

Executive Compensation and Merit Pay Trends

In the wake of the recession, executive compensation and merit pay have received much attention in the business community. With senior-level management uncertain as to which way the economy will turn, increased compensation has been put on the back burner for many organizations. However, as we enter 2012, some executives believe that this may change.

Mary Ann Sardone, a partner with Mercer, the global leader for trusted HR and related financial advice, products and services, is one of those people.

“With continued uncertainty in the economy, organizations are very focused on aligning pay with the overall performance of the company and individuals,” she said. “More care is being taken to deliver rewards to those contributing most to the company.”

Research by Mercer shows merit pay increases in 2011 were approximately 2.9 percent, while budgets for 2012 are projected to be slightly higher, at three percent. They also identified that 97 percent of organizations are planning to award base pay increases in 2012.

That is still below what executives have received in the past. Joe Mallin, managing director with Pearl Meyer & Partners, an independent compensation consultancy, points out that the traditional executive merit pay increases over the past several decades have been four percent.

“I think that this has been impacted by the economy to a great extent,” said Mallin. “We are at an inflection point right now where companies don’t know if the economy will recover or [if] we will enter a double-dip recession. This has created a great deal of uncertainty around things like merit budgets.”

Sardone and Mallin agree that the banking industry has taken the hardest hit to salary and compensation in recent years.

“The banking industry has been affected a great deal by executive compensation surrounding the Troubled Asset Relief Program [TARP],” said Mallin. “This has affected not only the level of pay but [also] the structure of pay in a sense, as many incentives that existed prior to TARP have been eliminated.”

Both note that changes in executive compensation also differ greatly between the public and private sectors.

“Since the public sector is under even more financial constraints than the private sector, adding to fixed costs through increased salaries is difficult to justify,” said Sardone. “However in the private sector, even amid economic uncertainty, there is more worry about losing the best talent to competitors.”

She added: “Budgets are inching up as companies begin to feel more comfortable with business performance and to address a pent up demand for base salary increases from the existing population.”

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Given this, Mercer reports that about 50 percent of organizations surveyed project higher 2012 pay increases than those granted in 2011. “Base salary continues to be at the top of the list of most valued elements of total rewards for employees today,” said Sardone.

These increases will come as good news for those in midlevel management positions, as base salary contributes to a greater portion of total pay for them than for those at the senior executive levels. Merit pay budgets, however, remain historically low, leaving little leeway for companies to distinguish strong performers.

“I think at the very senior executive level, what you find is that salary in a lot of cases is the smallest piece of total compensation, making up about 20 percent to 30 percent of total pay. Incentives far outweigh salary at this level, whereas equity-based incentives have been significantly reduced at the mid-management level,” said Mallin. “As a result, merit budgets are a much bigger deal here than with senior management because of the impact they have on total pay.”