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MERCER WEBCAST
TALENT RISK ASSESSMENT IN M&A

DECEMBER 12, 2013

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Agenda
What We'll Cover Today

- Talent Risk Assessment

- Recent Case Studies

- Q&A

The Proposition for Workforce Analytics
Key Questions Addressed…Some in Due Diligence…Others in "Integration"
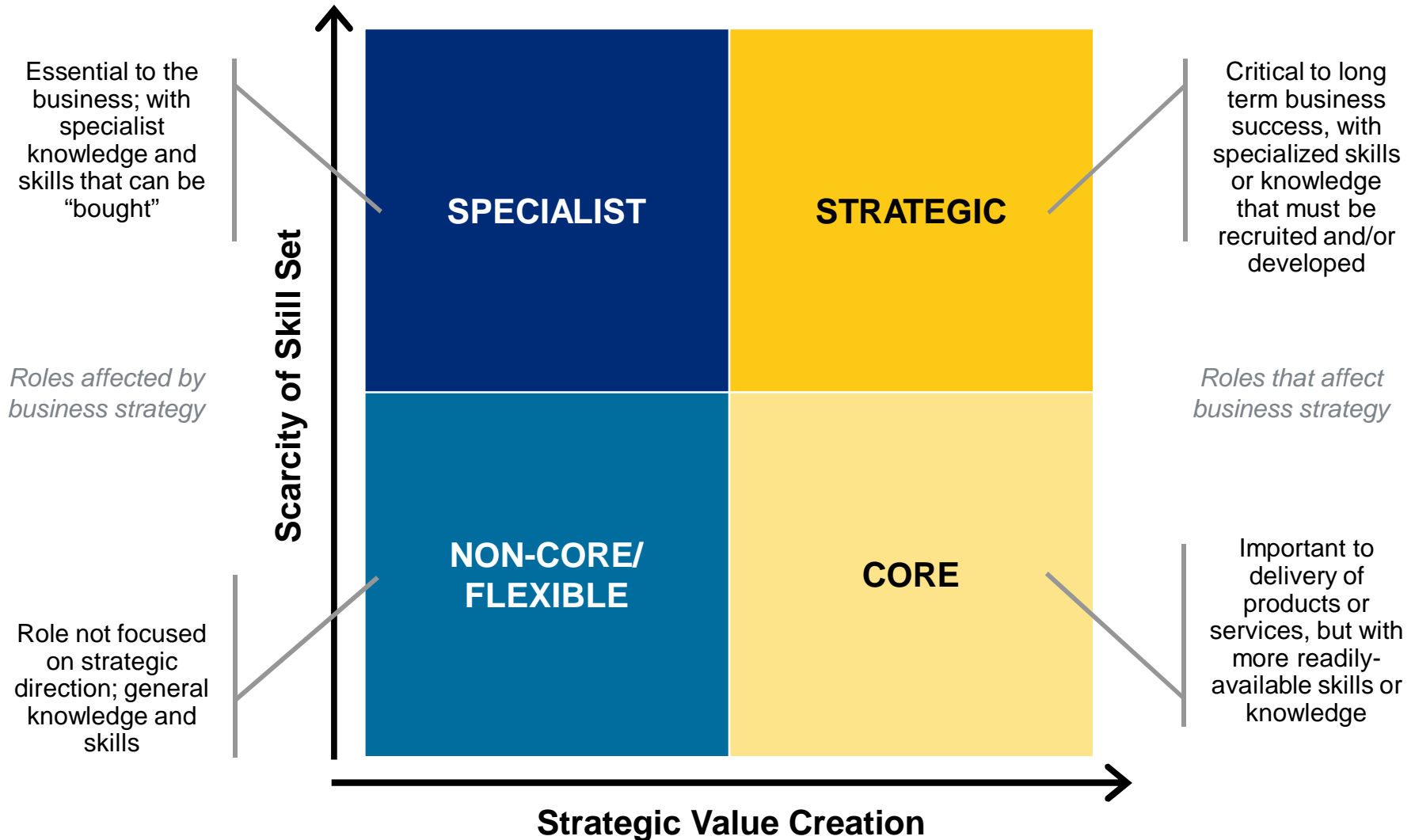
- **Strategy:** How do financial and operational imperatives inform future talent needs? Are current workforce trends sufficient to meet strategic objectives?

- **Structure:** Is the organization employing the "right" mix of roles and retaining top performers to support future business demands?

- **Sourcing:** How will future talent be supplied? Has it historically been sourced internally or externally? What changes are required?

- **Practices:** What policies or programs should be stopped, started, or modified to close the gap on talent risks?

What future workforce risks and/or opportunities are there in a transaction setting to validate or disprove the deal thesis?
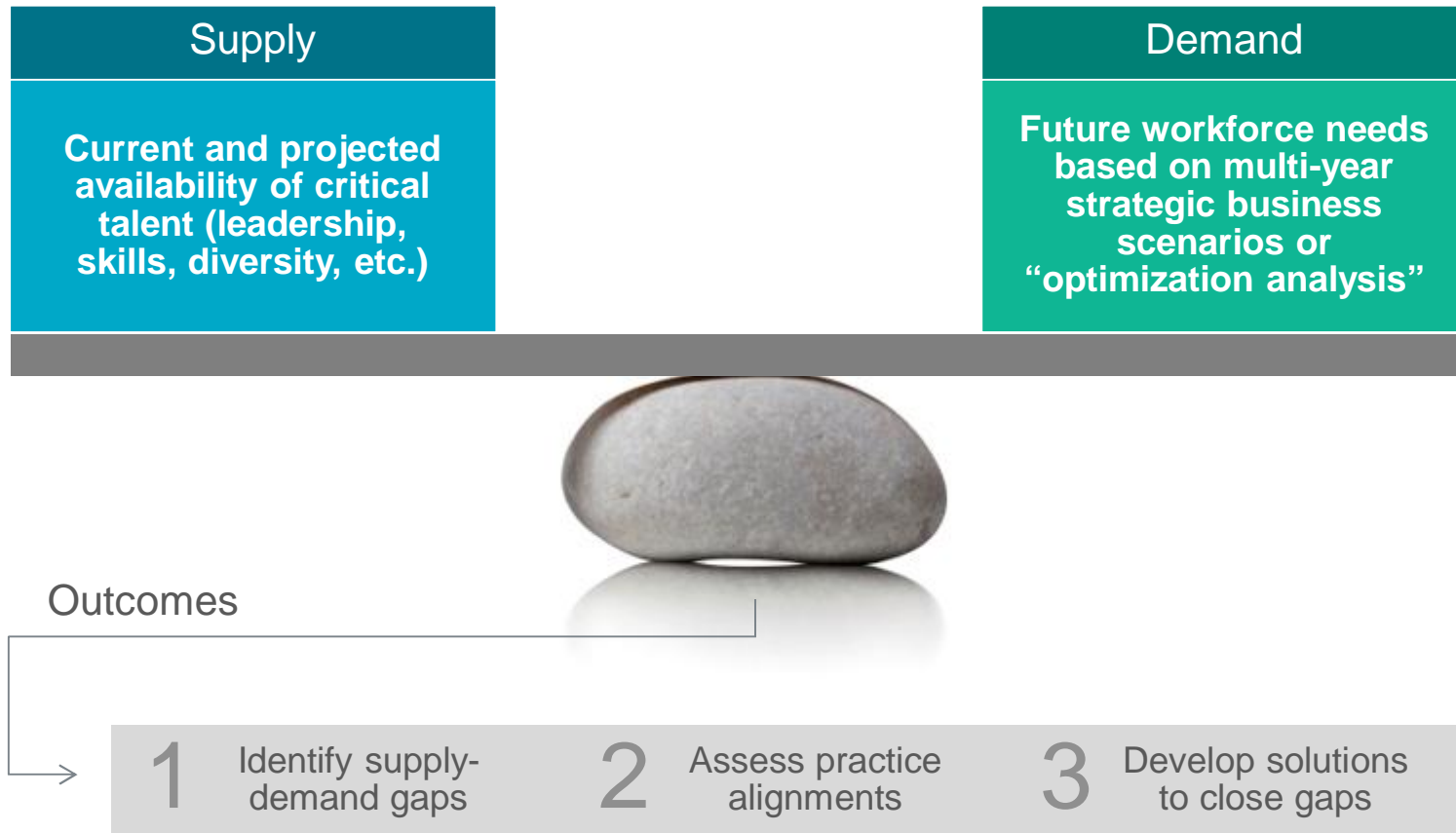
Strategic Context
Workforce Segmentation Categorizes Jobs or Job Families Based on Their Strategic Importance in the Business Context
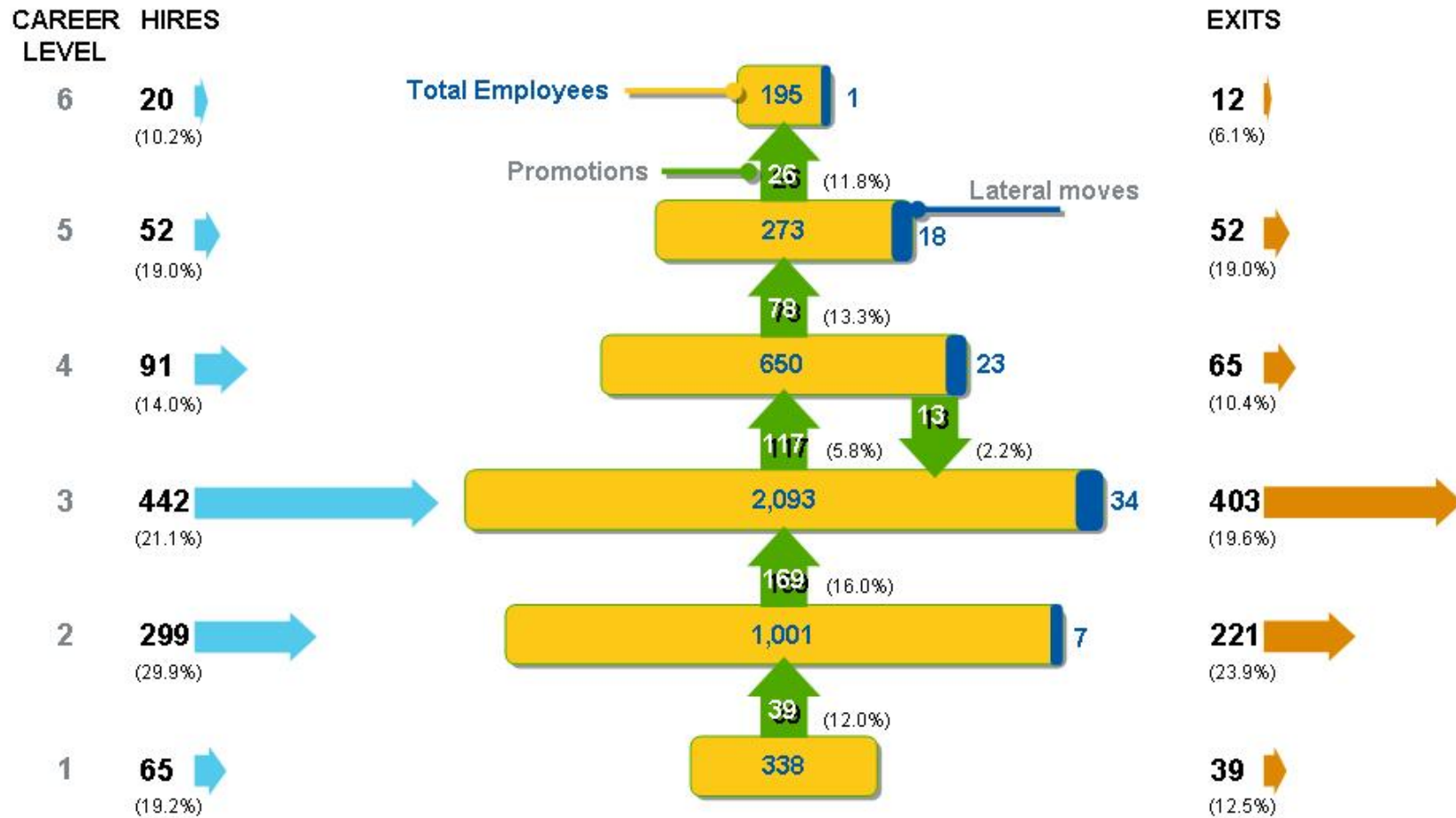
Essential to the business; with specialist knowledge and skills that can be "bought"

Critical to long term business success, with specialized skills or knowledge that must be recruited and/or developed

Scarcity of Skill Set

SPECIALIST

STRATEGIC

Roles affected by business strategy

Roles that affect business strategy

NON-CORE/ FLEXIBLE

CORE

Role not focused on strategic direction; general knowledge and skills

Important to delivery of products or services, but with more readily-available skills or knowledge

Strategic Value Creation

Adapted from The Conference Board, 2006

Talent Risk Assessment: A Workforce Planning Framework

Supply

Current and projected availability of critical talent (leadership, skills, diversity, etc.)

Demand

Future workforce needs based on multi-year strategic business scenarios or "optimization analysis"

Outcomes

1 Identify supply-demand gaps

2 Assess practice alignments

3 Develop solutions to close gaps

1. Identify Supply-Demand Gaps: *Internal Supply* Analysis
An Internal Labor Market (ILM)™ Map

DISGUISED CASE EXAMPLE 6

1. Identify Supply-Demand Gaps: *External Supply* Analysis
Looking to the External Labor Market

Legend is shaded to show actual range of incumbent aerospace engineers by postal code

	< 2
	2 - 6
	6 - 12
	12 - 20
	20 - 70

1. Identify Supply-Demand Gaps: *Demand* and *Gap* Analysis
Comparing Projected Supply Against Demand to Identify Gaps that Can Be Monetized

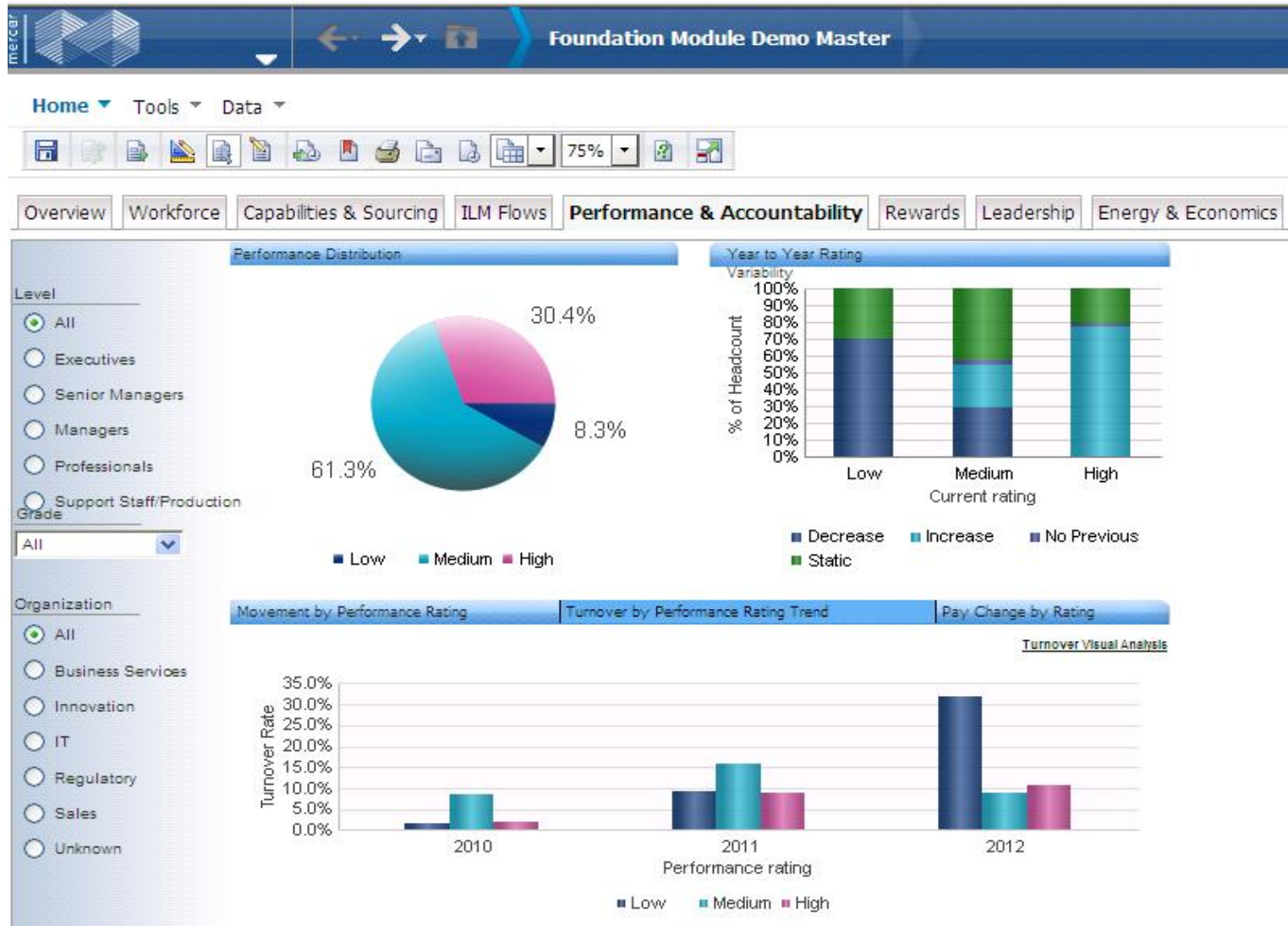*Demand Analysis:* Mapping business needs to workforce requirements

Shareholders' required returns (ROI, ROWC, etc.) → Required revenue/earnings growth → Required future headcounts for key workforce segments
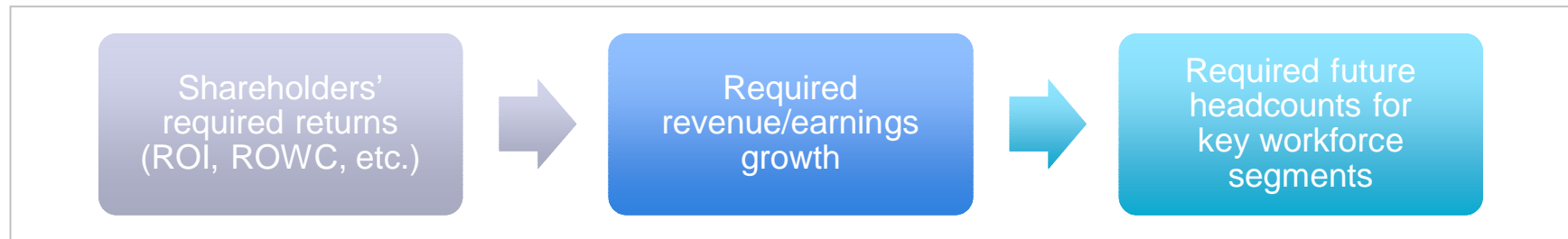
Gap Analysis:

Comparing both supply and demand inputs to identify future risk areas

DISGUISED CASE EXAMPLE   8

2. Assess Practice Alignments: Descriptive
Additional Analysis to Identify Misalignments

Statistical Modeling to Identify Further Misalignments and Help Close Gaps

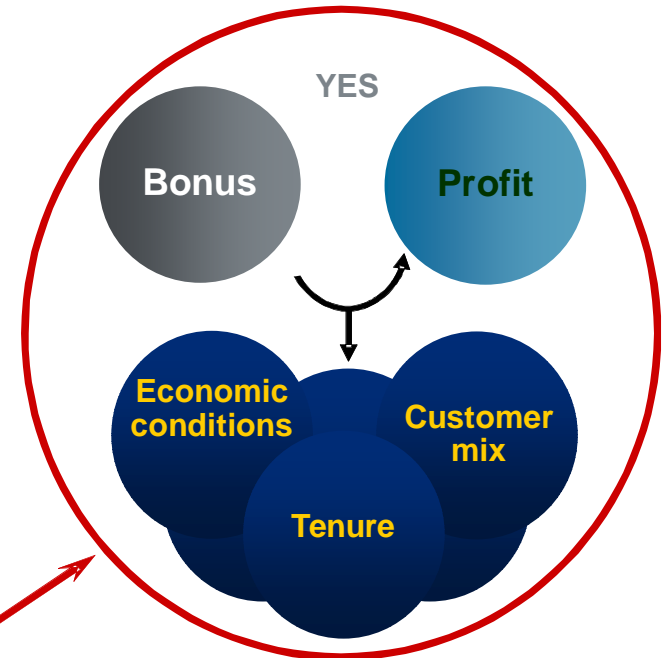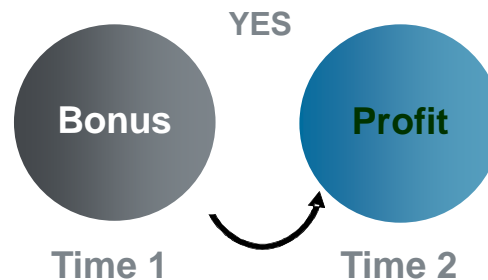*Three conditions* must be met to show that one factor drives another:

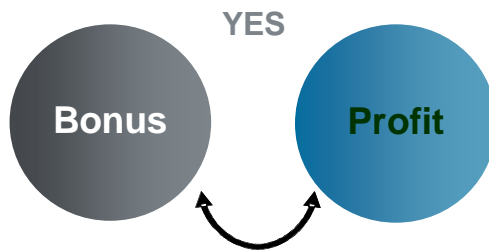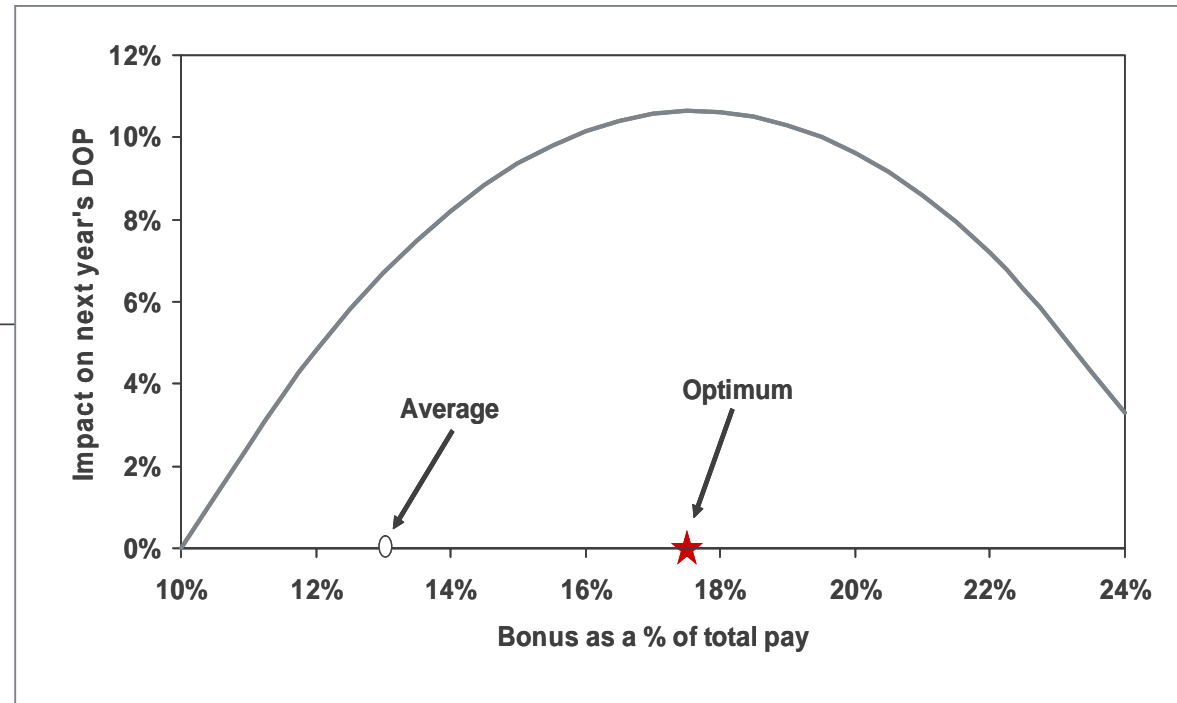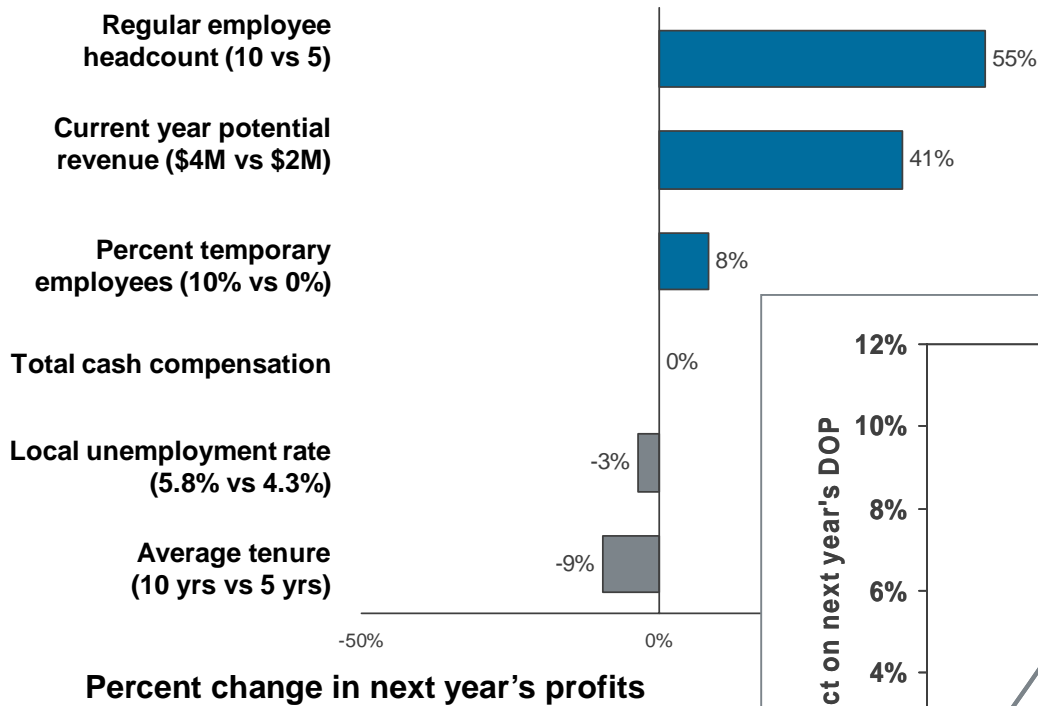| **1. CORRELATION** The factors are related.	**2. TIME** (Directionality) One *precedes* the other.	**3. ISOLATION** (Controls) Other factors are *ruled out.*

The key is to analyze multiple variables, then *isolate* those that *directly impact* the outcome

3. Develop Solutions to Close Gaps: Example #1
For This Logistics Company, Though Total Compensation Was Optimized, Enhanced Bonus Opportunity Showed Significant Potential

Regular employee headcount (10 vs 5) — 55%

Current year potential revenue ($4M vs $2M) — 41%

Percent temporary employees (10% vs 0%) — 8%

Total cash compensation — 0%

Local unemployment rate (5.8% vs 4.3%) — -3%

Average tenure (10 yrs vs 5 yrs) — -9%

-50%   0%

Percent change in next year's profits

Impact on next year's DOP (y-axis): 0%, 2%, 4%, 6%, 8%, 10%, 12%

Average

Optimum

Bonus as a % of total pay (x-axis): 10%, 12%, 14%, 16%, 18%, 20%, 22%, 24%

Disguised case example

The models on which these results are based control for individual attributes, organizational factors, and external influences.

3. Develop Solutions to Close Gaps: Example #2
For This Health Care Provider, Cost Reduction Led to Over-utilization of Part-time Employees
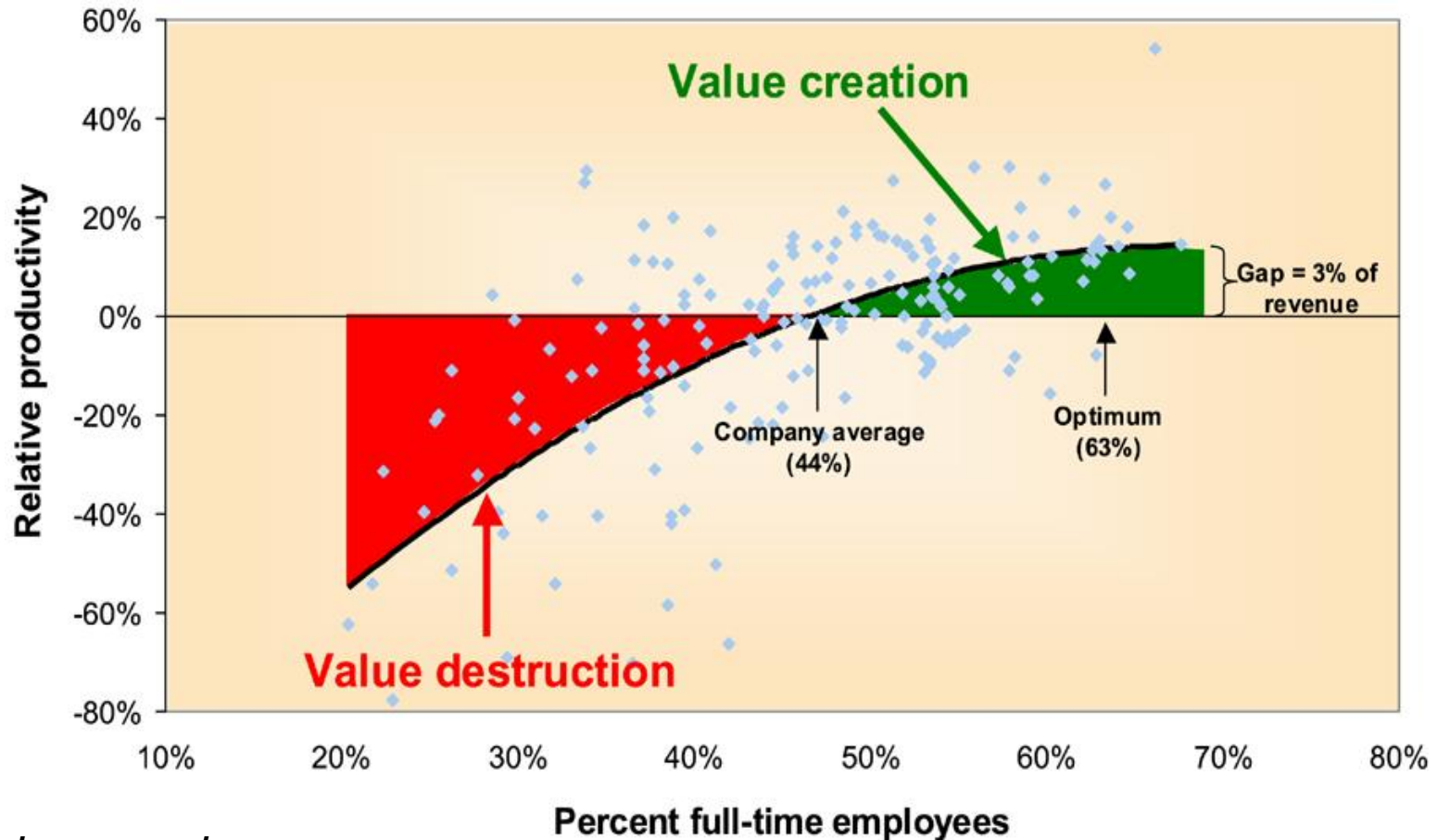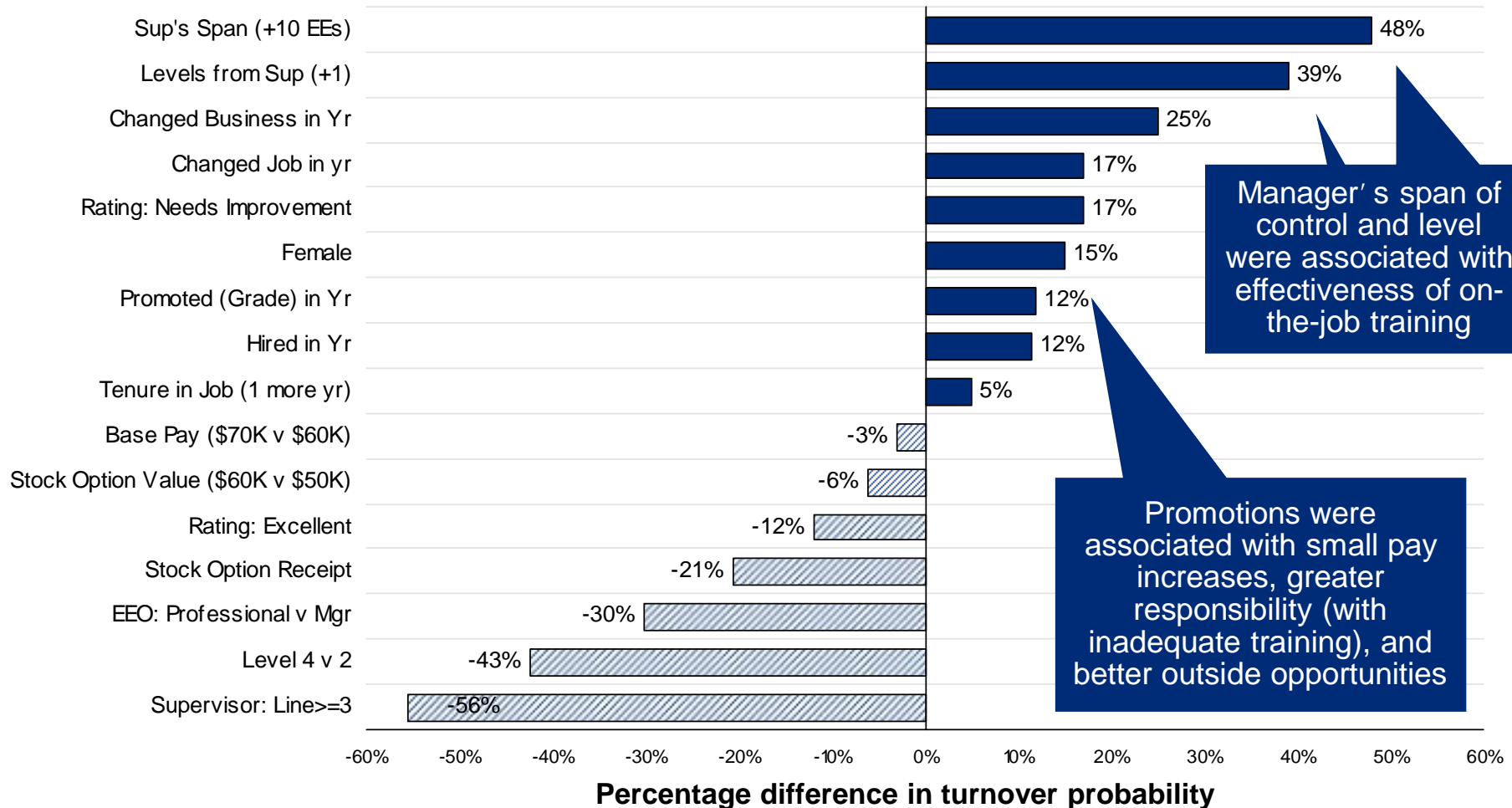

Disguised case example

The models on which these results are based control for individual attributes, organizational factors, and external influences.

3. Develop Solutions to Close Gaps: Example #3
For This Health Care Payer, Drivers of Turnover Clarified Need to provide Support and Development Through Small Spans of Control and to improve Retention of Promotees

Category	Percentage difference in turnover probability
Sup's Span (+10 EEs)	48%
Levels from Sup (+1)	39%
Changed Business in Yr	25%
Changed Job in yr	17%
Rating: Needs Improvement	17%
Female	15%
Promoted (Grade) in Yr	12%
Hired in Yr	12%
Tenure in Job (1 more yr)	5%
Base Pay ($70K v $60K)	-3%
Stock Option Value ($60K v $50K)	-6%
Rating: Excellent	-12%
Stock Option Receipt	-21%
EEO: Professional v Mgr	-30%
Level 4 v 2	-43%
Supervisor: Line>=3	-56%

Percentage difference in turnover probability

Manager's span of control and level were associated with effectiveness of on-the-job training

Promotions were associated with small pay increases, greater responsibility (with inadequate training), and better outside opportunities

The models on which these results are based control for individual attributes, organizational factors, and external influences.

DISGUISED CASE EXAMPLE

Case Study #1: Private Equity Firm

Talent Risk Assessment
Due Diligence

Key Questions and Sample Analyses

Objectives and Context

- Conduct an assessment of the target's Human Capital System to gauge risk factors that could undermine future earning expectations
- The target was a professional services firm where partners developed business and led projects, and "associates" performed the work
- There was a strong link between earnings and the number of partners – the target forecast 20% earnings growth over the next 5 years.

Key Questions

- How stable were target's partnership ranks – did these employee quit regularly (taking business with them); were many retirement-ready?
- Did the target have a track-record of promoting associates into the partnership ranks? Were the rates sufficient to achieve 20% earnings growth and replace losses, or were new partner-level hires needed?
- Did associates have an incentive to stay with the target while they waited for a promotion?
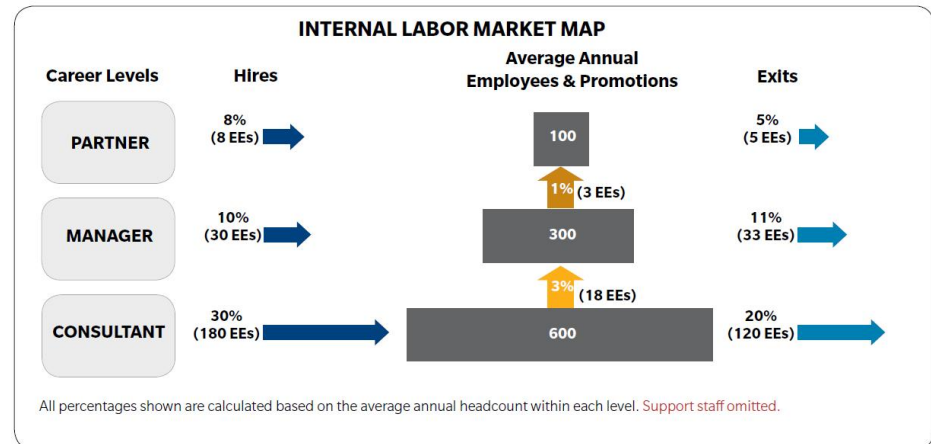
Activities

- Reviewed the target's internal labor market to understand historical inflows (hires), employees, workforce development (promotions, lateral moves), outflows (exits), employee distribution, and tenure dynamics
- Forecasted future workforce state, under status-quo assumptions of entries and exits, and under different scenarios of how to achieve the staffing levels needed to meet future earnings estimates.
- Reviewed existing rewards practices (financial and career advancement) at different career stages.

Sample Analyses

INTERNAL LABOR MARKET MAP

Career Levels	Hires	Average Annual Employees & Promotions	Exits
PARTNER	8% (8 EEs)	100	5% (5 EEs)
		1% (3 EEs)	
MANAGER	10% (30 EEs)	300	11% (33 EEs)
		3% (18 EEs)	
CONSULTANT	30% (180 EEs)	600	20% (120 EEs)

All percentages shown are calculated based on the average annual headcount within each level. Support staff omitted.
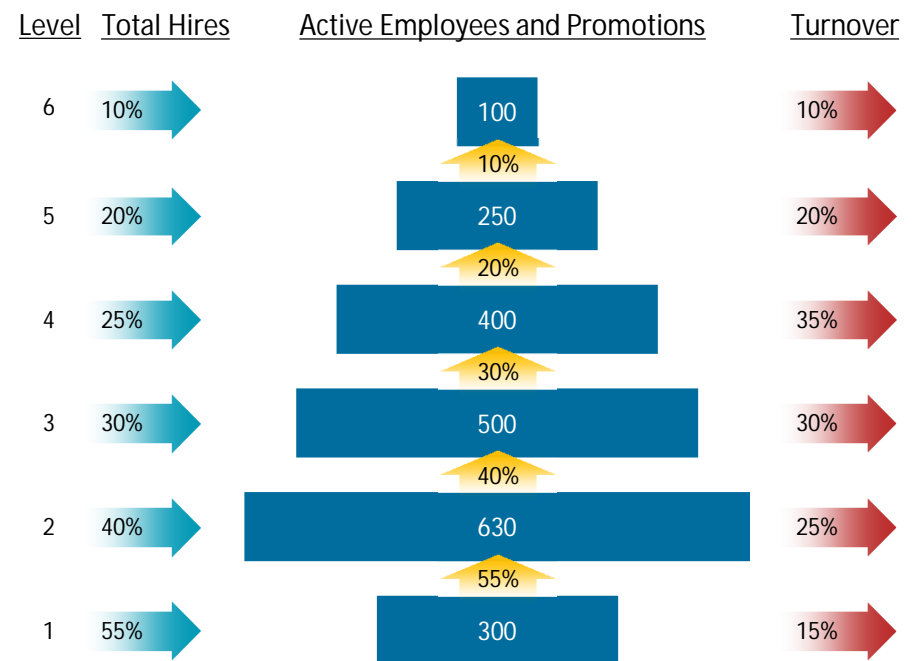
Case Study #2: Integration

This client faced the difficult challenge of blending the "high velocity" culture of the acquired company with its own internal labor dynamics

Acquiring organization (Company A)

Level	Total Hires	Active Employees and Promotions	Turnover
A	0%	750	1%
		5%	
B	0%	900	2%
		10%	
C	5%	1,110	4%
		15%	
D	5%	1,160	8%
		25%	
E	15%	1,100	10%
		40%	
F	30%	900	15%

Acquired organization (Company B)

Level	Total Hires	Active Employees and Promotions	Turnover
6	10%	100	10%
		10%	
5	20%	250	20%
		20%	
4	25%	400	35%
		30%	
3	30%	500	30%
		40%	
2	40%	630	25%
		55%	
1	55%	300	15%

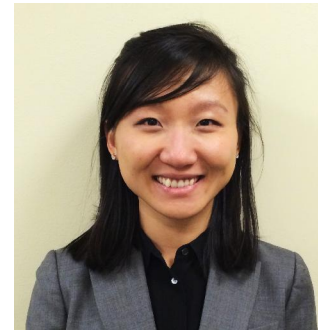**DISGUISED CASE EXAMPLE**

Questions

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QUESTIONS
Please type your questions in the Q&A section of the toolbar and we will do our best to answer as many questions as we have time for.

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