MERCER’S 2017 COMPENSATION PLANNING AND PERFORMANCE MANAGEMENT WEBCAST

GETTING IT RIGHT: SALARY AND PERFORMANCE MANAGEMENT RE-BOOT
TODAY’S DISCUSSION

1. INSIGHTS FROM THE SURVEY

2. HOT TOPIC: PERFORMANCE MANAGEMENT
INSIGHTS FROM THE SURVEY
THIS YEAR’S SURVEY

INDUSTRY BREAKDOWN
- Services Non-Financial: 22%
- Energy: 17%
- Retail & Wholesale: 8%
- Consumer Goods: 7%
- Other Non-Manufacturing: 7%
- High-Tech: 6%
- Other: 26%

NUMBER OF EMPLOYEES
- 5,000 and over: 18%
- 1,000–2,999: 27%
- 300–999: 13%
- 100–299: 13%
- LESS THAN 100 EMPLOYEES: 13%

300–499: 8%
CHALLENGES FACING ORGANIZATIONS TODAY

- Economic Uncertainty
- Multi-generational Workforce
- Competition from Emerging Markets
- Disruptive Technology
- Cost Reduction Initiatives
- Automation & Machine Learning
FACTORS INFLUENCING YOUR BUDGET IN 2017

- Overall Economic Climate
- Retention Concerns
- Attraction Concerns
- Strengthen performance culture / pay-for-performance
- Employee Engagement Concerns
- Career Mobility / Advancement

Multiple responses were allowed
### Results from This Year’s Survey

<table>
<thead>
<tr>
<th></th>
<th>2016 Fall Projection</th>
<th>2016 Actual</th>
<th>2017 Projection</th>
</tr>
</thead>
<tbody>
<tr>
<td>Excludes Freezes</td>
<td>2.6%</td>
<td>2.5%</td>
<td>2.6%</td>
</tr>
<tr>
<td>Includes Freezes</td>
<td>2.2%</td>
<td>2.1%</td>
<td>2.3%</td>
</tr>
</tbody>
</table>

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# Changes in Salary Budgets
## Primary Reasons for Change

<table>
<thead>
<tr>
<th>Projected 2017 lower than Actual 2016</th>
<th>Projected 2017 higher than Actual 2016</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>56%</strong> Response to economic uncertainty or general cost reduction initiative</td>
<td><strong>38%</strong> Account for salary freeze/delayed increase in previous years</td>
</tr>
<tr>
<td><strong>17%</strong> Business/industry performance weaker than expected</td>
<td><strong>22%</strong> Response to economic improvement</td>
</tr>
<tr>
<td><strong>8%</strong> Change in business strategy or competitive positioning to market</td>
<td><strong>20%</strong> Change in business strategy or competitive positioning to market</td>
</tr>
<tr>
<td><strong>8%</strong> Response to commodity prices</td>
<td><strong>5%</strong> Greater competition or anticipated labour shortages</td>
</tr>
</tbody>
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BALANCED INCREASES ACROSS THE COUNTRY
2017 PROJECTED SALARY INCREASES

- Territories: 2.5%
- Greater Edmonton: 2.7%
- Greater Calgary: 2.5%
- Greater Vancouver: 2.5%
- Saskatchewan: 2.5%
- Greater Montreal: 2.6%
- Other Quebec: 2.5%
- Other Alberta: 2.5%
- National Capital Region: 2.6%
- Greater Toronto: 2.6%
- Other British Columbia: 2.5%
- Other Ontario: 2.5%
- Manitoba: 2.5%
- Atlantic Canada: 2.5%

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AND NOW BY INDUSTRY
2017 PROJECTED SALARY INCREASES

- Consumer Goods: 2.8%
- Financial Services: 2.6%
- Other Manufacturing: 2.6%
- Mining: 2.6%
- Services Non-Financial: 2.6%
- High Tech: 2.5%
- Insurance: 2.5%
- Retail: 2.4%
- Energy: 2.4%
- Public Sector: 2.4%
SALARY FREEZES BY EMPLOYEE LEVEL

% Org’s Freezing

- Executive
  - 2015
  - 2016
  - Projected 2017

- Management
  - 2015
  - 2016
  - Projected 2017

- Professional
  - 2015
  - 2016
  - Projected 2017
Projected base salary structure adjustment in 2017

Top employees can expect to receive a salary increase 1.8x higher than average performers

Average promotional increase across all employee groups in 2016 – lower than 2015
**SMALL INCREASES CAUSING PRESSURE ON OTHER HR PROGRAMS**

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>JOB EVALUATION</td>
<td>PROMOTIONS</td>
</tr>
<tr>
<td>MANAGER SKILLS</td>
<td>PERFORMANCE MANAGEMENT</td>
</tr>
</tbody>
</table>
#1 **DISTRIBUTE THE BUDGET EVENLY ACROSS ALL EMPLOYEES**

<table>
<thead>
<tr>
<th>Why?</th>
<th>Why not?</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Easy to administer</td>
<td>• Perpetuates internal inequities</td>
</tr>
<tr>
<td>• Especially if your merit matrix is “broken”</td>
<td>• Higher chance of turnover from top performers</td>
</tr>
<tr>
<td>• Encourages a team-based culture</td>
<td>• Strongly counters existing company culture</td>
</tr>
</tbody>
</table>
## Strategies for a Smaller Budget

### Eliminate the Base Salary Increase for the Majority

<table>
<thead>
<tr>
<th>Why?</th>
<th>Why not?</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Focus on the top performers – the employees you want to retain</td>
<td>• Problematic for companies who are unable to identify top performers</td>
</tr>
<tr>
<td>• Opportunity to make some salary corrections</td>
<td>• Works at the expense of the morale and engagement of the broader employee population</td>
</tr>
<tr>
<td>• Strategizes budget spending</td>
<td></td>
</tr>
</tbody>
</table>
## Strategies for a Smaller Budget

### Focus on the Broader Employee Value Proposition

<table>
<thead>
<tr>
<th>Why?</th>
<th>Why not?</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Opportunity to focus on all the other “good stuff”</td>
<td>• If you haven’t thought strategically about this, it requires a lot of work!</td>
</tr>
<tr>
<td>• Money alone will likely not retain employees</td>
<td>• Pay-for-performance may be an important part of your EVP – need to have other avenues to reward performance</td>
</tr>
<tr>
<td>• Potential to increase employee engagement and morale</td>
<td></td>
</tr>
</tbody>
</table>
STRATEGIES FOR A SMALLER BUDGET

#1 DISTRIBUTE THE BUDGET EVENLY ACROSS ALL EMPLOYEES

#2 ELIMINATE THE BASE SALARY INCREASE FOR THE MAJORITY

#3 FOCUS ON THE BROADER EMPLOYEE VALUE PROPOSITION
PERFORMANCE MANAGEMENT
ESTABLISHING AN EFFECTIVE APPROACH
STATE OF PERFORMANCE MANAGEMENT
HEADLINE MARKET PRACTICES
ROOT ISSUES
MAXIMIZING THE EFFECTIVENESS OF PERFORMANCE MANAGEMENT
PERFORMANCE MANAGEMENT
NOT A DIFFERENTIATOR FOR MOST

77%
 Implemented one size fits all

89%
 Link employee pay and the performance rating

95%
 Set individual goals

86%
 Evaluate behaviours / competencies

57%
 Use a 5-point rating scale

89%
 Have overall performance ratings
## High Dissatisfaction with Performance Management

<table>
<thead>
<tr>
<th>Percentage</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>3%</td>
<td>Percentage of employers that believe their performance management system needs further work to be effective</td>
</tr>
<tr>
<td>48%</td>
<td>Percentage of employers that believe their performance management system delivers exceptional value</td>
</tr>
<tr>
<td>90%</td>
<td>Percentage of Heads of HR that believe their performance management system does not yield accurate information</td>
</tr>
<tr>
<td>95%</td>
<td>Percentage of managers dissatisfied with their organization’s performance management system</td>
</tr>
</tbody>
</table>

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HEADLINE MARKET PRACTICES VS. THE BOTTOM LINE

ELIMINATING PERFORMANCE RATINGS
Bottom Line - Companies that eliminated ratings still assess performance using multiple performance factors, and use these to make pay decisions.

CONTINUOUS FEEDBACK
Bottom Line - Creating a “feedback rich culture” remains a challenge for all organizations, requiring on-going sponsorship, training, tools and engagement – but technology can be an enabler.

ELIMINATING ANNUAL MERIT INCREASES
Bottom Line - Even with some companies considering eliminating annual merit increases, it is likely that pay for performance will stay, with an increased emphasis on variable pay.

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POTENTIAL ROOT ISSUES

Goal-setting
- Unclear expectations
- Lack of defined goals/wrong goals

Coaching
- Lack of focus on career development
- Lack of transparency

Feedback
- Not enough feedback
- Feedback intervals are too spread out

Rating
- Inconsistent process year-to-year
- Not enough effort put into performance reviews

Notes: 2015 data updated as of May 24, 2015. Non-Consulting Communications, Global Mobility and IS data not included.
ELIMINATING PERFORMANCE RATINGS?

THINK TWICE
1. Employees use their assigned rating as a proxy for where they stand
2. Employees believe a rating is an effective way to drive pay decisions

THERE IS STILL WORK WITHOUT RATINGS
Organizations without ratings still make performance-based pay decisions, relying on manager discretion, calibration committees, various performance metrics, or a combination of these assessment methods to deliver base salary and/or incentive pay.

IT CAN WORK
In a no-rating environment, an organization with fruitful discussions about goals, performance and development can easily communicate to employees about where they stand.
MAXIMIZING THE EFFECTIVENESS OF PERFORMANCE MANAGEMENT

#1 FOCUS DIALOGUE
Establish the right goals first, then talk about development

#2 REALLOCATE TIME
Reducing year-end focus in favor of ongoing engagement

#3 KEEP SCORE
Measure the effectiveness of your performance management strategy

#4 REWARD STRONG LEADERS
Provide higher base pay for consistently strong people managers
#1 - FOCUS DIALOGUE

Establish the right goals first, then talk about development

<table>
<thead>
<tr>
<th>Marginally skilled</th>
<th>Moderately skilled</th>
<th>Highly skilled</th>
</tr>
</thead>
<tbody>
<tr>
<td>36%</td>
<td>28%</td>
<td>20%</td>
</tr>
<tr>
<td>60%</td>
<td>68%</td>
<td>60%</td>
</tr>
<tr>
<td>4%</td>
<td>4%</td>
<td>20%</td>
</tr>
<tr>
<td>54%</td>
<td>50%</td>
<td>58%</td>
</tr>
<tr>
<td>8%</td>
<td>4%</td>
<td>12%</td>
</tr>
</tbody>
</table>

Linking individual performance to “actionable” development planning

Setting “SMART” goals

Candid dialogue with direct reports on performance

Career development coaching & direction

Holding formal performance evaluation discussions

Gathering “meaningful” information on employee performance

Ensure performance evaluations are “fair” and “equitable”

Statistically what matters most

HR – Belief about what matters most
#2 - REALLOCATE TIME

Goal setting | Mid-year | Year-end
--- | --- | ---
Current | Desired

Level of Effort
#3 - KEEP SCORE

Measure the effectiveness of your performance management strategy

<table>
<thead>
<tr>
<th>94%</th>
<th>89%</th>
<th>51%</th>
<th>58%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Have a year-end performance review</td>
<td>Link performance and pay</td>
<td>Link performance to succession planning</td>
<td>Use performance management to motivate and retain</td>
</tr>
</tbody>
</table>

**YET ONLY...**

<table>
<thead>
<tr>
<th>75%</th>
<th>42%</th>
<th>23%</th>
<th>19%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Measure completion</td>
<td>Measure linkage</td>
<td>Measure selection of top performers</td>
<td>Measure retention between top and poor performers</td>
</tr>
</tbody>
</table>
New Employee Segments
Find new employee segments to understand their employee experience: Employees that received high performance ratings this year and last? High performance ratings over the last 5 years? Three low performance ratings in the last 5 years?

Reward for Performance
Find out if you reward consistent high performers with greater pay increases, bonuses, promotions and career opportunities. Who are your outliers?

Downgrades and Upgrades
Research the characteristics of employees that go from medium to high performers, high to medium performers, or medium to low performers. Are there consistent attributes? Does one of these things tend to happen at a certain career level?
Provide higher base pay for consistently strong people managers

- People managers are at the core of performance management
- People management skills are rarely rewarded directly
- People manager training may be inconsistent or non-existent
- Disconnect between organization needs and actions
KEY TAKEAWAYS

1. THINK CREATIVELY ABOUT HOW YOU CAN ADDRESS A SMALL BUDGET WITHIN YOUR ORGANIZATION
2. THINK TWICE BEFORE YOU GET RID OF RATINGS
3. FOCUS ON DATA ANALYTICS TO KEEP SCORE
4. EMPLOYEE VALUE PROPOSITION IS MORE IMPORTANT THAN EVER
5. REWARD PEOPLE MANAGERS
QUESTIONS
MAKE TOMORROW, TODAY