Use of Market Data in Today's Labor Market

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In case anyone has been living under a rock for the past year or so, the labor market has done more than a few crazy things. We have seen massive layoffs and workforce reductions in the private sector, although these reductions are not universal in terms of industry or geographic location. In almost all cases, these reductions were the result of economic conditions nationally and were heavily focused in the financial, real estate and manufacturing sectors. This is not to say that other areas have not been affected, but these were more heavily impacted.

For the public sector, these retrenchments have had some interesting ripple effects that, to some, have looked more like a tsunami. In many states, like Arizona, Nevada, California, and Florida, that are heavily dependent on real estate and construction, the results have included substantial decreases in their primary revenue sources: property and sales taxes. This has necessitated some serious reexamination of government operations and services that, quite frankly, has been long overdue. Unfortunately, from our perspective, some of the decisions that have been made by policy makers lead us to believe that strategic

thinking has gone by the wayside. For example, we all have seen many agencies simply imposing across the board freezes on wages and salaries without any consideration as to how that will impact the agencies ability to recruit new employees given the demographic changes that virtually all organizations are facing. Even public safety, long the darling child of elected officials, has taken its share of the hit.

In previous articles and columns, we have talked about the fact that there will be fewer workers to replace the current workers given the aging of our workforce. Jobs in the public sector have changed over the years. Today, more of the jobs in public sector are "knowledge jobs" and fewer are focused solely on manual labor or on work that can be taught to unskilled individuals in a short period of time. Simply stated, fewer people do routine work. In addition, one of the major areas for the public sector is health care and public health. With an aging population, this is going to be an even greater issue for public agencies.

Given the demographics, and regardless of the economy, competition for the shrinking workforce is coming from the private sector as well as other public agencies. We have a tendency to forget that approximately 84 percent of the workforce is in the private sector. Ignoring that reality will continue to cause public agencies difficulty in fulfilling their missions.

Regardless of how you think we got into the current mess or what solutions may get us out, the stock market has taken a serious hit even if the DOW is back over 10,000 for the first time in 18 months. The housing market is still in the dumps, layoffs continue, although not at the same rate as a year ago… For government, this continues to mean less revenue from property tax, sales tax, usage tax, income tax and every other tax or revenue source.

We said earlier that we are seeing policy bodies making decisions that are clearly not focused on any strategic goal but are simply knee-jerk reactions to having less money to work with. One need only look at the states of California and Arizona, as well as several other states that cannot seem to figure out how to balance their budgets while still providing the services that are fundamental governmental responsibilities; however, this article is about use of market data in this economy, and not the economy itself. So, on that note, we will discuss why, in these times, it is both appropriate and necessary to review labor market conditions and make changes as needed to your compensation system. Hopefully, this article will provide you with the arguments you will need to use to enlighten policy makers and others as to why this is both the smart move and the right move to make, as opposed to placing one's head in the sand and pretending that the world around us has stopped spinning.

The Market

As we travel throughout the country talking to clients, the common perception is that salaries are not moving, unless they are governed by a labor agreement. Furloughs are being forced upon the workforce and layoffs have created a situation that simply screams to elected officials that NO ONE IS GETTING A RAISE. On top of that, elected officials are in the unenviable position that to raise pay—or to adjust the pay of any government employee—would be political suicide.

We understand all that. However, from where we sit, here is what is really happening.

- Only about one-third of organizations reporting (in three different surveys) stated that they froze salary increases for 2009. That means, for the mathematically challenged, that most employers raised pay. They didn't raise pay by much—only about 2.2 percent—but 2.2 percent is far greater than zero. So, for those organizations that did not raise pay, you are now at least 2.2 percent below the market.
- Recent surveys indicate that this trend of freezing salaries will continue in 2010 but that fewer organizations will freeze salaries. In 2010 about 20 percent of organizations have frozen or will freeze salaries and the other 80 percent will increase pay rates. For those of you planning to freeze salaries in 2010, by the end of the year you will then be about 4.4 percent below the market.
- An increasing number of organizations are reversing cost cutting measures taken during 2008-2009.
- An increasing number of private employers are restoring their 401K match.
- Eighty percent of employers who reduced their work-week in 2009 are expected to reinstate full weeks in the next six to 12 months.
- Roughly 20 percent of employers continue to expect workforce reduction through 2010.
- Merit budgets are projected to increase by 2.7 percent in 2010; up from 2.2 percent in 2009 (excluding frozen budgets).
- Salary structures are expected to move up by 2.4 percent (excluding frozen structures).
- Despite signs of improvement in the general economic environment, 36 percent of organizations are freezing their salary structures.
- Roughly 10-15 percent of the employers are planning on freezing their salary budget.
- More employers are planning on restoring the salary reductions made in 2009.

We experienced similar issues following 9/11, with frozen salaries, layoffs and reduced workweeks. Then, about two years later, many people woke up and found that their pay levels were substantially behind the market. It cost them anywhere from five to 10 percent of their total payroll dollars to catch up—a very expensive process.

What we also found during that time is that average market wage rates actually went up—not sideways or down, as the rumor would have it. Why this happened is simply a matter of statistics. As organizations experienced layoffs, the first to go were the poorer performers and the most recently hired. Those are the employees whose pay is usually the lowest. Now, when you average the salaries of the remaining employees—those who are the longer term and the higher performers—the result is that average pay rates are higher. And even though you may have hundreds of applicants for any job opening, you will still want to select the people with the better skills and the highest potential. They cost money, which the market will bear out.

So, even though national surveys tell us that employers are still giving pay raises, the surveys also tell us that organizations are still adjusting the overall pay structures to more accurately reflect what is going on in their competitive labor markets. Why do they do that, you might ask. Well, the answer is actually fairly simple—they want to keep the good people that they have and they want to be able to compete in the labor market for talent when and if the need arises. While not exactly the poster children for good management, let alone public relations, one need only look at the financial services industry to see this. In recent weeks, there has been abundant news coverage about major financial institutions wanting to pay their key people more, along with reinstituting bonus programs that the federal government has been vilifying as the root cause of the financial crisis. Regardless of one's personal view about the excesses of some organizations, it is telling that the primary reason given for reinstituting these practices is the need to retain their top performers and to be competitive in the recruitment of new personnel.

Maintaining the Vehicle

If you are not maintaining your compensation system now to keep it competitive, you will not be able to compete in the marketplace once the economy does rebound. To use an analogy, if you don't maintain your vehicle, it will eventually stop working, and, as we all know, that tends to happen when you put it under stress.

In this era of economic uncertainty and shrinking public revenue sources, failure to maintain your compensation system is a roadmap to disaster.

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