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"THE HEALTH CARE MODEL THAT WE HAVE IN THE U.S. TODAY IS NOT SUSTAINABLE."

— Former Senator Joe Schwarz at the MMA CEO Forum

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Michigan Manufacturing Pay Growth Returns to Normal

By Edmund B. Ura, JD

Average market pay growth for Michigan manufacturing employees returned to the long-term historical trend of about three percent per year, after a sharp decline that included one year of virtually no growth at all. This is one of the many findings of the 2007 Compensation in Michigan Manufacturing℠ report, sponsored by the MMA and conducted by Management Resource Center, Inc. (MRC).

The largest increases over the past year involved jobs in quality control, production, engineering, information systems and sales, all of which recorded average increases of more than five percent. Lagging behind, and continuing a pattern of slow growth in recent years, are a number of office and administrative positions, including accounting, human resources and general clerical support.

Increases return to trends and national averages

The return to historic averages also signals a return to comparability with national trends. To set the stage for this comparison, it is important to put pay measures in perspective. The survey statistics represent the median pay given to employees in a particular job, and the market increase represents the year-to-year change in that median. This is not the same as the average pay increase granted to employees who continue in their job. The market increase is typically two-thirds to three-quarters of the average pay increase, reflecting typically higher paid employees who retire and are replaced by lower-paid employees.

Most media reports attempt to reduce pay growth to a single number that summarizes a broad spectrum of data. While it is possible to create a simple average representing pay movement from year to year, there are a number of stories beneath the headlines. Table 1 below displays two measures of overall pay inflation in Michigan manufacturing over the last seven years.

In one measure, all jobs, the change in pay represents the simple average of the increases in median pay for a group of jobs that have been tracked since 1992. A second measure, by job family, is an average of averages — that is, an average is created for each family of jobs (e.g., accounting, engineering, human resources), and these are then averaged to create an overall average. (See Table 1.)

This reduces the impact of job families that have more titles in the survey, such as production. Neither number is "right," they are just different ways of looking at the data.

The 2007 increase in market rates brings Michigan back in line with national figures. National increases in market rates, as measured by the U.S. Department of Labor Employment Cost Index, are reported at 3.2 percent from the first quarter of 2006 to the first quarter of 2007, a measurement period comparable to the Compensation in Michigan Manufacturing Survey. This figure falls between the two measures of increase in the survey results, as noted above.

Looking at the past seven years provides a view of how Michigan manufacturers followed the national trend. National figures showed a decline of about one percent in annual employment cost increases from 2000 to 2006; Michigan followed that trend until the sharp downturn that took place in 2005 and continued through last year. The increase reported for 2007 returns Michigan to the national levels and follows a general upswing in nationally reported wages during the past 12 months (see Table 2).

Table 1

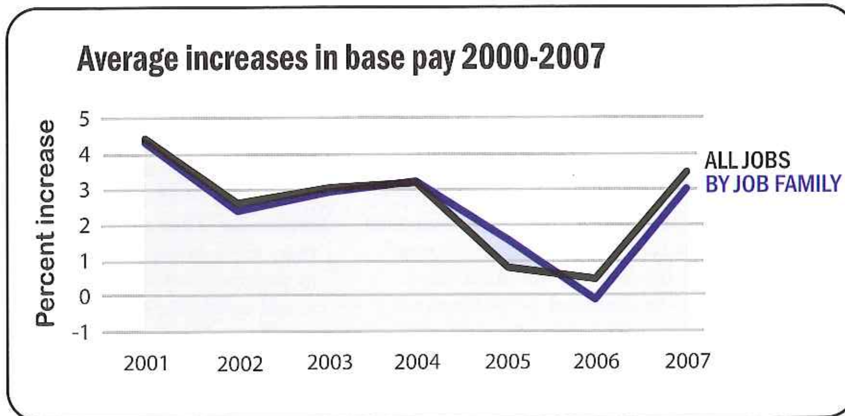
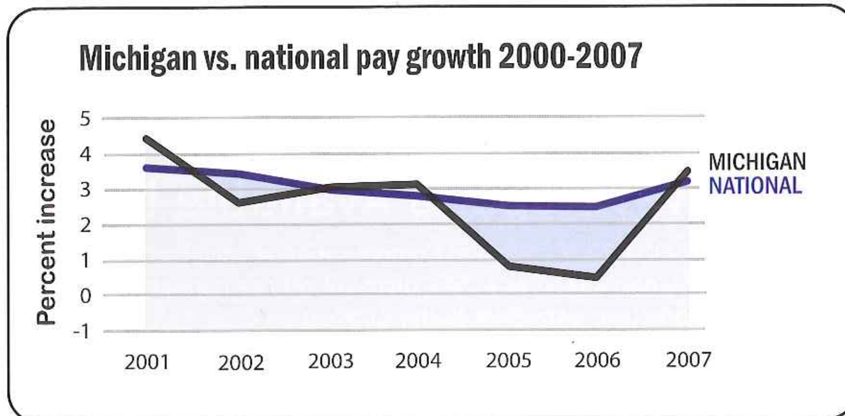


Table 2



Watching out for the traps in an employer-friendly market

Employers need to be concerned with the effects of the two-year downturn in market rates, particularly those who expect a general improvement in the business environment. While having a "buyers market" for employees can save employers in the short term, it can have damaging long-term effects.

One of the most serious compensation problems faced by employers is "locking in" employees' pay based on where they started. When all employees receive generally similar increases their long-term pay will tend to be in line with where they started. An employee who started in a down economy may end up being paid less than an employee performing at the same level, simply because of when he started work.

There are at least three negative results of this situation for the employer. First, resentment builds when employees' pay is not in line with their perception of performance. Employers who do not move to equalize or properly match pay to contribution will find morale and performance problems; paradoxically, many employers do not adjust the pay of lower-starting-rate employees because they feel they can't justify a "higher increase" (despite the fact that the adjustments need not be described as "performance related" but can be simply explained as equity adjustments).

A second (and one of the most common pay-related problems cited by employers) is when you must pay more to a new, inexperienced employee than what you are paying to fully functioning individuals with years of experience in the company.

One of the solutions is simply to adjust pay to match an employee's growth during her employment. However, the problem is exacerbated when the long-service employee was hired in a down market and the new employee is hired in a less employer-friendly market. The employer ends up in what appears to be a "no-win" situation: Do nothing and allow resentment to build or adjust the long-service employee's pay to at least match the new hire.

The reality is that the adjustment only brings the long-term employee to their real value, as compared to the outside market.

The third major issue is the risk of losing short-service, but valuable, employees when the market turns upward. Most employees show their most significant growth in contribution to their employers in the first few years of their careers. Having learned the job, they then settle into a situation in which they have established the level of performance that will be maintained as long as they stay in the job. This growth in knowledge and ability translates to an increase in market value that an employer may not recognize.

Consider how much more an employee is worth to you with only one year of experience and how much more you would have to pay to hire that same amount of experience. Then consider whether the raises given in the first year increase pay to the same level as what that experience would cost in the outside market.

The unfortunate truth is that employers generally do not increase pay commensurate with the growth of the employee and are at risk of losing employees after making the investment to train them into valuable staff members.

In a paradoxical twist, the employer who fears it has become a "training ground" for others may decide not to bother with the extra training or pay under the assumption that they will lose these employees anyway. This results in a negative spiral.

Solving the dilemma

The answer to all of the morale problems associated with under-payment is actually relatively simple — make sure that your company's pay program is aligned with the market in which it competes for talent.

Short-term savings, even if necessary to get the company through a hard-time, should be dealt with as the market and the company's condition improve. This may mean a series of adjustments to those hired in down market conditions to bring them up both to company averages and the outside market.

Many organizations feel that they do not need survey data in an employer-friendly market because they can pay whatever they want and still have the flexibility to hire the skill sets they need. While this may be true in the short-term, it is essential to know what you will be facing when conditions improve.

Failing to keep compensation in line with the market will increase the costs of turnover, training and productivity and the only way to know where your organization's pay program stacks up is to have reliable data. ■

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Survey Reports Available Now

Copies of the 2007 edition of Compensation in Michigan Manufacturing are available by calling MRC at 734-454-2500. MMA members receive a 20% discount off the regular price and survey participants receive a 50% discount for submitting your data prior to the publication date. Call MRC to request inclusion in the electronic distribution list so you can participate through an Excel spreadsheet which you can maintain to simplify participation in later years.