Finding the Right Combination: How the Most Admired Companies Unlock Reward Effectiveness

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Hay Group has partnered with Fortune magazine since 1997 to identify the World’s and America’s Most Admired Companies (MACs). To generate the annual rankings, Hay Group surveys executives, directors and industry analysts in a peer review of corporate reputations.

Recently, we studied how organizations achieve a better return on their reward program investments. The study reveals a number of best practices from which almost any employer can benefit. Specifically, the most admired companies:

- Ensure reward strategies are clearly aligned with organization goals, strategy and culture;
- Pay less than their peers. In aggregate, we found MACs pay about five percent less in base pay for management and professional jobs versus the peer group;
- Focus on executional excellence in reward programs. There is no magic answer or universal set of best reward practices for achieving results;
- Promote a ‘total rewards’ view across the organization and leverage an array of intangible rewards; and
- Leverage the involvement of managers in reward program implementation and do a better job of communicating reward strategies and engaging line managers in the rollout of reward programs.

PART 1: GET YOUR STRATEGY RIGHT

Our research found that MACs ensure that their reward programs are clearly aligned with their organization’s goals, strategy and culture. They tend to take a more centralized approach to reward strategy, compensation structures and performance management programs.

These organizations are also much more likely than their peers to say they have centralized compensation structures that emphasize internal consistency in market comparators. Also, these organizations often have clear reward positioning strategies and clear criteria for incentive eligibility.

A key rationale for more global consistency in reward

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and performance management systems is that international experience is viewed as a criterion for advancement to senior management positions. Without a consistent platform for evaluating performance across the organization, it is difficult to match people with global job opportunities based on what the roles require and the appropriate development steps for those individuals.

Alignment and consistency are also more evident in the MACs’ reward programs, in addition to a higher degree of stability in their design over time. This is consistent with past Hay Group research which suggests that even in difficult times MACs have a tendency to ‘stay the course’ with regard to key strategic priorities. Other organizations are more apt to focus on short-term objectives and change their strategies when times get tough.

When survey respondents were asked what performance measures their organizations focus on, not surprisingly growth and profitability were the two biggest factors cited. For MACs, however, ‘building customer loyalty,’ ‘building human capital’ and ‘operational excellence’ are more likely to be emphasized as well. MACs also balance their short-term and long-term performance measures better than peer organizations, ensuring that performance measures are clear, understandable and challenging, as well as realistic and achievable.

Our research suggests that when designing a reward program, organizations should:

- Align reward programs with the business across regions, business units and functions;
- Build reward platforms; then, over time, fine tune them rather than making wholesale changes; and
- Include and promote intangible as well as tangible rewards and balance different types of performance measures—financial, customer, operational, human capital.

PART 2: GET PAY LEVELS RIGHT

Surprisingly, Hay Group found that in aggregate, MACs pay about five percent less in base pay for management and professional positions.

This is because of stronger talent development programs and processes that encourage the internal sourcing of candidates. The result is less need to hire expensive talent from outside the organization; and lower costs associated with recruiting and developing internal talent. The ease of managing individuals who are already aligned with the culture and business priorities of the organization also leads to an increased return on investment.

Despite offering less in base pay than their peers, MACs generally achieve higher levels of performance and are better at implementing business strategies. These organizations achieve more with less; because they are better at giving people more rounded experiences and development, they need not rely so much on cash compensation to persuade their people to perform.

But while base salaries are five percent lower among the MACs, there are some differences by job level. Top companies actually pay their very top people more than average. At the function-head level and above, we find average pay to be about 10 percent higher. And when bonuses are taken into account, senior managers in the world’s top companies can earn 20 percent more than their peers. These people are being rewarded for their ability to deliver and ensure their companies stay at the top of their sectors. They are the ones who are driving the strategy and motivating their people.

MACs also do a better job at allocating their base pay increases. In previous research
on linkages between pay and performance, Hay Group asked about the average differential between increases of top performers and average performers.

Assuming a four percent pay increase in budget, our research found that in two-thirds of these organizations the typical top performer receives a six percent increase—not particularly meaningful. But MACs make pay increases mean more. They typically provide their outstanding performers with an increase that is at least double that of the average performer. It’s the same pool of money, but MACs do a better job differentiating.

Organizations would do well to keep in mind that:

- There are no silver bullets when it comes to managing employees and the linkage with their rewards; differentiating pay meaningfully takes time and effort;
- Managers must learn to see merit and incentive pools as investments, not as staff entitlements; they must be prepared to make the tough calls;
- Having a bell curve performance distribution is not sufficient; emphasize how you reward the ‘tails of the curve’; and
- Top performers should earn base salary increases at least two or three times more than typical performers; employers have to be prepared to offer no increases at all to provisional/poor performers—it takes discipline and good data to support a ‘no increase’ decision.

PART 3: GET YOUR LINE MANAGERS ON BOARD

Great execution, as opposed to elegant design, is a key differentiator in successful reward programs. MACs do a much better job than their peers in executing their reward programs on a global basis.

In our experience, best practices are not about sophisticated design. They’re what works best for organizations given their strategies, business priorities, values and work cultures. They involve effective execution and ensuring alignment between reward programs and business priorities. They are characterized by focused communications using appropriate messengers and mediums, and require the full involvement of line management in implementing and sustaining programs.

Getting reward programs to work is increasingly the job of line managers, not HR. And our research suggests that managers are finding this difficult. According to a recent Hay Group study of 1,200 organizations, only 30 percent view themselves as effective at implementing reward programs; less than 40 percent believe that their managers are effective at communicating reward programs; and only 28 percent believe their managers manage the pay-for-performance relationship effectively.

Line management is the lynchpin in making things happen within the organization. Given that managers take the lead role in planning, coaching and assessing employee performance—not to mention reinforcing performance via reward outcomes—it should also be their role to influence employees regarding the intent and relevance of the organization’s reward programs.

Often, it’s these intangible rewards that drive the company’s ‘employer of choice’ platform, and managers are the primary vehicles in attracting and retaining talent. In this context, managers play a significant role in fostering the work climate of an organization and in creating development and career opportunities for employees. Hay Group retention studies over the years have found that in many situations, when it comes to voluntary employee turnover, people tend to leave bad
bosses rather than bad organizations.

Managing people effectively is hard work, but the rewards are great. Because of its unique role within the organization and its knowledge of how to build capabilities, HR has a critical role in facilitating managers’ success and leveraging best management practices across the organization.

PART 4: GETTING COMMUNICATIONS RIGHT

MACs do a much better job than their peers of promoting a ‘total rewards’ view across the organization, as well as leveraging intangible rewards. Beyond the traditional tangible rewards such as base salary, incentive compensation and benefits, most organizations provide an array of intangible rewards such as career growth opportunities, quality of work, non-financial recognition and a great work climate.

MACs do not necessarily offer more intangibles than peer organizations, but they do a much better job of communicating what they do offer and getting people to understand their value. They also link reward to performance and provide tools to help managers maximize their use of rewards.

The Most Admired Companies achieve success, in part, by developing and executing a comprehensive rewards communications strategy and by segmenting employee groups to sustain core reward program messages.

Reward program communications take multiple forms. In previous work that Hay Group has done with WorldatWork and Loyola University, Chicago, we found that most organizations have a reward philosophy. However, when we asked how often that philosophy is documented, the figure dropped to 62 percent.

While it may not matter whether the philosophy is actually written down and formalized, we believe it is a likely indicator that an organization sees rewards as important to communicate. When we assess how many organizations have a documented reward philosophy, among the MACs, that 62 percent figure jumps to 76 percent.

Clearly this point is one area where companies can enhance overall employee engagement and, in so doing, garner a better return on their reward program investments.

MACs and their peer companies are also quite far apart in regard to regular provision of employee total reward statements. About 25 percent more MACs engage in this practice than peer companies. As Bruce Lasko, senior manager of compensation and benefits at Avaya explains, “We’ve spent hundreds of millions on providing benefits that employees didn’t value, understand or even know existed. Regularly communicating the total value significantly improved the effectiveness of our rewards programs.”

Even the best programs or the most sophisticated designs fail if they’re not properly rolled out, and communications are key to effective implementation. Our research suggests that organizations need to:

- Consider key messages, messengers, communication media and audiences;
- Develop a course of action that weaves reward program messages into the fabric of the organization;
- Ensure core messages are clearly communicated and reinforced;
- Start using total reward statements if not doing so already; and
- Engage line managers—early and often.

The World’s Most Admired Companies are already employing a number of best practices when it comes to implementing reward programs. There is much in their approach that other companies can use to
make their own programs more successful. To that end, the HR department has a key role in educating managers on how to influence employees and execute effective programs.

Hay Group and Fortune magazine research highlights the key ways that the Most Admired Companies design, execute and sustain their reward programs. It shows that they do a better job than others when it comes to implementing reward programs on a global scale. It demonstrates that they know how to align their programs with their business goals and how to communicate the benefits of their programs to their employees on an ongoing basis.

MACs successfully avoid the trap of focusing exclusively on cash compensation and benefits. In so doing, they enjoy the win-win scenario of both maximizing their reward investment and effectively managing their talent.

They manage to have their cake and eat it too with some simple measures, such as promoting a total reward approach that emphasizes intangible reward. This focus has a beneficial effect on pay. Because they develop talent from within and can then promote these candidates as job vacancies arise, the Most Admired Companies generally pay less than their peers. Another crucial difference is that they know how to draw on the skills of their line managers to sell the program to their employees and are good at using HR to support managers in this role.

This simple best practice approach distinguishes them from their peers in the area of reward and ensures that—as times get tougher—they are in a better position to ride out the storm.