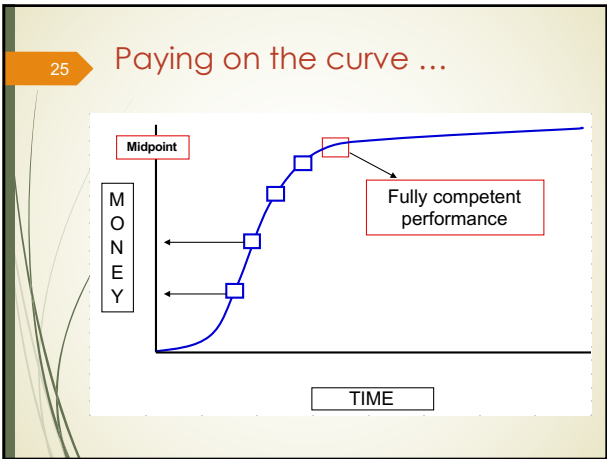
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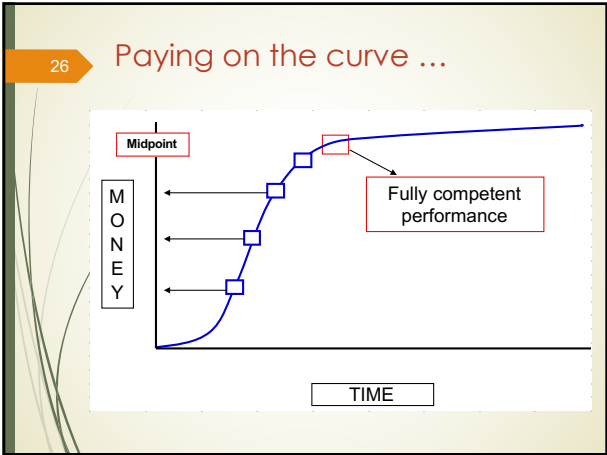


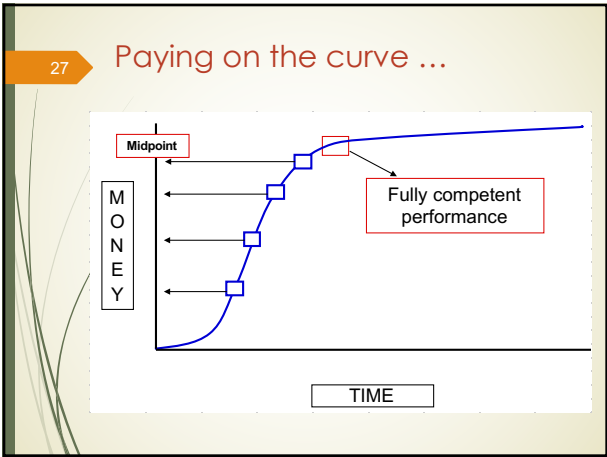


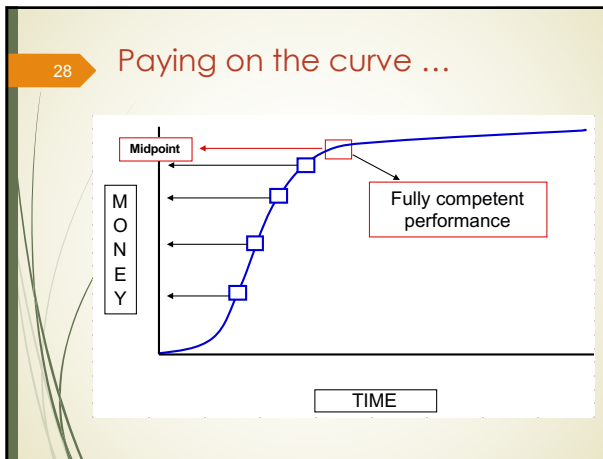


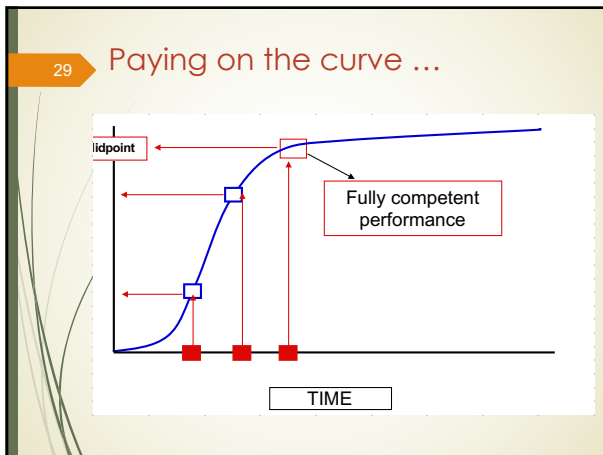













30 Critical questions ...

- Question 1: "How long does it take for a qualified person to become really good in a given job?"
- Question 2: "How long does it take to move from the hiring rate to the midpoint of your pay grade (or market)?"

If there is a difference of more than 18 months between Question 1 and 2, you've got high got turnover potential!



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32 Using the 'Expected Rate' ...

- Assume the following
 - Employee in job 2.5 yrs making \$33,000
 - Pay range: MIN \$ 28,500 MID \$35,625
 - Philosophy: get to Midpoint in 3 years
- Excel formula
 - $\text{ABS}(\text{FV}(7.7217\%, 2.5, , 28500))$
 - \$ 34,348.13

33 Market adjustments ...

- Expected Rate v. Current Rate
- Using previous example
 - Exp Rate: \$34,348.13
 - Employee rate: \$33,000
 - Market Adj = \$1,348.13
- These adjustments should be merit based and, if very large, should be spread over 12-24 months to stay within budget restraints

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Eliminating pay compression

- Use the “hiring range” (i.e., don’t hire at more than lowest paid competent peer)
- Hire the best people you can afford, not the best people you can find
- Plan on possible compression when structures change – and, *budget* for it
- Identify compression issues and fix them even if over 2 or 3 years

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Gaining approval ...

- Calculate the cost of turnover
- Gather facts from line management on the effects of turnover
- Calculate the increases necessary and provide at least one or two options to spread costs over a period of time
- Build a business case for the increases

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Questions ?



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