

MERCER GLOBAL HR CONFERENCES

# Executive Remuneration – Emerging Trends

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MAKE TOMORROW, TODAY

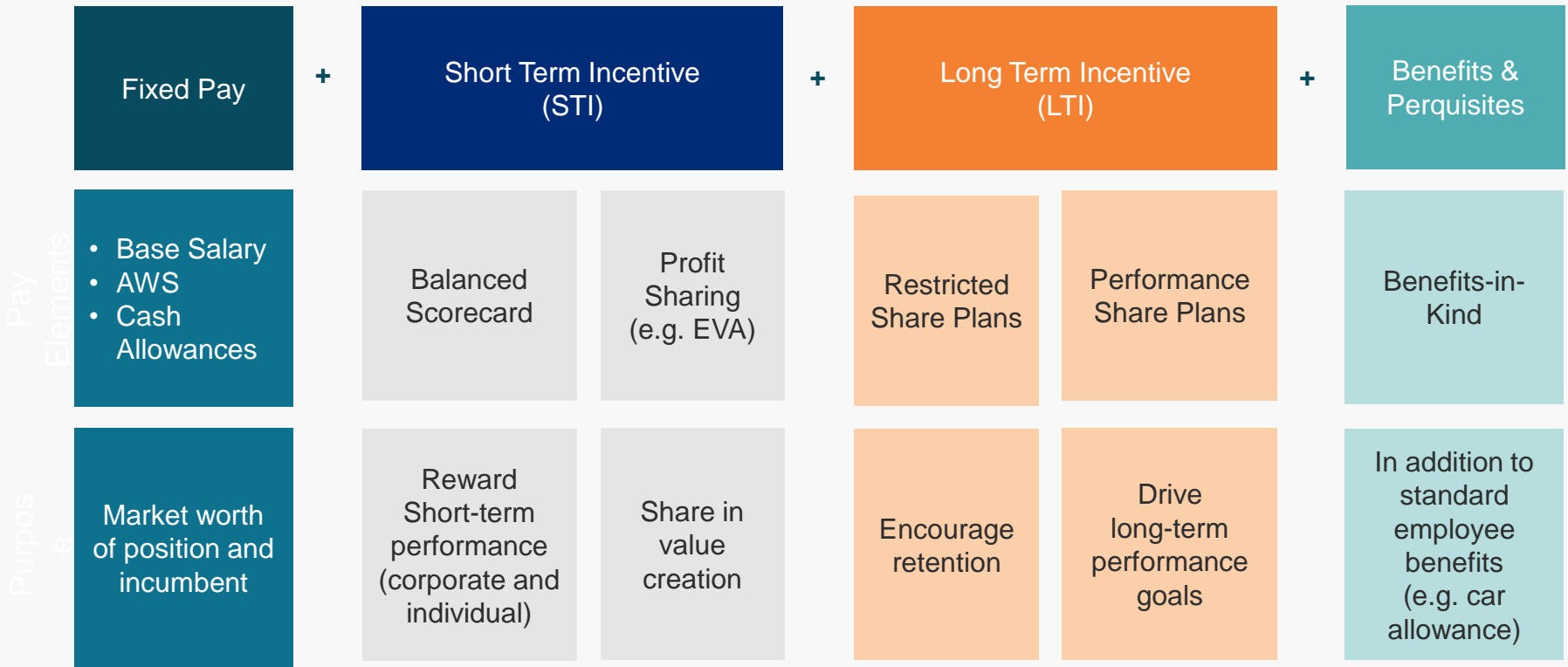


# Global ER Trends



# TOTAL COMPENSATION FRAMEWORK

## TYPICAL ELEMENTS OF PAY



# EXECUTIVE REMUNERATION GLOBAL TRENDS



**Pay Opportunity Constant** – The maximum earning opportunity in US and European markets has broadly remained constant in the last 5 years but actual payouts (realized pay) have actually declined in the past 3 years for CEO's – broadly flat for other executives.



**Strategic KPI Usage** – TSR usage has flattened out and non-GAAP metrics (e.g. FCF, adjusted EPS, EBIT) are becoming more common – both in prevalence and weightage. ESG measures (carbon emissions, workforce diversity, cybersecurity) are increasingly being used as well.



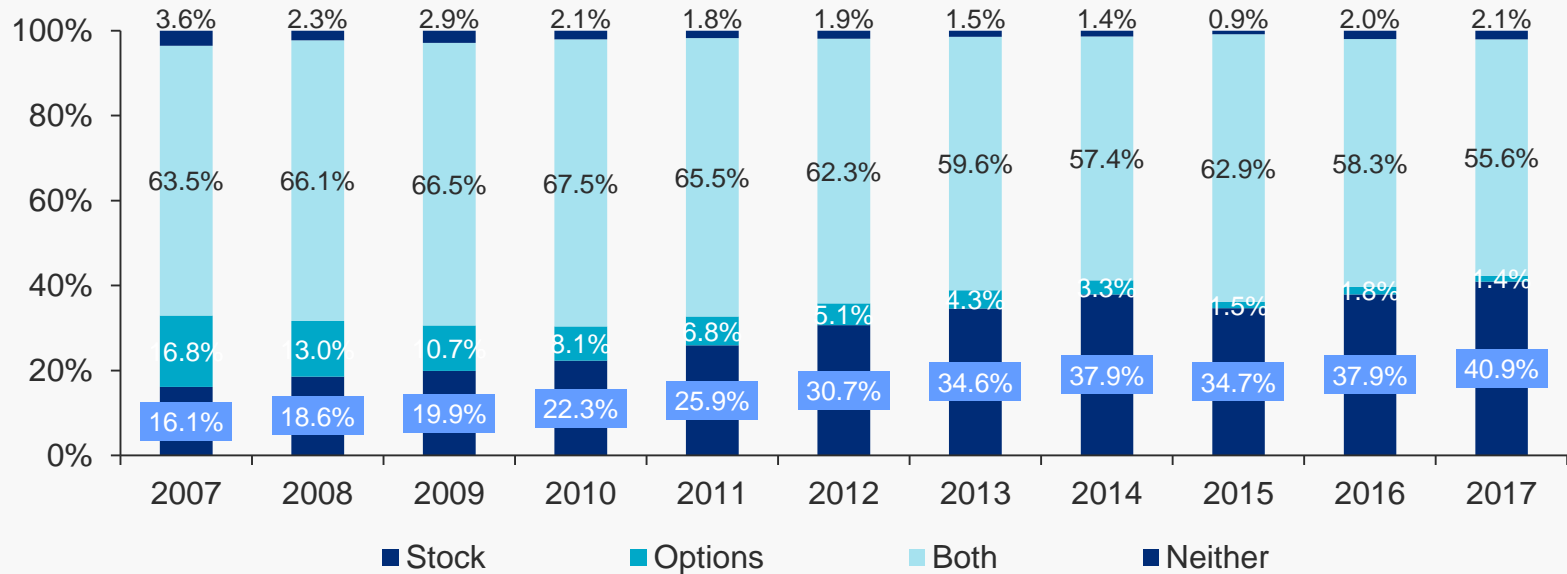
**Workforce Relativity** – Disclosures of CEO to median employee pay and gender pay gaps in organisations being mandated to address public concerns around pay inequity



**Shareholding Requirements** – Post-vesting holding periods (typically 2 years) and higher shareholding requirements (3-5 times of salary for CEOs) are becoming increasingly common

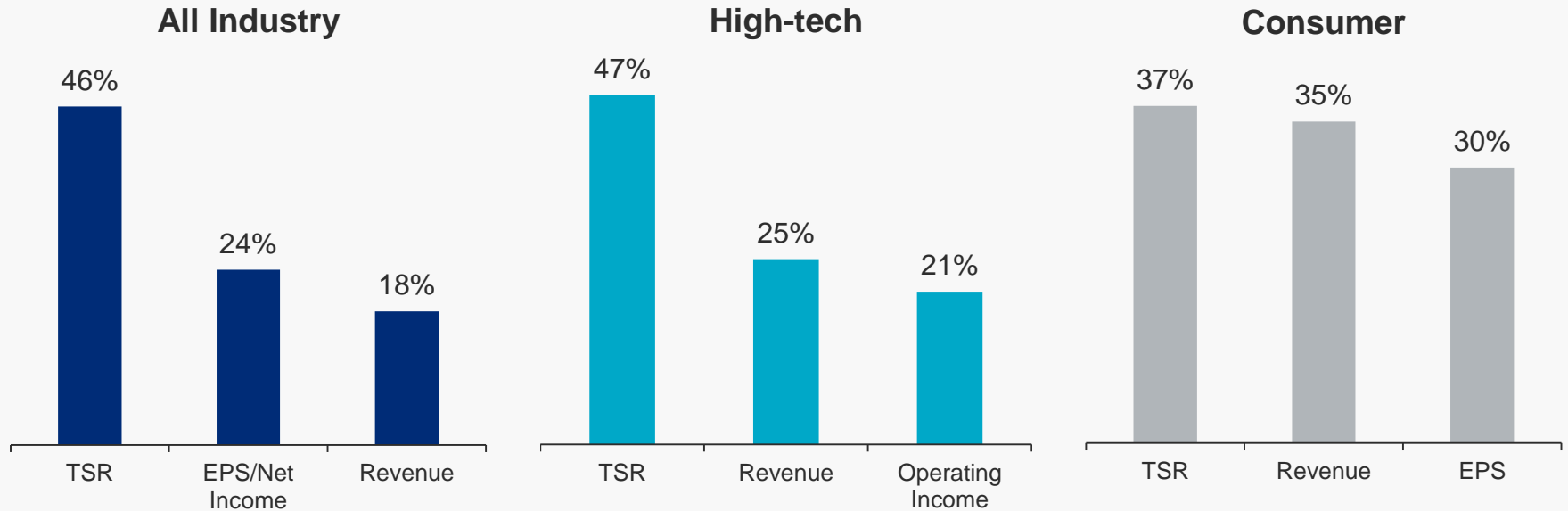
# S&P 500: VEHICLE USAGE

## STOCK IS THE MOST PREVALENT VEHICLES AMONG S&P 500 COMPANIES.



# S&P 500: KPI FOR LTI PLAN

## TSR IS THE MOST PREVALENT KPI FOR LTI PLAN

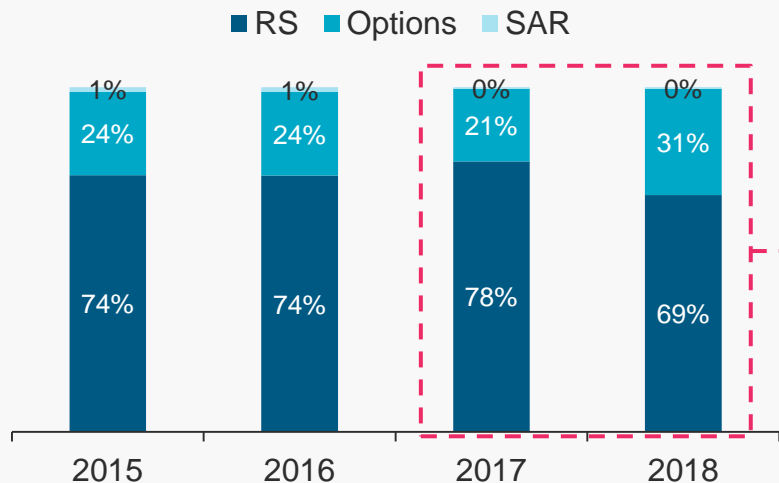


# A-SHARE: VEHICLE USAGE

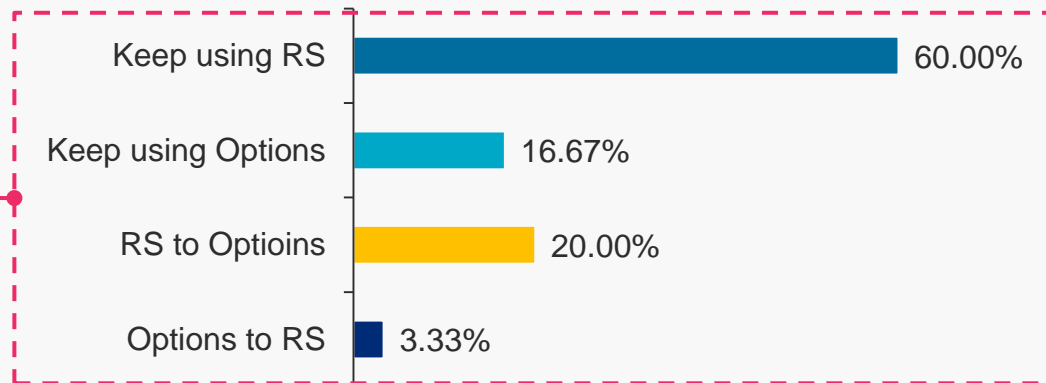
## RS IS STILL THE DOMINANT VEHICLE

- Though has its own pitfalls, RS is still a very popular vehicle in A-Share. An increasing number of companies are buying-back shares as the source of equity to implement RS plan.

A-Share LTI Vehicle(2015-2018)

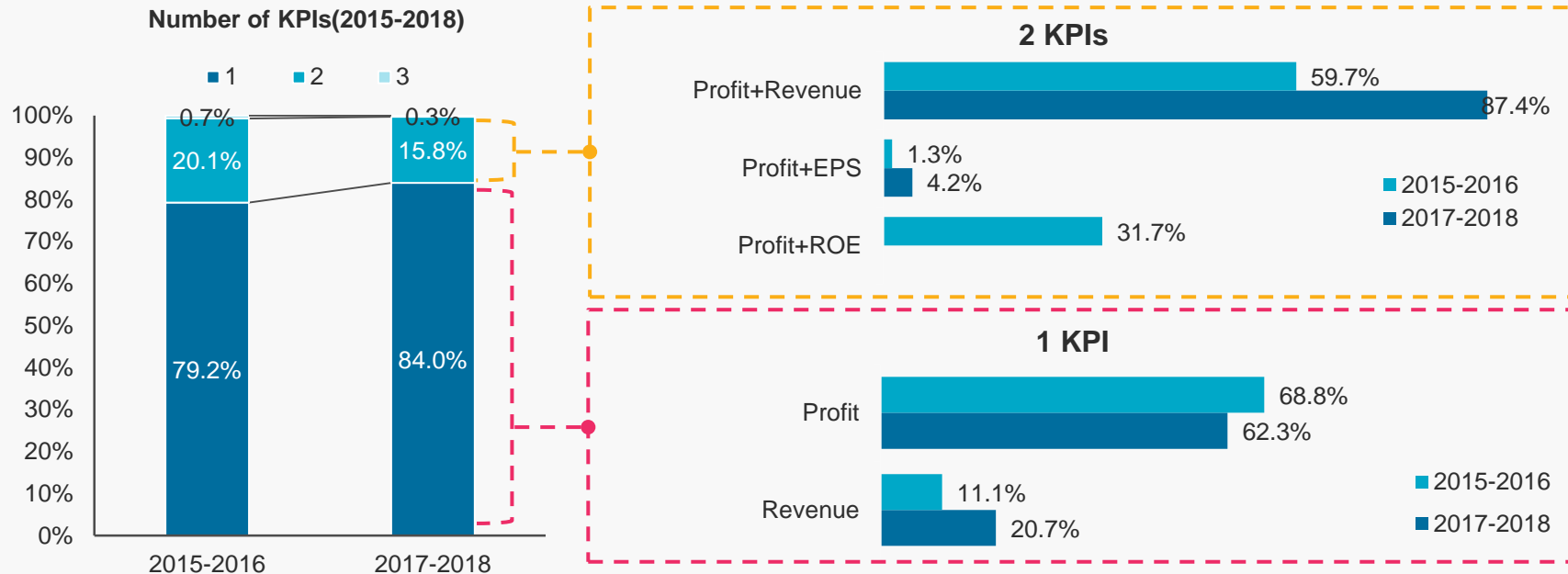


Vehicle usage for Companies implementing LTI plan in 2017 and 2018



# A-SHARE: KPI FOR LTI PLAN IN NON-SOE COMPANIES

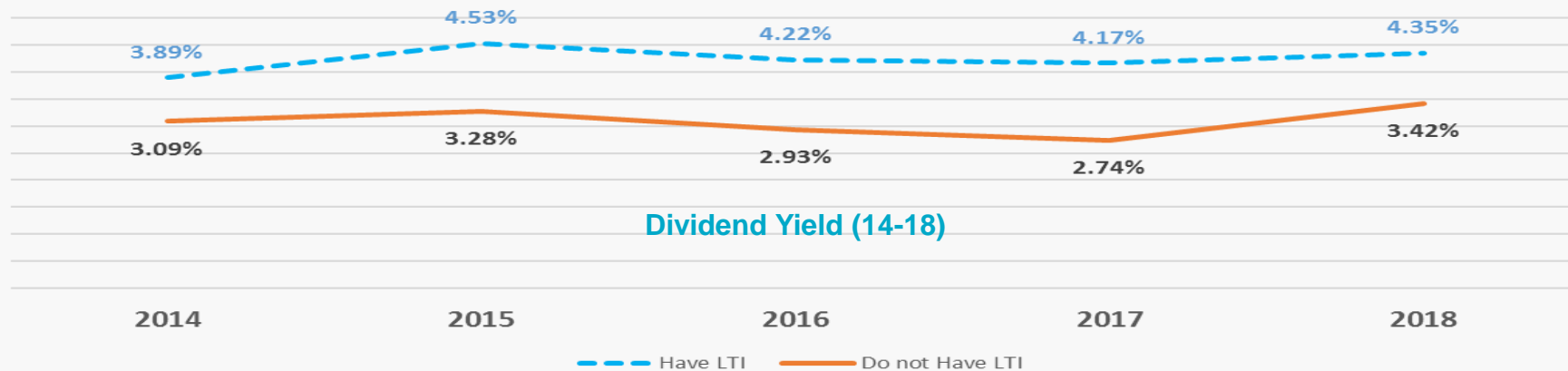
## PROFIT IS WHAT MOST COMPANIES LOOK FOR





# EXECUTIVE REMUNERATION LONG TERM INCENTIVES – DO THEY DELIVER?

LTI plans allow firms to tie in organizational objectives with executive performance and then allow for sustained long term value creation and better returns for shareholders.



## GROWTH RATE NET INCOME (14-18)

Firms with LTI Plan(s)	12%
Firms without any LTI Plans	3%

(N=100)

## GROWTH RATE ROCE (14-18)

Firms with LTI Plan(s)	3%
Firms without any LTI Plans	-1%

# What's Different In China



# WHAT'S DIFFERENT IN CHINA- PRE-IPO EQUITY INCENTIVE IS IN GREAT POPULARITY

# 1

## Corporate Governance

- Founder also plays the role as CEO.
- Family-owned business.
- Weak board, no formal supervision of ER.

# 2

## Capital Market

- Enthusiastic investors
- High appetite of risks in the private financing rounds.
- IPO is a way to measure fortune and success

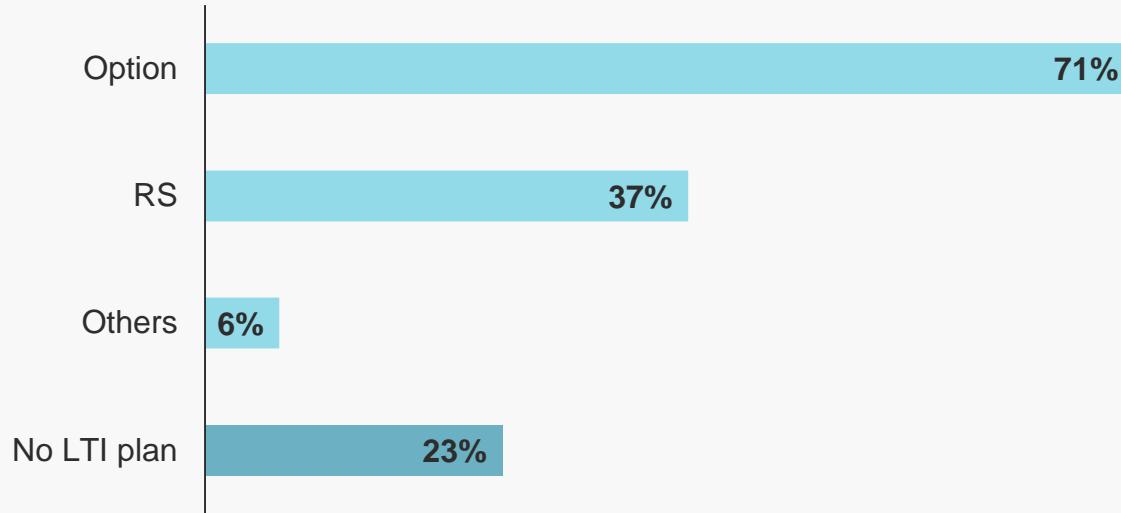
# 3

## Employee's Expectation

- High pressure of living in big cities.
- Lots of millionair fairytales.
- Eager to change life.

# LTI VEHICLES FOR PRIVATE COMPANIES IN CHINA

- For the 35 high-tech companies listed in U.S. 71% of them are using options as their vehicles



# KEY CONSIDERATIONS WHEN CHOOSING OPTIONS



## Business

- Measure the contribution
- Fair and easy to manage.



## Tax

- Income tax implication
- Possible tax deduction(No. 101)



## FX

- Don't have to make No.37 registration.

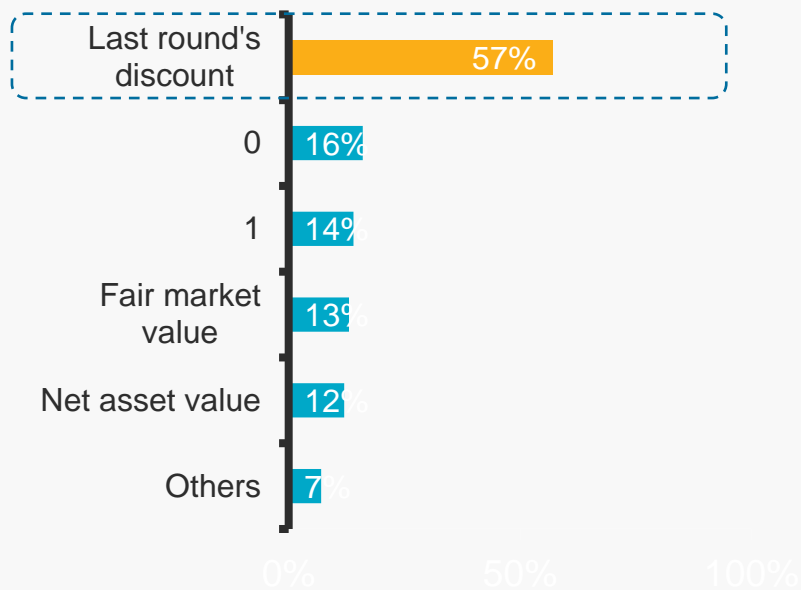


## Legal

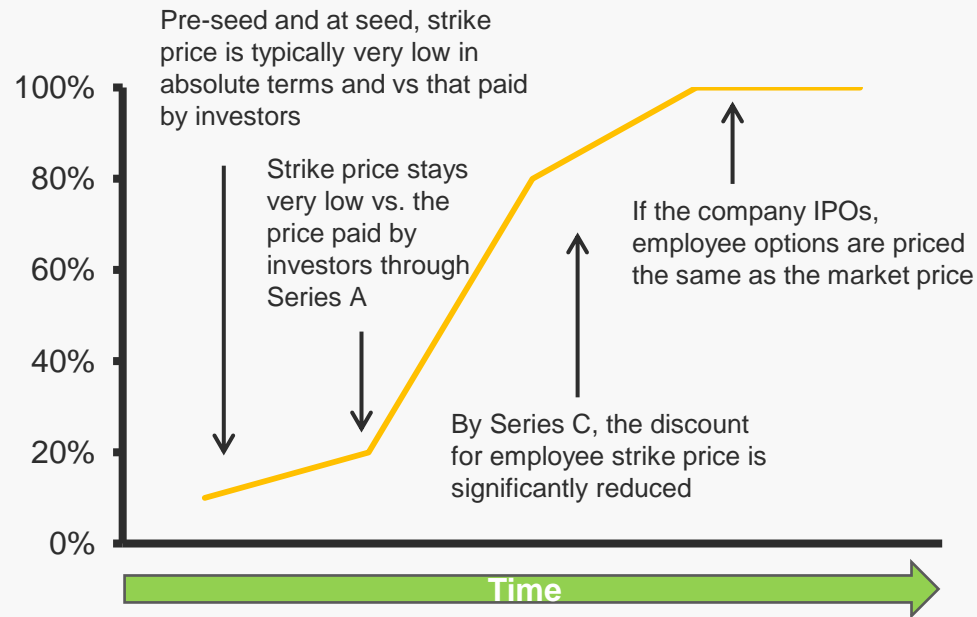
- Legal structure
- Local law compliance

# HOW TO DECIDE EXERCISE PRICE FOR A PRIVATE COMPANY

## How does private companies decide exercise price

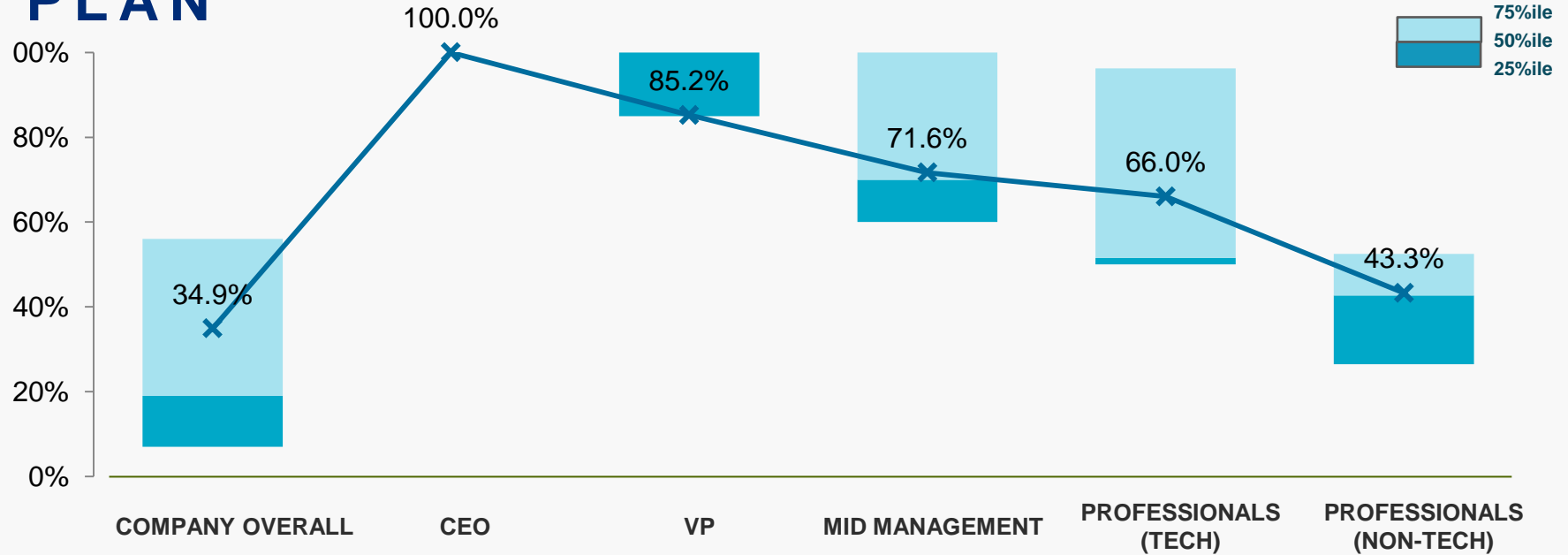


## Exercise price vs Latest round share price



# PARTICIPATION RATE

## 35% OF THE TOTAL EMPLOYEE WILL PARTICIPATE IN THE PRE-IPO INCENTIVE PLAN



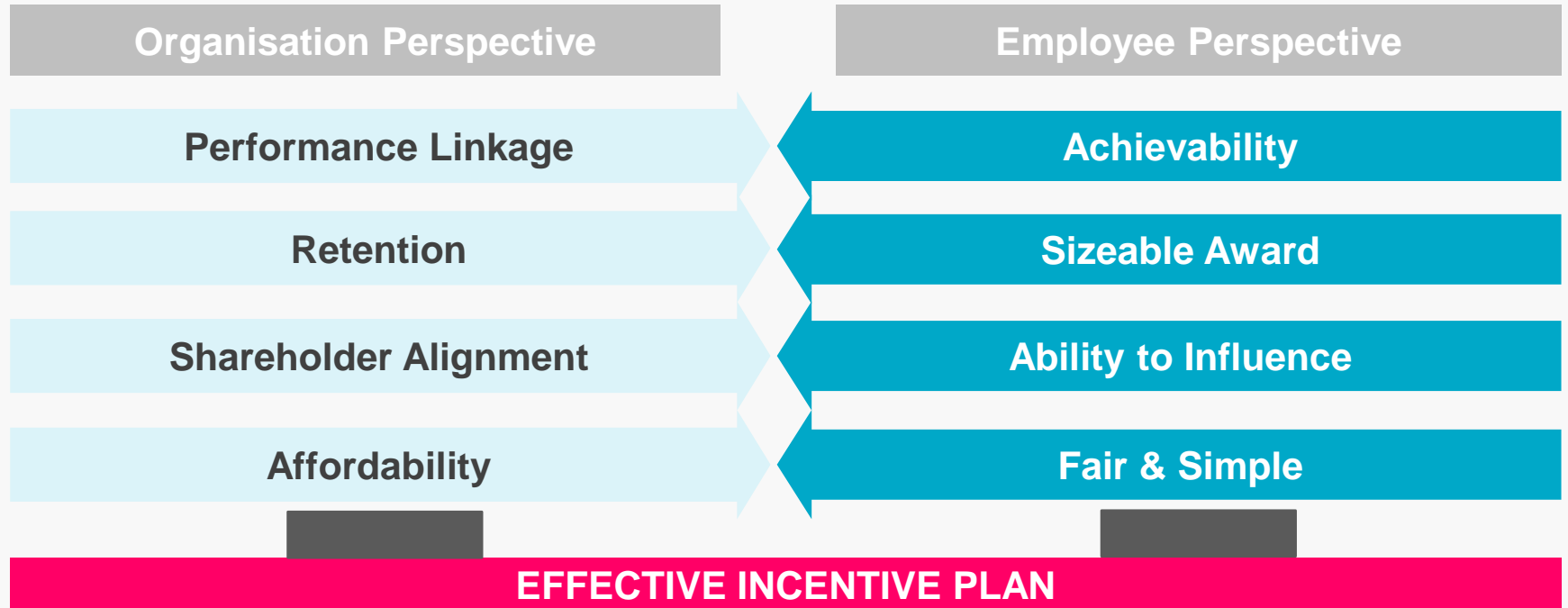
# Effective Long Term Incentive (LTI) Design Considerations





# LONG TERM INCENTIVE PLAN OBJECTIVES

## A DIFFICULT BALANCING ACT



# KEY LTI PLAN DESIGN CONSIDERATIONS

## THOUSANDS OF DESIGN COMBINATIONS

<b>Objectives</b>	Performance	Retention	Market Competitiveness	Shareholder Alignment
<b>Eligibility</b>	Top Executives only	Top Executives & Mid Management	All Employees	Key Talent
<b>Award Size</b>	Market Aligned	Desired Pay-Mix		Internally Consistent
<b>Plan Type</b>	Performance Shares	Restricted Shares	Stock Options	Cash Plan
<b>Performance Measurement</b>	KPI Targets	Peer Comparison		Share Price Movement
<b>Plan Mechanics</b>	High/Low Leverage	Wide/Narrow Performance Range		Capped/ Uncapped
<b>Grant Frequency</b>	Annually	Discretionary	Periodically	One-time Only
<b>Exercising</b>	Shares	Cash	All at once	Deferred over time
<b>Accounting/ Tax</b>	Total Cost	Company/ Individual Tax	Accrual Time	Adjustment Provisions

# AWARD SIZE DETERMINATION - MARKET BENCHMARKING

## KEY DECISION CRITERIA

No peer group is perfect as no two businesses are the same. But using the filters below, select a peer group that resembles your talent market as closely as possible



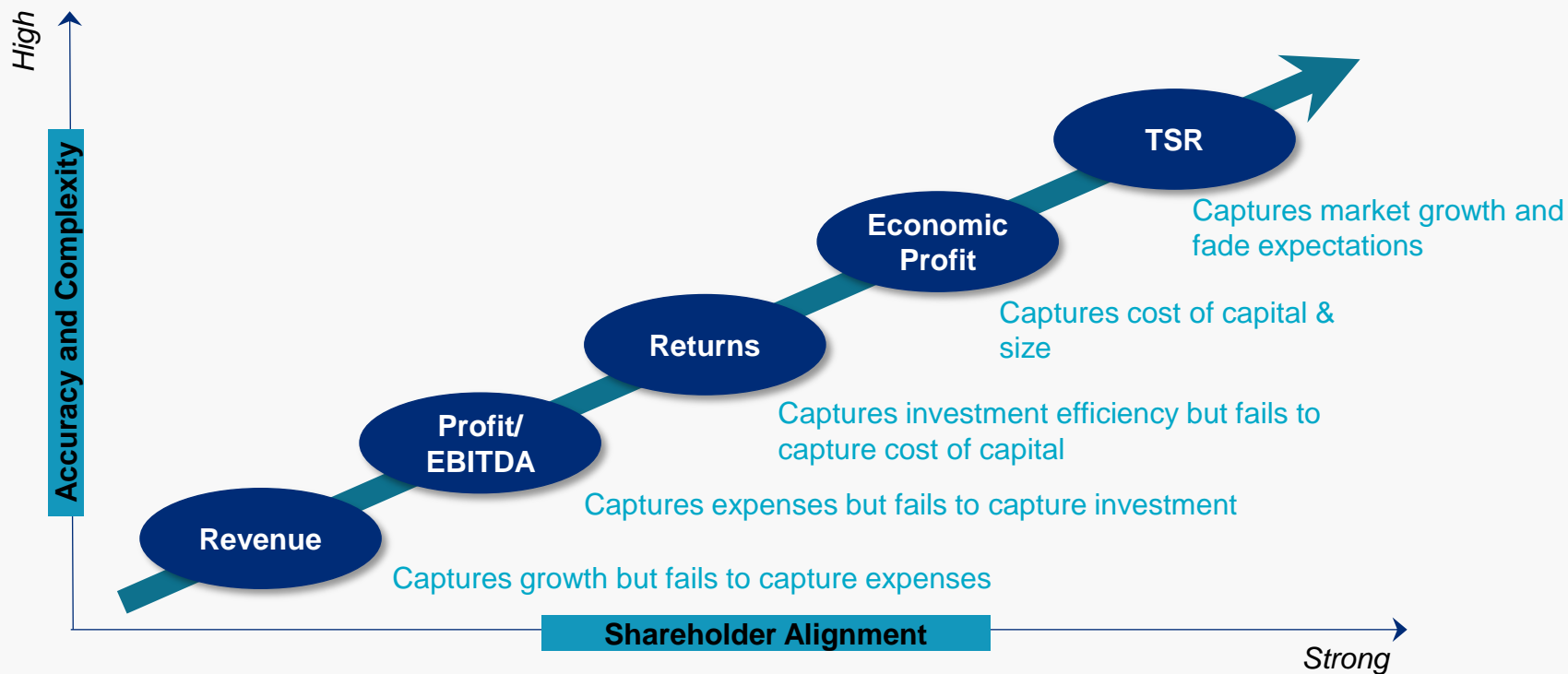
# TYPES OF LONG-TERM INCENTIVE PLANS

Business objectives	Stock Options/SARs	Restricted Shares	Performance Shares	Long-term Cash/ Bonus Deferral
Align employees' and shareholders' interest	○	○	●	○
Staff retention	○	●	○	○
Increase Shareholders' Value	●	○	○	○
Minimize share dilution	○	○	○	●

● Good   ○ Average   ○ Poor

Plan Suitability	High Upside	Retention key	Performance led	No Shares
	No Dilution Concern	Dilution concern	Direct Linkage b/w Performance & Reward	Managed Cost (budget set aside)
	Difficulty in KPI Selection/ Target Setting	Difficulty in KPI Selection/ Target Setting	Clarity in Key Business Drivers & Forecasts	Can be performance related or retention led
	Shareholder Aligned	Simplicity desired	Shareholder Aligned	

# PERFORMANCE METRIC SELECTION ACCURACY VS SIMPLICITY



# DETERMINING RIGHT KPIS' AND TARGETS

## EVIDENCE BASED DECISION MAKING

### KPI SELECTION – KEY TESTS



BUSINESS STRATEGY  
ALIGNMENT



LEAD VS LAG  
INDICATOR



VALUE DRIVER  
ANALYSIS



PERFORMANCE  
SENSITIVITY ANALYSIS

### TARGET SETTING – KEY TESTS



MANAGEMENT  
FORECASTS



HISTORIC  
PERFORMANCE



HISTORIC PEER  
PERFORMANCE



ANALYSTS FORECASTS



MARSH & MCLENNAN  
COMPANIES