

Will “Non-Guaranteed” Merit Increases Become the New Normal?

Those were the days. Not too long ago, it was a foregone conclusion that every year a salary bump was not only anticipated but expected. Do I hear Archie and Edith Bunker tinkling the ivories? Have we said good-bye to those days? And if yes, is the departure a permanent one, or a temporary state of affairs as a result of the economic downturn?

According to all reports, both merit increase budgets and annual bonus funding are down in 2009. The projected merit increases that companies had planned for 2009 were reduced sharply. In February, merit budgets were projected to be only 1.5%¹ which is well below the 3.5% average raise employees received in both 2007¹ and 2008¹. As the recession worsened, more companies planned zero merit increases; by April, two in five companies eliminated merit increases altogether¹. Our two proprietary surveys confirmed this trend:

- In our *2009 Compensation Trends Survey* which targeted business process outsourcing companies, we found that the average planned merit increase for 2009 was 2.3% for all employees (and 3.3% for those companies planning to provide increases), while the actual merit increase average was only 1.2%.
- Our survey that targets the tech sector, the *2009 Global Inside Sales Compensation Survey* indicated a similar trend. For those companies providing increases, North American companies planned a 3.2% salary budget increase for 2009, but only implemented a 2.3% increase when the time came. On average, including companies that provided no increases, the picture is more dismal with an average of only 0.6%.

So we acknowledge that companies scaled back on merit increases, but in what volume?

- Our *2009 Compensation Trends Survey* found that 71% of companies *planned* to give merit increases to the all employee group, but only 45% *actually* gave them.
- Our *2009 Global Inside Sales Compensation Survey* shows 43% of North American companies *planned* salary budget increases, but only 25% *actually* implemented them.

Of course these statistics are not constant across all industries. Some fared better than others¹.

- The utilities and energy industries saw the highest increases in salaries and total cash compensation, at 3.3% and 4.6% respectively.
- IT and E-Commerce Development industries also scored fairly well, with salary increase averages at 2.7% and total cash compensation rising 2.8%.
- The insurance industry fared the worst, with the lowest salary and total cash compensation increases at 2.5% and 1.7% respectively.

In addition to smaller merit increases, many companies implemented a salary freeze to reduce escalating payroll costs and in some instances eliminate the need for layoffs. Our *2009 Global Inside Sales Compensation Survey* found that 61% of companies indicated they were implementing salary freezes in their North American Markets, and 60% in other global mature markets such as Western Europe. Only two companies in our survey indicated that they were actually reducing salaries.

¹ “US Strategic Rewards Report, 2009/2010”, Watson Wyatt

However, we seem to be in a thawing-out phase:

- 33% of employers who froze salaries plan to unfreeze them within the next six months, which is up from 17% two months ago¹.
- 44% plan to roll back salary cuts in the next six months, which is up from 30% two months ago¹.
- 24% of employers plan to reverse reductions to 401(k) match contributions in the next six months, up from 5% in June¹.

The following table summarizes the findings of three surveys² and includes average planned 2009 salary increases, actual 2009 salary increases and projected increases for 2010.

- The consistent trend is that actual and projected salary increases are significantly lower than the 3.49% average increase initially projected for 2009.
- Executive increases were lower than all other employee groups, something that has rarely been seen.

Salary Increase Averages

Employee Group	Planned 2009	Actual 2009	Projected 2010
All Employees	3.49%	1.93%	2.73%
Executive	3.65%	1.83%	2.73%
Management	3.10%	2.20%	2.80%
Exempt Salaried	3.50%	2.07%	2.77%
Nonexempt Salaried	3.45%	2.07%	2.70%
Nonexempt Hourly Non-Union	3.80%	2.20%	2.73%
Nonexempt Hourly Union	–	2.20%	2.70%

Is it possible there is a silver lining among all of these clouds? The answer is yes...and no. In addition to the indications of the lifting of salary freezes and roll-backs of salary cuts:

- The CEO Confidence Index has nearly doubled to 77.4 in August from its historical low of 39, reached in February, 2009; however, while the Employment Condition Index increased 16%, climbing to 57.0, 93% of CEOs continue to rate employment conditions as “bad”³.
- Companies with limited merit increase budgets have ensured that the increases go to employees who exceed expectations - employers are cutting back merit increases for poor performers and funding salary increases for top performers. High performers received an average increase of 4%, though this increase was still down from the 2008 average of 5.25%¹.
- As the chart above shows, salary increases are projected to be on the rise; while this is good news for employees – it may be too soon to count on a guaranteed annual salary increase.

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¹ “2009/2010 US Salary Budget Survey”, Watson Wyatt.

² “2009/2010 Salary Budget Survey, World at Work”; “2009/2010 US Salary Budget Survey”, Watson Wyatt; “Historical Overall US Salary Increase Budgets”, Hewitt Associates; All statistics include zeros.

³ “CEO Confidence Index”, August 2009, Chief Executive Magazine.