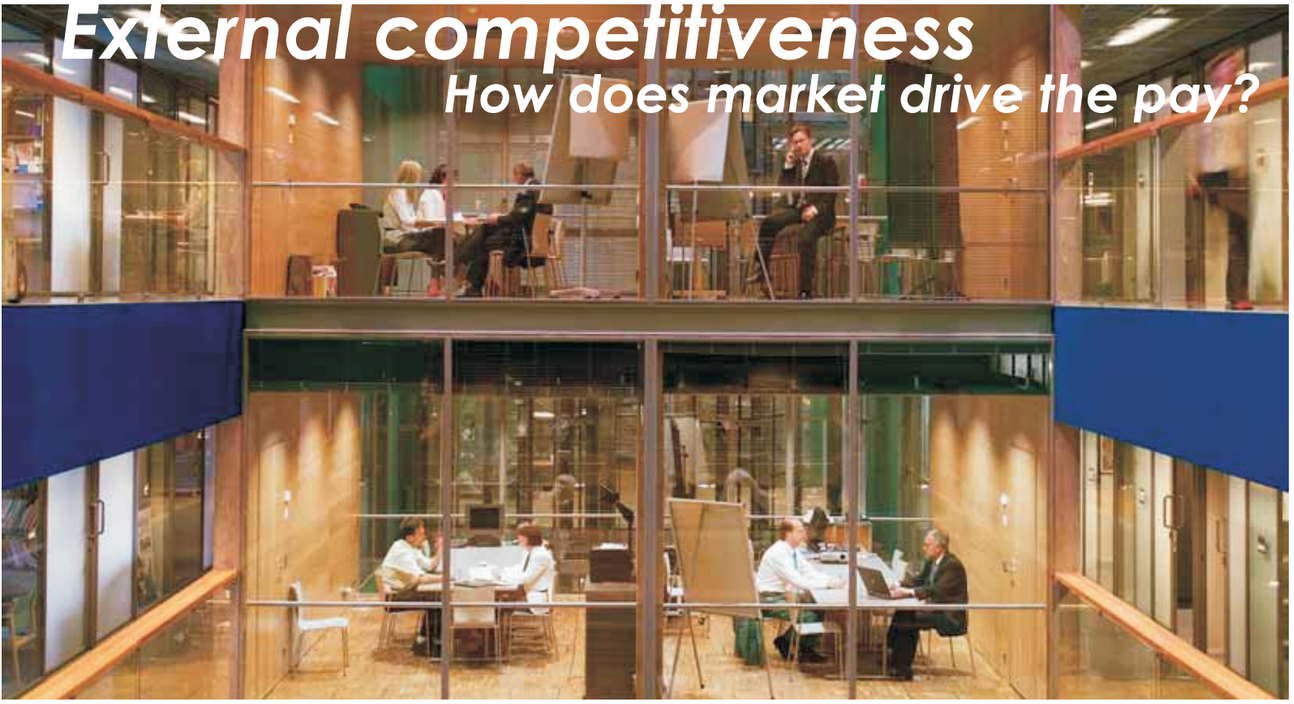
External competitiveness

How does market drive the pay?



Because pay is one of the most important means employers have to attract, retain, and motivate employees, as well as a major cost of doing business, it requires careful management.

(Milkovich, 1997, p. 457)

When you begin the process of paying employees, your first concerns will probably be related to deciding how much employees get paid. These issues revolve around the principle that you want to pay your employees enough to keep the good ones, but at the same time you can't afford to pay so generously that your business's cash flow is jeopardized. Issues you should consider when addressing the "how much" question are:

- how much other employers are paying
- how to negotiate the salary of a new hire
- how much of a rise to give an employee

Also when considering these issues, HR manager has to comply with minimum wage and overtime laws.

What Influences the pay?

Pay decisions may be affected by the economic conditions facing the company, the company's policies and practices, its relations with unions, and the types of people employed. Important external influences include the economy and government regulations.

(Milkovich, 1997, p. 457)

Economy: Product and labour markets

Although some may believe that people should not be subject to forces of supply and demand, they are. During times of expanding demand for products and services job opportunities expand and employers are more willing and able to increase pay to attract and retain employees who possess the needed skills and experience.

(Milkovich, 1997, p. 457)

Increased wages mean increased costs of production. Organizations usually pass these costs on to the consumer's shoulders in the form of higher prices. This is easier to do if there is strong demand for products. Even public sector employers such as states pass on the increased labour costs as tax increases.

Labour market conditions affect pay, also. During periods of shortages of qualified employees, pay tends to increase. In recessions, or when surpluses of qualified employees are available, rates of pay increases are slowed; pay may even decrease.

(Milkovich, 1997, p. 457)

Government regulations

Government policy and regulations influence pay more than any other human resource activity. State and federal laws regulate wage rates (e.g. minimum wages) and hours of work, prevent discrimination, and require certain benefits (e.g. social security, unemployment insurance). Government also competes in the labour market to hire employees. Government tax policy shapes the type of pay offered. Differences in tax policy among countries are reflected in pay differences.

(Milkovich, 1997, p. 458)

Unions

Although in recent years, below 20% of all US employees were members of labour unions, it would be a mistake to conclude that the impact of unions on pay is minor. The threat of becoming unionized encourages managers to improve wages, benefits, and other conditions of employment. In unionized organizations, the union is the one that can improve compensation, working conditions, job security and chances for promotion.

Outside the US, unions play a much more dominant role in wage setting, particularly in Europe and Asia.

(Milkovich, 1997, p. 458)

Retaining employees

Organizations usually try to avoid employee turnover because it is expensive. It may cost $1000 to replace a data-entry operator when hiring, training, and lost productivity are considered, and replacement of a specialized professional or executive may cost $50000.

(Bovée, 1993, p. 402)

Job satisfaction, the positive emotional state resulting from performance of a job is a major factor in retaining employees. Employees are satisfied, when human resource managers design work activities with built-in motivating factors such as achievement, recognition, responsibility, and growth of promotion. Turnover, on the other hand, is associated with low job satisfaction, low pay, lack of clarity about the job, low unemployment rates, and job alternatives outside the organization.

Comparisons among organizations

Why should you pay attention to what others are doing? You want to offer a competitive wage to make sure you attract the best candidates and retain the best employees, but you'll want to do it without putting yourself into the risk. The best way to find out what a competitive wage is in your area is to find out what others are paying for the same type of work. Therefore the offered pay should be externally competitive. You can read more about external competitiveness in the next section.

Other reasons to keep on top of market rates

- Inflation:

Inflation causes the buying power of your employees' salary to decrease, when the money amount remains the same. Since many employers adjust for inflation every year, maintaining competitive pay may, in fact, require you to adjust salary at least every two years.

- Mobility of the workforce:

As the educational level of your employees will rise, more will change jobs and change employers more frequently. At the lower end of the pay scale, turnover can be high and makes it necessary to keep on top of who's getting paid what in the field where your employees work.

- Credibility:

Without wage and salary data, it's impossible to know that you offer pay that is fair in relation to other employers. If your employees begin to feel underpaid, you won't be able to tell them, with confidence, that they're not.

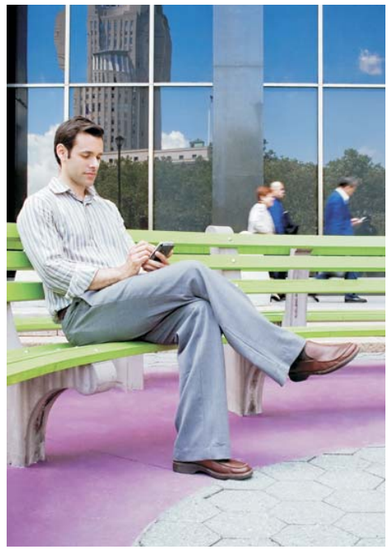
employees do not see their pay is comparable with what other organizations pay for similar work, they are likely to leave.

- because labour costs make up a substantial percentage of an organization's total labour costs, they directly affect the price the organization must charge for goods and services. Labour costs must be set at a level that permits the organization to maximize its efficiency in producing goods and services.

External competitiveness

External competitiveness refers to the pay relationships among organizations. The heart of the concept of external competitiveness is its relative nature: comparisons with other employers.

How much do other employers pay accountants, and how much do we wish to pay accountants in comparison to what other employers pay? Some set pay levels higher than their competition, hoping to attract the



best accountants. Of course, this assumes that someone is able to identify and hire the ôbestö from the pool of applicants. Another employer may offer lower base pay but greater potential bonuses, better benefits, or more flexible working hours than those offered by others.

(Milkovich, 1997, p. 463)

External competitiveness has two aspects:

- pay rates must be high enough to attract and retain employees. If

Hewlett-Packard global base pay policy reads:

"HP provides base pay intended to attract and retain a competitive workforce. HP uses market data from high-technology companies to construct competitive pay ranges. Funds available for increases may be impacted by business performance, affordability, and/or investment trade-offs. In addition to the above, increases in base pay are influenced by individual performance relative to peers.

HP conducts annual salary surveys, globally and within each country. For local country surveys, additional companies may be added to better represent the local competitive market. New hires should be brought into the company within the established salary range for a given job."

As results from the policy above, also big companies like Hewlett-Packard have to conduct surveys to find out the competitive pay level for its employees. To achieve this task, managers should focus on these three key issues:

- *Measuring the market (what competitors are paying)*
- *Setting a pay level relative to competitors that reflects external competitiveness policy*
- *Implementing programs to achieve that targeted pay level*

(Milkovich, 1997, p. 466)

Measuring the market

Organizations find out what their competitors are paying through wage surveys. Pay surveys are conducted by employers, either individually or in associations; by consulting companies; and by government agencies. In the US,

Bureau of Labour Statistics at U.S. Department of Labour is a major source of publicly available data. However, many private sector companies find its data too generalized to be useful and therefore are conducting their own surveys. How are these surveys done? A personal interview develops the most accurate responses, but it is also the most expensive method. Mailed questionnaires are probably the most frequently used because this method is the cheapest.

The relevant labour market for the survey must be defined companies involved in the survey should be similar in size, industry, and geographic location. The jobs being surveyed must be clearly defined, or the data may be suspect. As employers do not seek market data for all jobs; only selected jobs, called key or benchmark jobs, a brief description of the job being surveyed helps users to decide if the tasks and responsibilities of the internal job match the survey job. Key jobs have the following characteristics:

- *The work content is relatively stable over time*
- *A large number of employees hold them*
- *They are common across a number of different employers*
- *They are free of discriminatory employment patterns*
- *They are not subject to recent shortages or surpluses in the marketplace*

(Milkovich, 1997, p. 466)

The result from such surveys provide us with distribution of rates paid by competitors for similar jobs and allows survey users to make comparisons between what their organizations are paying for this single job and market rates what competitors are paying. On the other hand, a survey rarely focuses on a single job. Instead, data are gathered for a number of different jobs, which may be related or may cover a broader range of work. If the purpose of the survey is to set pay rates for a number of jobs with respect to the market, a way is needed to combine data from all the surveyed jobs. This can be done by the market line which summarizes the rates of the various jobs found on the market.

Setting a pay level relative to competitors

Pay level may be also called the average of all the averages. It may refer to the average for a job family or the entire company. The

employer's pay level decisions translate policy on external competitiveness into practice. These decisions focus on two objectives: attracting and retaining employees, and controlling labour costs.

(Milkovich, 1997, p. 466)

Even though pay level is a primary determinant of external competitiveness, other factors such as benefits, career opportunities, and/or the financial stability may also influence how attractive an organization appears to potential and current employees.

Other things being equal, the higher the pay level, the higher the labour costs. Furthermore, the higher the pay level is relative to the pay level of our competitors, the greater the relative costs to produce similar products or to provide similar services. Therefore, it would seem that the obvious conclusion is to set the minimum pay as low as possible.

However, other things are rarely equal. For example, high pay may make it easier to attract and retain a qualified workforce. High-wage employers should not have to train or recruit as extensively as low-paying ones. This could be explained by the greater selectivity in hiring that is made possible by the larger number of applicants attracted by the high wages. If better applicants are hired, greater productivity may compensate the higher labour cost per employee.

There are three pure alternatives in setting a pay level to set pay so it leads competition, matches competition, or falls below what others are paying.

(a) Match competition:
Matching organizations try to ensure that their wage rates are approximately equal to those of competitors. Equal wage rate place competing employers on an equal footing in their ability to attract and maintain a qualified workforce.

(b) Lead:
Employers who offer higher pay rates than their competitors maximize their ability to attract and retain quality employees and minimize employee dissatisfaction with pay. The idea is that higher pay increases the number of applicants and permits the selection process to skim the cream of the applicants.

(c) Lag:
Letting pay rates fall below competitors' rates may hinder an employer's ability to attract or retain employees. However, the opportunity to work overtime, to secure promotions and avoid layoffs, or to be part of a friendly work environment may offset lower pay rates for many potential employees.

(Milkovich, 1997, p. 471)

To be precise when hiring new employee, manager should not have only the knowledge of the pay level, but should also know the background information on the candidate and the position. He should:

- Determine the pay band of the new position. Locate the pay band minimum and maximum for the current year.
- Obtain the candidate's current pay level. Before making a salary determination, it is often valuable to understand the candidate's current salary and future expectations.
- Identify any other job offers that the candidate has received. To understand the competitiveness of a job offer, it is helpful to determine whether the candidate has any other job offers and their associated salary levels.
- Compare the candidate's experience and breadth of skills as they relate to the requirements of the position.
- Assess current budget status to determine available funds.

Implementing pay levels

Depending on the organization's pay level decision, there are two possible alternatives. Usually companies won't choose to pay less than is the market value as they don't want to have unqualified employees or employees who will leave to the better paying competitors.

If an organization's pay level policy is set to match competition, this policy can be translated into practice by projecting market rates forward to the middle of the next budget period and then paying those rates at the start of the next budget period. If the market rates continue to rise, but unless the organization continues to increase its rates, its pay will begin to lag the market, rather than match it. Most organizations get around this by projecting survey rates forward an additional six month. With this technique, an organization actually leads the market for the first six months, matches the market at mid-year and then lags the market for six months.

For a lead pay policy, the market line may simply be redrawn higher or the rates may be multiplied by some constant. How closely the organization's actual pay corresponds to its specified pay policy depends on the techniques used.

(Milkovich, 1997, p. 472)

Conclusion

HR department in every company has to decide on how much employees should be paid. Employees have to be paid enough, so they will not leave the company but at the same time you have to minimize labour costs as the final price of goods and services provided by your company depends on your labour cost. To set the pay levels in the particular company, HR should think about supply and demand on labour market, government regulations,

unions, retaining employees, inflation, mobility of the workforce and about wage comparisons with other competitive organizations.

External competitiveness is a good start to set the pay levels in a company. When you know how much are your competitors paying the workers on the same positions as you have, you can propose your future employees a little higher pay and adjust your current employees pay to fit the market value. You will attract more applicants, so you will be able to choose the best fit for your position. You will also ensure that your current employees won't leave the company because of the lower pay as in the competitive company.

about author:
Som celkom obycajny chalan, s celkom obycajnymi zalubami, s celkom obycajnym zivotom a s nie celkom normalnym postojom k zivotu. Vacsina ludi ma nechape, co je ich problem, a ti ostatni co sa ma snazia chapat tak im odkazujem: "nepochopite".
Vo vacsej ci mensej miere vsetko o pocitacoch a programovani. Ale asi takto to ma asi byt.