

## SPOTLIGHT

# Wage Growth in 2010: HR Professionals Face Tough Choices

It has taken more than two years, but many employers are finally in a position to add workers to their ranks. With productivity rising for the past several months in the manufacturing sector and demand returning in the service industry, there are plenty of signs that the U.S. economy is emerging from its downturn, albeit at a very slow pace. What remains to be seen is whether compensation will make a similar recovery after a dismal 2009, when countless companies cut or froze salaries for their workers.

Some current data show that wage growth will improve in 2010, but it will not make great strides compared with recent years. In those companies that are raising salaries in 2010, workers' wages will increase by an average of 2.2%, according to SHRM's 2010 Human Capital Benchmarking Survey. This represents a slight increase from 1.9% in 2009, but below average increases of 3.7% and 3.6% in 2007 and 2008, respectively.

Some of the U.S. labor force's largest industries are not veering far from the average salary increase for 2010, according to SHRM's Benchmarking Service. Manufacturing-sector companies plan to raise salaries by an average of 2.1%, service-industry companies are budgeting for a 2.4% average increase and members of the health care industry are planning to raise salaries by an average of 2.2% in 2010.

Joan Reutter, president of Manassas, Va.-based human resource consulting company JBR Consulting and member of SHRM's Total Rewards/Compensation and Benefits Special Expertise Panel, says many companies are still skittish about distributing more money for paychecks. Reutter's company

handles a variety of for-profit and nonprofit clients.

"A lot of companies are still checking out the going rates for compensation before they make any decisions," Reutter says. "They may not have given any increases last year, and they're still wondering how to reward performance on such a small budget. When you only have two to three percent to spend, at the end of the day, when taxes are taken out, there's not a lot to show for it."

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JBR Consulting*

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## Did you know?

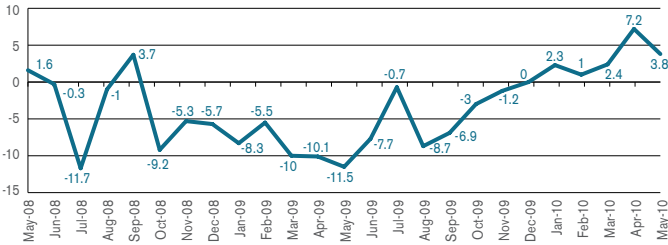
33% of companies planned to freeze employee wage increases if economic challenges continued to exist in the first half of 2010.

*SHRM Poll: Financial Challenges to the U.S. and Global Economy (January 2010)*

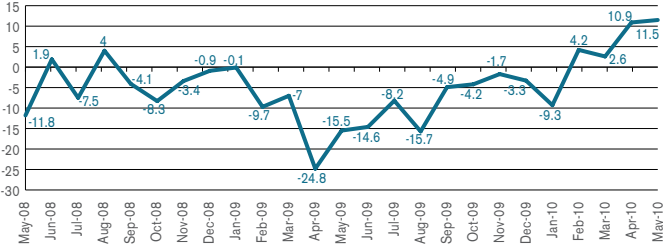
Other data show that while compensation levels remained flat through much of the recession, some employers are starting to open up their wallets. In every month in 2009, the rate of increase for new-hire compensation fell on an annual basis, according to the SHRM Leading Indicators of National Employment (LINE) report. The report tracks hiring and compensation trends in the manufacturing and service industries. But from February to May 2010, the year-over-year rate of increase for new-hire compensation rose every month in both sectors. The trend is positive, but few employers in both sectors are actually raising wages and benefits, and the majority of the survey's respondents are still keeping compensation packages flat.

Metric	2007	2008	2009	2010	Percent Change 2007 to 2010	Percent Change 2008 to 2009	Percent Change 2009 to 2010
<b>Compensation Data</b>							
Annual salary increase	3.7%	3.6%	1.9%	2.2%	40.5%	-47.2%	15.8%
Target bonus percentage, nonexecutives	10.1%	4.3%	3.3%	3.1%	-69.3%	-23.3%	-6.1%
Target bonus percentage, executives	22.5%	11.8%	9.6%	7.4%	-67.1%	-18.6%	-22.9%

### Annual Change in Rate of Increase for New-Hire Compensation, Manufacturing Sector



### Annual Change in Rate of Increase for New-Hire Compensation, Service Sector



## Did you know?

35% of HR professionals said their companies' overall financial health was in a mild recovery in early 2010 compared with the same period in 2009.

*SHRM Poll: Post-Recession Hiring (March 2010)*

Federal data also reveal that wages are making incremental gains in 2010. The U.S. Bureau of Labor Statistics' Employment Cost Index (ECI) showed that in the first quarter of 2010, wages and salaries for all workers rose by 0.4% from the previous quarter. Just one year prior, in the first quarter of 2009, wages and salaries increased a mere 0.3%—an all-time low since BLS began recording the data in 1975.

Personal income actually increased \$54.4 billion in April 2010, or up 0.4% from March, according to the U.S. Bureau of Economic Analysis. But the rise in dollars paid out to workers was probably more a function of job creation in the U.S. labor force rather than an increase in actual salaries. The bureau's report also showed that personal saving (as a percentage of disposable personal income) was 3.6% in April, up from 3.1% in March. That shows that while many workers are earning paychecks once again and perhaps earning more money, they are also saving more money. That scenario has many economists worried, since the fiscal recovery of the United States will depend largely on consumer spending, which accounts for about two-thirds of economic activity.

### Many employers still struggling to meet budgets due to economic conditions

As long as the U.S. economy continues to expand at its current rate of around 3% or 3.5% each quarter, it is not likely to translate into commensurate increases in wages and salaries. In the field of higher education, for example,

many employers cannot afford sizable salary hikes this year due to persistent weakened economic conditions, says Linda Lulli, associate vice president of human resources at Bryant University and member of SHRM's Total Rewards/Compensation and Benefits Special Expertise Panel. Some schools are struggling to find the money for 1% or 1.5% raises, she says.

Consequently, many colleges and universities are exploring retirement incentives for long-tenured staff members as a means of controlling wage costs, Lulli says. The loss of experienced staff, while not entirely favorable, removes high salaries from the books and can create a "healthy level of transformation" in the higher education workforce, she says.

And with economic conditions still unsettled, employers are taking new tacks with compensation packages for their workers, she says. At Bryant in 2009, for example, the school froze its annual salary increases but ended up providing a partial lump-sum payment to workers at the end of the year as a means of offsetting the losses from the salary freeze.

"When we can't give the desired level of a salary increase, we try other things," Lulli says. "One time we gave some people extra days off in lieu of the increase. That was received very well."

## Did you know?

18% of companies reduced employee work hours with a reduction in pay during the last half of 2009.

*SHRM Poll: Financial Challenges to the U.S. and Global Economy (January 2010)*

On a global level, other nations are in better shape than the United States, despite recent improvements in domestic economy. China and India have enjoyed strong growth in gross domestic product in late 2009 and early 2010, and companies there are expected to reward their workers: salaries will rise by an average of 6.3% in India in 2010 and by an average of 4.5% in China this year, according to a recent survey by Hewitt Associates, a global HR consulting and outsourcing company.

Wages are also likely to jump higher in the near future in developing nations in Africa and the Middle East, says Warren Heaps, partner at The Birches Group LLC, an international compensation consulting firm.

Heaps says gross domestic product is expected to grow an average of 4.25% in 2010 in the Middle East and 4% in Africa, both slightly ahead of U.S. projections of 2.5% to 3%.

"One thing is very clear," Heaps says. "The impact of the global recession is being felt in the developing world. But when the recovery comes, it will be more pronounced in these places, these 'second-tier' economies. Obviously, when

you start smaller, you're going to get bigger percentage growth. As economies improve in these locations, they will become more developed and more robust."

Based on conversations with clients, Heaps says a growing number of technology companies and other interests are exploring opportunities in sub-Saharan Africa and Central America. Wages in these countries are generally low compared with other nations, but market demand for labor could help to raise compensation.

"These companies are being forced to put people on the ground in these areas," Heaps says. "They tend to be based on natural resources, infrastructure, banks and consumer products like mobile phones. Many of these companies are saying, 'Well, we've done all we can in Asia, now let's go to Central America.' They're following their future clients."

### More scrutiny will be focused on executives' salaries in the future

In the future, HR professionals may want to look closer at the CEO's office when preparing their salary budgets. Executives' paychecks drew the attention of President Obama and various lawmakers in 2009, after large bonuses and highly lucrative compensation packages were doled out to the heads of Wall Street firms whose practices had a hand in the economic downturn. Part of the financial reform bill that was approved by the U.S. Senate in May included a requirement for "clawback provisions" in the compensation contracts for CEOs, which forces executives to repay any earnings that were based on inaccurate financial statements.

Some companies are already moving to rein in executive pay. The target bonus percentage paid to executives—based on their salary—was an average of 7.4% in 2010, down from 9.6% in 2009 and far below the average 22.5% handed out in 2007, according to SHRM's 2010 Human Capital Benchmarking Survey.

At a recent forum sponsored by the Economic Policy Institute (EPI), a Washington, D.C.-based think tank, various academics debated whether executive pay packages need to be restructured.

"Executive compensation is a highly controversial topic," says Alex Edmans, assistant professor of finance at the University of Pennsylvania's Wharton School. "No one complains if a CEO is paid well and they've added a lot of value to the firm. On the flip side, some CEOs destroy the value of some companies and walk away with a lot of pay."

Edmans says that while it is not necessarily wrong for CEOs to be well-paid, their incentive packages need to be restructured. Most CEOs get guaranteed bonuses, regardless of their performance, and the bulk of CEOs' incentives come from changes in previously granted stock options. The

timing of these incentives is also misguided, he says—for example, a CEO's stock options will not be as lucrative when the company's stock is down during a downturn, and that's a time when the CEO's leadership is needed the most.

"The level of incentives is generally sufficient, but the incentives are low at the wrong times," Edmans says. "They allow CEOs to cash out early."

Robert Frank, a professor of management and economics at Cornell University, disagrees. Frank says heightened levels of executive pay are simply a reflection of today's ultra-competitive business world.

One Harvard study showed that the average CEO made a salary 44 times that of an average worker in 1980. In 2007, CEOs earned 344 times the salary of an average worker, but the exponential jump in compensation isn't the result of a rise in greed or wrongdoing, Frank says.

"The ratio has gotten so much bigger not because malfeasance has increased," Frank says. "Competition has increased. The stakes are higher now, and it's a free agent market for CEOs, in effect."

Among other classes of workers, however, competition is still not that fierce. A recent estimate by EPI indicated that there are 5.6 unemployed persons per each job opening in the U.S. labor force. That means employers still have the advantage when negotiating salaries for new hires or workers who are due for an annual salary review.

But there is a danger in keeping salary budgets too tight, says Reutter, of JBR Consulting. When the economy improves and job opportunities increase, workers will have greater confidence to take their talents elsewhere.

"In the past, companies were reluctant not to give raises to all of their employees," she says. "Now they're saying, 'What should we do to keep the most talented workers?' It might not be the best approach [to limit salary growth]. You may need to spend the money in order to keep your best people."

In short, selective wage increases—rather than uniform salary hikes for all workers—may be the norm for the near future, even as the U.S. economy makes small gains and hiring begins to improve.

## Sources

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