MERCER REWARDS FORUM

APRIL, 2014

Brisbane, Tuesday 8 April
Melbourne, Wednesday 9 April
Sydney, Thursday 10 April
Perth, Tuesday 15 April
MERCER REWARDS FORUM

FROM ENTITLEMENT TO RESPONSIBILITY

Anthony Shippard
AGENDA

• Economic update
  – Australia within a global context
  – Economic change
  – Industrial relations
  – Development opportunities

• Reward, legislative change and productivity
  – Reward movements, general market and by sector / job family / state
  – Legislative change – its impact on you, your role and the economy
  – Productivity – the levers for change
  – What do your employees really think?
  – What can you do to affect a shift?
  – Development opportunities

• Summary
ECONOMIC OVERVIEW
ECONOMIC OVERVIEW

- Key economic indicators present mixed results
- With the exception of inflation (and the exchange rate, depending on point of view) all other areas show weaker results compared to 12 months ago
- Unemployment is of particular concern (currently at a the highest levels over the last decade. Increases driven by
  - Resources, Construction, Engineering
  - Manufacturing
- ANZ’s job advertisement series:
  - February 2014: highest number of job adverts since May 2013
  - Yet 4.8% lower than February 2013 outcome

<table>
<thead>
<tr>
<th>Economic Indicator</th>
<th>Current</th>
<th>Prior year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unemployment Rate</td>
<td>6.0%</td>
<td>5.4%</td>
</tr>
<tr>
<td>Cash rate</td>
<td>2.5%</td>
<td>3.0%</td>
</tr>
<tr>
<td>GDP growth</td>
<td>2.8%</td>
<td>3.1%</td>
</tr>
<tr>
<td>Exchange rate (AUD – USD)</td>
<td>90 cents</td>
<td>1.05 cents</td>
</tr>
<tr>
<td>Inflation (CPI)</td>
<td>2.7%</td>
<td>2.2%</td>
</tr>
</tbody>
</table>
INTERNATIONAL COMPARISONS

• Comparing similar economies, Australia is expected to record falling GDP growth whilst all other countries experiencing increasing GDP.

• In contrast, unemployment is expected to increase in Australia whilst decrease in all other locations.

• Again, reflects some of the ‘growing pains’ which the economy is expected to undergo over the next two years.
  – However, Australian GDP still much stronger than all other locations in 2013.
THE CHANGING AUSTRALIAN ECONOMY

- Compared against other like economies, Australian has a high reliance on resources based project as an input to overall GDP
- Focus has now turned away from the resources sector as the driver of growth into a more multi faceted economy supported by a number of key sectors
- Manufacturing also a key focus
  - Peaked in 1960’s contributing approx. 25% of GDP, currently at 9%
Australian economy has a high reliance on Agriculture and Industry when compared against similar economies.

Particularly in the case of Industry, Australia is essentially competing against other countries offering the same output at a fraction of the price.
EVOLVING ECONOMY – DECLINING MANUFACTURING SECTOR

• Jobs lost:
  – Qantas: 5,000
  – Ford: 1,500
  – Holden: 2,900
  – Toyota: 2,500
  – Approximately 65,000 roles expected to be impacted as a result of the automotive closures

• Between February 2008 and August 2013, the manufacturing sector in Australia has lost approximately 141,400 employees
Australian salaries on average 30% higher when comparing against similar economies

Minimum wage standards also a lot higher than like economies

High wage costs have presented challenges to many organisations
“I see the unions wants pay rises when productivity is very low……it shows inflexibility to understand how the world has become global”
Steen Jakobsen – Chief Economist, Saxo Bank (March 2014)

"It’s critically important we say to the community our intention is not to dislocate travellers,"

"But we will take whatever steps are necessary into the future.

"If people out there are prepared to stand with us, we are prepared to take whatever action is necessary.

Tony Sheldon - TWU National Secretary (Australia, 2014)

We could either accept the Board's proposals in the certain knowledge that they were only the start of a massive closure programme, resulting in the huge loss of jobs for our members -or we could take strike action, and fight with dignity and pride for the position we knew to be right.

There is only one response. Faced with this legislation we should say we will defy the law…. If there is an attempt to use this legislation then you defy it not as an individual union but as a movement.

Arthur Scargill, NUM President (UK, 1985)
## World Bank: "Ease of Doing Business Index" Rankings 2014

<table>
<thead>
<tr>
<th>Country</th>
<th>Overall</th>
<th>Starting a business</th>
<th>Construction permits</th>
<th>Getting electricity</th>
<th>Registering property</th>
<th>Getting credit</th>
<th>Protecting investors</th>
<th>Paying taxes</th>
<th>Enforcing contracts</th>
</tr>
</thead>
<tbody>
<tr>
<td>Singapore</td>
<td>1</td>
<td>3</td>
<td>3</td>
<td>6</td>
<td>28</td>
<td>3</td>
<td>2</td>
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<td>HK</td>
<td>2</td>
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<td>5</td>
<td>89</td>
<td>3</td>
<td>3</td>
<td>4</td>
<td>9</td>
</tr>
<tr>
<td>NZ</td>
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<td>1</td>
<td>12</td>
<td>45</td>
<td>2</td>
<td>3</td>
<td>1</td>
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<td>US</td>
<td>4</td>
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<td>25</td>
<td>3</td>
<td>6</td>
<td>64</td>
<td>11</td>
</tr>
<tr>
<td>UK</td>
<td>10</td>
<td>28</td>
<td>27</td>
<td>74</td>
<td>68</td>
<td>1</td>
<td>10</td>
<td>14</td>
<td>56</td>
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<tr>
<td>Australia</td>
<td>11</td>
<td>4</td>
<td>10</td>
<td>34</td>
<td>40</td>
<td>3</td>
<td>68</td>
<td>44</td>
<td>14</td>
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<tr>
<td>China</td>
<td>96</td>
<td>158</td>
<td>185</td>
<td>119</td>
<td>48</td>
<td>73</td>
<td>98</td>
<td>120</td>
<td>19</td>
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<tr>
<td>Brazil</td>
<td>116</td>
<td>123</td>
<td>130</td>
<td>14</td>
<td>107</td>
<td>109</td>
<td>80</td>
<td>159</td>
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<tr>
<td>India</td>
<td>134</td>
<td>179</td>
<td>182</td>
<td>111</td>
<td>92</td>
<td>28</td>
<td>34</td>
<td>158</td>
<td>186</td>
</tr>
</tbody>
</table>
Top 30 countries ranked by competitiveness score

Australia 21st out of 148!
GLOBAL COMPETITIVENESS INDEX
– GOOD AND BAD

Good rankings

✓ Financial market development
✓ Higher education and training
✓ Low debt to GDP

Poor rankings

✗ Labour market rigidities
✗ Burdensome government regulation
✗ Tax regulations and rates
REWARD MOVEMENTS, LEGISLATIVE CHANGE, AND THE PRODUCTIVITY CRUNCH
GENERAL MARKET SALARY INCREASES

- Current median movement: 3.0%
- This represents the lowest salary increase figure recorded by Mercer over the last 10 years, and also one of the lowest historically
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Relative levels of uniformity across each of the states, with South Australia now the highest paying state for salary increases

Salary freezes recorded in regional Western Australia, a fall from the double digit increases passed on two / three years ago

Regional Queensland showing strength, driven by CSG projects

Regional Western Australia recording a 0% ‘increase’
Further contraction evident in the majority of sectors, particularly Construction & Engineering and Insurance.

Life Science, Education and Finance and Energy sectors continue to be market leaders.
• Key corporate function job families all centred around the overall 3% median, with minimal movement from the last six months.
POOR RANKINGS FROM THE WEF

- Labour market rigidities
- Burdensome regulation
- Tax regulations and rates

- The government (both current and past) are showing signs of a shift into a more advanced economy:
  - Outcome of Qantas, Ford, Holden & Toyota decisions
  - Change in Employee Share Scheme rules
  - Retrospective changes to award conditions
ESS CHANGES
– PERHAPS FOR 2014 / 2015?

• 2009: Employees Share Scheme law changes
  – Designed to reduce the hiding of income in shares
  – Shares were taxed at grant instead of at vesting
  – Immediate negative impact on start-up firms who would always offer shares instead of salary
  – Movement offshore of a number of innovative business

• 2014: Bi-lateral agreement to repeal changes

  “We need to reach out to small business… I want it to be easy for an Australian with a good idea to attract talented employees. We will no longer let the Tax act define who votes for what party”

  Bill Shorten, Australian Labor Party (March, 2014)
PRODUCTIVITY, WAGES AND ECONOMIC GROWTH

LABOUR PRODUCTIVITY GROWTH

<table>
<thead>
<tr>
<th>Decade</th>
<th>OECD 24 Average</th>
<th>Australia</th>
</tr>
</thead>
<tbody>
<tr>
<td>1960's</td>
<td>4.7</td>
<td>2.9</td>
</tr>
<tr>
<td>1970's</td>
<td>3.3</td>
<td>2.2</td>
</tr>
<tr>
<td>1980's</td>
<td>2.1</td>
<td>1.1</td>
</tr>
<tr>
<td>1990's</td>
<td>2.1</td>
<td>2.4</td>
</tr>
<tr>
<td>2000's</td>
<td>1.5</td>
<td>1.2</td>
</tr>
</tbody>
</table>

Source: The Conference Board Total Economy Database and Treasury
What Companies* Are Focusing On:

1. Improving manager capability around the execution of Talent, Performance and Reward programs.
2. Improving how workforce productivity is defined and measured.
3. Building stronger links between productivity and pay for all employees.
4. Improving the use of non-cash benefits that match employee preferences.
5. Using on-line tools to better communicate and monitor total rewards.

Key research findings

Australian Managers lag global best people management practices including:

- **Opportunities for improvement included:**
  - Instilling a talent mindset
  - Attracting and retaining high performers
  - Addressing poor performers
  - Rewarding high performers

- **Research showed to improve managers need to:**
  - Receive better training on day to day basics
  - Be better equipped with tools and resources
  - Have their “people” performance measured
  - Be rewarded for the quality of execution

Source Understanding Productivity – Australia’s Choice, The McKell Institute 2012.
ONLY 50% OF EMPLOYEES ARE SATISFIED WITH THEIR “MANAGER EXPERIENCE”

Mercer Research – Inside Employee Minds

- Just 49% of employees believe that their manager does a good job of developing people to their full potential.
- Only 42% believed they are paid well when they do a good job.
- Just 57% say managers do a good job of setting work objectives.
- Only 43% of employees believe that their manager plays an active role in their personal career planning.
- Only 49% believe the organisation does a good job of retaining its most talented people.

Poor coverage of key workforce segments
NZ Benefits Review (NZBR) only 63% of organisations offer variable pay to operations roles
Australian Benefits Review (ABR) only 58% of organisations offer variable pay to operations roles

Productivity metrics don’t feature heavily enough on scorecards
NZBR: 57% use financial measures – only 47% have process improvement as a metric
ABR: 68% use financial measures - only 41% have process improvement as a metric

Fixed pay entitlement culture
A pay entitlement culture over the past 20 years has generously provided year on year fixed pay increases without any direct connection to productivity or performance - some negotiated years in advance as part of collective agreements.
The efficiency and effectiveness of performance-based pay remains a challenge for most organisations. The main challenge is proving the impact of plans.

**Variable pay efficiency**

**Variable pay effectiveness**

**Impact on labour cost**

Are we investing the right amount?

Ensuring the right level of *workforce cost* through the design and execution of *variable pay* programs.

**Impact on productivity**

Are we driving the right outcomes?

Ensuring *variable pay programs* are having the right *impact on employee engagement* and *performance*. 

BUILDING STRONGER LINKS BETWEEN PRODUCTIVITY AND PAY
Organisations applying greater differentiation between poor and strong performing employees

This applies to both fixed and variable reward

Poor performing employees particularly worse off

High performers also found to be remunerated on average 4% more when compared against low performers

This shift signifies moves toward a 21st century reward model
ORGANISATIONS ARE BEING FORCED TO LOOK FOR WAYS TO DO MORE WITH LESS...

... WITHOUT DISENGAGING THEIR KEY TALENT

**The workforce productivity challenge**

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SUMMARY
YOU CAN LEAD THE CHANGE

• Productivity challenge – evidence the first steps are being met
  – Greater association of performance to reward outcomes
  – Strong movement towards a sustainable rewards model and focus on managing high-cost base

• Poor rankings – can/are being changed
  – Labour market rigidities: shift in Union relations, move to market forces retrospective appeals to Fair Work Commission
  – Tax regulations and rates: repeal of ESS laws

• Economy is moving away from dependence on resources, innovation
  – Life sciences, including other high-technology industries and finance are leading the way