

Executive Insight >> At The Rim

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The benefits' burden

45 million people in the US are not covered by health insurance and 40 percent of US companies do not offer health care coverage to their workers. The issue of healthcare continues to be at center-stage of political, policy and competitiveness debate.

Wal-Mart and GM illustrate that employee benefits is not just a human resource issue but a core competitiveness one. The world's larger retailer currently faces the grim reality that unabated, benefits costs could consume an incremental 12 percent of total profits in 2011, equal to \$30 billion to \$35 billion in market capitalization. GM struggles with a per-car medical expense burden five times that of Toyota, and projects a future pension obligation of \$89 billion, default of which could cripple the Pension Benefit Guaranty Corporation.

General Motors (GM)

GM's Chevy Impala, with a purchase cost of \$21,000 that includes over \$2,000 in pension and health insurance cost burden; the medical expense component of \$1,500 compares with about \$300 for Toyota per car US employee medical costs.

Benefits are GM's single biggest cost line item, more than steel; in 2004, GM alone spent \$5.2 billion on health care for its 1.1 million employees, retirees, and dependents throughout the U.S. \$4 billion of this went to retirees who outnumber the current 160,000 workforce by a factor of 2.5.

Current UAW employees pay 7% of costs; white-collar workers 27%; there are no deductibles, no monthly premiums only modest co-pays for doctor's visits and prescriptions.

Recent labor agreements have provided unprecedented concessions from the UAW with a union leadership cognizant that GM is on the edge; it was time for reality not positioning.

GM also has by far the biggest company pension plan in the United States, having promised to pay benefits worth \$89 billion to its current and future retirees; until now GM has been setting aside money to make good on those promises, keeping its pension plans compliant with the law. But if it lost its ability to generate enough cash to do that, and had to default on its pension obligations, the cost could overwhelm the agency that insures pensions, the Pension Benefit Guaranty Corporation.

Wal-Mart

Prompted by a leak, Wal-Mart recently released into the public domain an internal memo to the Board that laid out the company's employee benefits challenge and offered "five bold steps" to improve on the situation.

The memo clearly shows the challenging balance and tradeoffs between cost containment, employee satisfaction and external reputation and asserts that the growth in benefits costs is unacceptable:

- From 2002 to 2005 benefits costs grew significantly faster than sales, rising from 1.5 percent of sales to 1.9 percent.
- Benefits spend grew from \$2.8 billion to \$4.2 billion during this period, at a rate of 15 percent per year.
- Unabated, benefits costs could consume an incremental 12 percent of our total profits in 2011, equal to \$30 billion to \$35 billion in market capitalization.

The Board was advised that:

- Wal-Mart's workforce is aging faster (0.50 years per calendar year) than the national average (0.12 years per calendar year) and
- Its workers are getting sicker than the national population, particularly with obesity-related diseases

The memo added a segment of Wal-Mart's workforce consumes healthcare inefficiently, and in particular, the least healthy, least productive Associates are more satisfied with their benefits than other segments and are interested in longer careers with Wal-Mart (so they are unlikely to be leaving).

Conversely, the so-called "low utilizers" are the most attractive Associate segment to Wal-Mart because they cost less in terms of healthcare expenses and are reported to be more productive in their jobs.

Unfortunately, the memo adds, the "low utilizers" were also least satisfied with our benefits and were planning shorter careers with Wal-Mart.

Company executive recommended nine "limited-risk" initiatives and "five bold steps" to the Board.

A copy of this memo is available at the Executive Insight archive at www.charlesmore.com