Labor Cost Actions

in Response to COVID-19

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INSIGHTORY CONSULTING

Background

Following up on Craig's article "Managing Cost in the Midst of COVID-19 Uncertainty" https://bit.ly/2RR3Ugv we received several questions around "So what should I do in my company?" (hint: it depends!)

In the 4 weeks since that article was published, we are seeing strong and very welcome signs that the pandemic is easing (if only on a relative basis) and companies are starting to ask, "What does back to work look like?" However, the cost questions haven't gone away. Nearly every company is facing headwinds and is looking for guidance on how to right-size their labor cost structure for a downcycle environment.

To provide some concrete data points around these questions, we did a quick analysis of the labor cost actions announced by leading (mostly publicly traded) companies. We selected 21 companies, with 7 companies in each of these 3 groups:

- **Significant Cost Actions:** Companies that have announced mass furloughs, layoffs or significant pay and benefit reductions.
- **Moderate Cost Actions:** Companies that have taken moderate/ precautionary actions across the board, and/ or significant reductions in certain Business Units (but not across the board).
- **No Cost Actions:** Companies that have not announced a major cost actions so far, and in many cases may have announced that they will protect jobs or even increase pay/ benefits during this crisis.

All 21 companies are very large corporations (annual revenue range $7B to $524B); however, we are aware from other conversations that smaller companies in their respective industries are following a similar patterns of cost action.

The data reflects a snapshot in time (gathered between ~April 15 – 20, 2020), and is changing on a daily basis. The longer this pandemic's after-effects persist, the more we expect companies to move from "no actions" to "moderate actions" and from "moderate" to significant".

Summary of findings

We found that the extent of cost action can be explained by 2 main factors:

1. The degree of business disruption (depth and duration of impact)
2. Relative company profitability

	High Business Disruption		Low Business Disruption
High Profitability		Apple	Microsoft Google
	Delta Airlines Marriott Disney Darden Starbucks	HCA Rockwell Automation Home Depot	Comcast
Low Profitability	Macy's Schlumberger GM	GE Gannett Walmart Target	

Legend *Significant Cost Actions* *Moderate Cost Actions* *No Cost Actions*

Business disruption is a subjective measure of the % of total annual revenues and earnings that might be at risk due to the pandemic.

- **High Disruption**: The entire company or major divisions are shut down for multiple months with revenues and earnings dropping 50% or more. Some of these companies had other factors pre-dating the pandemic (e.g. oversupply in oil & gas, secular decline in retail, etc.)
- **Medium Disruption**: Majority of revenue flows are continuing, but they are seeing pipeline reductions, order cancellations or other indicators of weak demand. Their ability to maintain core operations may be diminished due to employee or supply chain issues. Some business units or locations may be deeply impacted but others are still able to sustain significant revenues. Some of the revenue may be deferred, not lost permanently.
- **Low Disruption:** Impact is limited to a smaller part of the business and/ or lagged, while the main profit engines are still functioning. In some cases, the crisis may have actually increased demand and/ or they have been declared essential services and/ or a large % of their employees is able to work from home.

Relative company profitability was measured by net margin for the last completed fiscal year (net income ÷ revenues). Companies with margin at or below 5% were considered "low profitability", 6 – 15% were considered "medium" and 16% or above were considered "high profitability". We looked at a number of other proxies for measuring a company's financial resilience (including cash per employee, debt to equity ratio, etc.) but there was too much "noise" in the 2019/ 20 data for those measures to be useful. Net margin – while far from perfect – turned out to be simpler and a better predictor of cost actions.

As expected, companies with the highest disruption and lowest profitability are taking the strongest and most urgent cost actions. At the other end of the spectrum are companies that have lowest disruption and highest profitability – they have both the means and the need to protect jobs as well as employee programs. Starbucks is an interesting outlier. Its business has been significantly impacted

(Q2 '20 earnings are expected to be ~half of Q2 '19) and it's 13.6% margin (while very high for its industry) isn't at the level of a major tech company. Despite all this, they protected employees' pay through the month of April, and even increased hourly workers' pay by $3/ hour for those choosing to come to work. That one can only be explained by "culture"!

What is new this time around

When we compare cost actions to previous crises (especially the 2008-09 Financial Crisis), we see a number of differences.

1. **Base pay reductions**: Base pay was considered a bit of a sacred cow and was only reduced in the most extreme circumstances. This time around, we are seeing a wide range of companies – not just the most distressed ones – reduce base pay for salaried employees. This is an area where employers need to be careful to not run afoul of employment law.
2. **Sliding scales:** Several companies are implementing "progressive" pay reductions based on salary or position level – with the most highly paid employees taking the largest cut, and employees below a certain salary level (or hourly employees) not seeing any reduction at all.
3. **Executive pay:** One of the hallmarks of the "Great Lockdown" crisis is the number of Boards, CEOs and other top executives taking voluntary pay cuts. For the most deeply impacted companies, they are giving up the entire year's salary. For the moderately impacted ones, they are giving up a few months of pay. While this is an important symbolic gesture, we should take care to not read too much into it since salaries constitute a small fraction of top executive compensation. There are already indications that compensation committees are granting new stock awards at current low prices, which should easily make up for the lost salaries as their stock price recovers.
4. **Furloughs**: Furloughs are fairly well known in the cyclical industries (airlines, oil and gas etc.) but this is the first time in our experience that furloughs are being deployed in industries like retail, manufacturing, services, restaurants etc. This indicates that employers are expecting a rapid rebound and don't want to permanently lose their employees.
5. **Increase in pay and benefits**: Several retailers and tech companies are actually increasing pay and benefits (especially sick leave) for the duration of the crisis. This can be seen as a combination of hazard pay and a bonus for showing up to work in trying times.
6. **Pay deferrals**: The big automakers (GM & Ford) announced very unusual pay deferral programs. All of GM's 69,000 salaried employees will see a temporary 20% salary reduction till March 2021. Ford's top 300 executives will have their salaries deferred by 20-50% for at least 5 months. Both companies will pay back the amounts deferred with interest at the end of those periods, so this is really a cash flow issue versus a cost saving.
7. **Huge gap between the "significant actions" and the "no actions" group:** In a "standard" recession, the tide tends to go out for the entire economy. This one is a little different in that there is a group of companies making perhaps the most draconian decisions in their history, while another group of companies is increasing pay and benefits. If these differences persist for a while, they will inevitably exacerbate the talent gap between these groups of companies.

Significant Cost Actions

Significant cost actions of 7 companies are summarized below. This group pulled most of the labor cost levers available.

	Base Pay/ Bonuses/ Hours	Benefits	Executive Pay	Furlough	RIF
Delta Airlines	Reducing >40k ees to 3-4 workdays/ week from April through June; Est. savings = 25% of payroll over the next 90 days	Delaying $500 million in voluntary pension funding	CEO & Board salaries cut to zero for next 6 mo. All Officers' pay cut by 50%, Directors & MDs pay cut 25% through June 30	21k of Delta's 90k employees have taken voluntary short-term, unpaid leaves.	No layoffs through end of Aug. in return for federal payroll grants
Macy's	Pay cut at Director and above (% not specified); Deferred all 2020 bonuses.	Deferred 401k matches "till later in the year"	CEO and Board to receive no salary for duration of the crisis	Furloughed majority of their 125k store employees	125 store closures and 2k layoffs announced pre-COVID
Schlumberger Limited	Reduced work hours for support personnel, resulting in reduced salaries (no details)		Executive & Sr Mgmt salaries reduced by 20%	Announced furloughs (no details)	Announced layoffs (no details); Accelerated land ops restructuring
GM	Deferred 20% of base salary for 69k salaried employees; Deferred amount paid back with interest by March 2021	Furloughed employees will retain seniority and health benefits	Sr Mgmt pay cuts up to 10% in addition to the deferral; Board total compensation cut by 20%	6,500 US employees who can't work from home will receive 75% of normal pay	
Marriott	Corp employees who are not furloughed will be subject to 20% pay cuts and reduced workweeks	Deferred 401k matches till September	CEO's salary suspended for the balance of 2020; Sr Executive Team's salary reduced by 50%	Furloughed "tens of thousands" hotel employees & 2/3rd of Corporate; Corporate employees receive 20% salary for benefits & other costs	
Disney		Will pay 100% of health insurance for furloughed employees up to 12 months	Salary reductions for Exec Chairman (100%), CEO (50%); EVPs (30%), SVPs (25%) & VPs (20%)	Furloughed ~100k "non-essential" U.S. Parks & Resorts employees (~40% of total workforce)	
Darden Restaurants	Sliding scale pay cut for corp employees not furloughed. Hourly employees still working will receive additional $10 a day.	3-week emergency pay program for hourly employees not working due to restaurant closure; Added a new sick leave policy	CEO is forgoing annual salary; Sr Executives will take 50% pay cut	~150k hourly employees furloughed; ~20% of corporate employees will receive 100% pay for 1 week, 50% for 3 weeks & insurance coverage beyond that	

Moderate Cost Actions

This group used several of the labor cost levers, but didn't cut as deep, and any furloughs and RIFs were limited to a subset of the company.

	Base Pay/ Bonuses/ Hours	Benefits	Executive Pay	Furlough	RIF
Baker McKenzie	15% salary cut for U.S. lawyers and others earning >$100k; Bonus pool reduced; Will still reward top performers later in the year	Establishing an emergency loan fund to help staff facing extreme hardships			
HCA	For facilities that are closed, employees will receive 70% of base pay for 7 weeks			CEO will donate 2 mo. pay to employee fund; Board waived cash comp for rest of '20; Sr leaders pay cut by 30%	
Mayo Clinic	Physicians & Senior Admin salaries reduced 10%; Other salaried employees by 7%; Hourly employees not impacted		CEO and CAO salaries reduced by 20%	Involuntary furloughs begin on April 28 (# not disclosed)	
GE	Merit increase cancelled for salaried employees		CEO will forgo full salary for rest of '20 and Vice Chair/ President of Aviation will forgo half his salary.	~50% of US MRO employees will be furloughed	10% of jet engine workforce (~2,500 employees)
Gannett		401k matches frozen during the crisis	CEO will not take a salary until furloughs and pay cuts are reversed; Other Execs will take 25% pay cut	Employees who make >$38k will be furloughed 1 week a month for next 3 months	
Rockwell Automation	7.5% salary reductions for all non-mfg. employees; Mfg. employees not impacted and will receive a one-time additional payment	401k matches frozen during the crisis	Salary cuts for CEO (25%) & SVPs (15%); Board cash compensation reduced by 50%		
Comcast	Universal employees paid at 100% through April 19, then majority will see 20% pay cuts	Benefits protected for furloughed employees	CEO has set up a $500M fund to support impacted employees; Top 5 executives will donate 100% of their salaries to COVID charities	NBC part-time hourly workers will be furloughed starting May 3	

No Cost Actions

There were no significant executive pay reductions, furloughs or RIFs to note for this group.

	Base Pay/ Bonuses/ Hours	Benefits
Microsoft	Continuing to provide regular pay for retail team, regardless of number of hours worked; Retail team members who sign up for optional remote customer service roles earn weekly bonuses	Implemented 12-Week Paid Pandemic School and Childcare Closure Leave; Offering drive-through COVID-19 testing for employees and their dependents
Google	Stated that hourly employees will continue to receive their regular pay regardless of closures.	Two weeks paid leave for employees who are caring for family members
Apple	Will continue to pay employees and contractors through the crisis	Announced unlimited sick time for full and part- time employees; Added digital service for managing stress and anxiety for retail employees; Provided retail employees $100 reimbursement for work-from-home equipment.
Home Depot	Temporary bonus program from 3/23 to 4/19 that gives them additional $100/week for 35+ hours and extra $50 week for 16-35 hours.	Extended PTO policy (Full-time: additional 80 hours; Part-time: additional 40 hours; Over 65 ees – 2x of the additional hours); 14 days paid time off for anyone required to be quarantined.
Walmart	Fulfillment center/ warehouse employees will earn additional $2/ hour through Memorial Day; Special bonuses to all U.S. hourly employees in stores, clubs, supply chain and offices ($300 for full-time and $150 for part-time); Will accelerate the next scheduled quarterly bonus for store, club and supply chain employees by one month.	Employees who contract COVID-19 receive up to 2 weeks' pay, and if unable to return to work, may be eligible for up to 26 weeks' pay; Employees required to quarantine will receive up to 2 weeks' pay; Attendance policy waived so employees can take voluntary unpaid leave if they feel unable or uncomfortable coming to work
Starbucks	Committed to paying employees through May 3, regardless of whether they work. Service Pay (additional $3/ hour) extended through end of May for all store employees who work during this period.	Implementation of Catastrophe Pay through end of May for employees diagnosed or exposed to COVID or where stores are closed, or if employees are high-risk (60+ years old, pregnant, health conditions etc.); Expanded Care@Work benefit (heavily subsidized child/ adult care) benefit with 20 additional days
Target	Raised hourly pay by $2/ hour until at least May 2; Bonuses ranging from $250–1,500 to 20k team leads who oversee store departments.	New paid leave program: Up to 30 days paid leave for employees 65+, pregnant or with underlying medical conditions; Waived absenteeism policy; Quarantine & confirmed illness pay at 100% for 14 days; Waived eligibility & copays for childcare benefits

Additional Observations on the data

All data has been gathered from secondary sources, hence this not a comprehensive set of actions. Blank cell in any of the tables above could mean that the company hasn't made any change, or simply that the information isn't in the public domain yet.

Each company probably has additional actions that are not reported. E.g. we can safely assume that the following will be very common among majority of companies:

1. 2020 base pay increases are postponed or even cancelled. Some companies in the 3rd group might reduce rather than eliminate merit increases altogether.
2. Bonus pools funded at lower levels.
3. Hiring freeze for all but essential jobs for the first two groups
4. Fewer hours for hourly workers
5. Significant reductions in contractors
6. Elimination of company perks like lunches, gyms etc. – both from a health and cost perspective
7. Employee relief funds (for all three groups)
8. Greater availability and access to internal service centers (especially HR and IT) and Employee Assistance Programs

This analysis is not meant to be prescriptive, but looking at these larger companies can provide some frames of reference for companies who are reviewing their own cost structures. The starting point should be the grid on page 2. Each company should do an objective assessment of:

- What is the degree of business disruption (depth and duration of impact) for your business?
- What is your financial ability to sustain current labor cost structure?

Using these as starting points will enable you to make the appropriate decisions for your company.