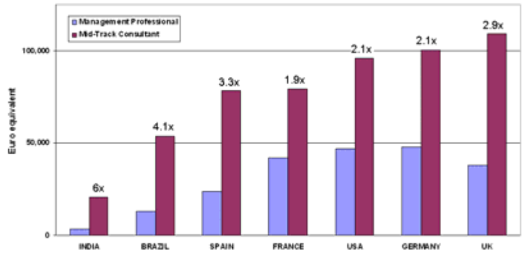
Remuneration Perspectives

4th Quarter - October 2005

"A World of Difference?"

Given the nature of its international recruitment practices, its global clients and multi-national projects, Strategy Consulting has probably the most geographically mobile workforce in the World. In this article we look at how salaries in the Strategy sector accommodate the huge variation in domestic economies between the New World and the Developing World.



To the outside observer, Strategy Consulting must appear as Capitalism Incarnate. Graduates of the World's leading business schools, driven by analysis, structure and logic, they hold up the mirror of market forces and competitor threats to CXOs around the globe and challenge them to face the grim reality of 'Evolve or Die'. Consulting itself has not been immune to market changes over the last years, and is only now emerging from its first prolonged period of 'negative growth' in a generation. Consequently, our outside observer might expect that Strategy Consulting, of all industries, would operate a Darwinian salary structure – drive your primary costs to the lowest price location, and every man (and woman) for himself. In such an environment we could expect to see radical variations in earnings between individuals and/or national offices, as 'Survival of the Fittest' rules.

Yet immediately we see an obvious and fundamental conundrum at the higher reaches of the leading management consulting firms. Perhaps more than any other industry, consulting partners are internationally mobile: they all speak fluent English, many will be alumni of the same elite International Business Schools, their clients are usually trans-national, and international travel is often merely the prelude to another day in the office. Hence location alone, even on a Continental scale, cannot justify significant variation between a firm's partners. As a result, there is considerable homogeneity in the earnings of Partners and Vice Presidents of the major firms. Indeed, Vencon Research International's most recent Partner Compensation Study, which compares the aggregate compensation for partners across a number of global firms, confirms this parity of reward at Senior and Experienced Partner levels, irrespective of geography. Simply put, at the top level, mobility precludes differentiating purely on the basis of location.

But how does the reward structure look lower down the consulting hierarchy? For this we shall refer to Vencon Research International's Strategy Consulting Compensation Studies, which collate, compile and cross-refer thousands of salary data points from nearly 40 countries bi-annually.

In framing the situation, we start with an obvious fact: the global market in Management Consulting originated in, is driven by, and continues to be dominated by the US. In an industry worth an estimated $125 Billion in 2004, the US comprises 46% (see Figure 1 below). Indeed, at the turn of the Millennium the US represented over half the World's Management Consulting market, but deeper and faster reaction to the market downturn in the US and – much more significantly – an up to 30% decline of the dollar against the Euro means the combined consulting markets of Europe now almost equal US revenues when expressed in dollar terms.

Asian markets, though experiencing strong growth, are much smaller, representing just under 8% of the global market, whilst "Rest of the World" equates to only 5% of the world market for Management Consulting.

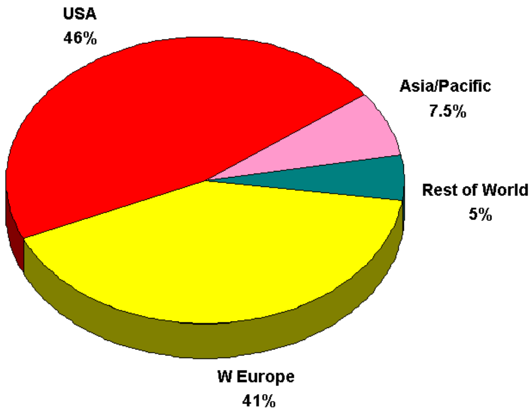


Figure 1: In 2004 the Global Management Consulting Market was estimated at $125 Billion

Management consulting, of course, is driven by economic activity. Overlay a graph of Global GDP growth with growth in management consulting revenues and you will find an almost perfect match.

Of course the service lines most in demand will vary, depending on whether the global markets are growing – when strategy and big infrastructure projects are in demand – or in downturn, when Outsourcing, HR consulting and BPR are dominant.

Consequently strategy consulting was particularly badly hit by the economic downturn of the new millennium. On most recent data those lines which fall under the heading of 'strategy' - Corporate Strategy, M&A, Financial Advisory, Strategic Marketing – made up around 20% of our $125 Billion market. In theory, therefore, strategy consulting should now be experiencing greatly increased demand, as global GDP growth hits a 20 year high.

The reason for the concentration of consulting in the US and Western Europe is clear from Figure 2 below – this shows the World, with each country scaled to represent its GDP.

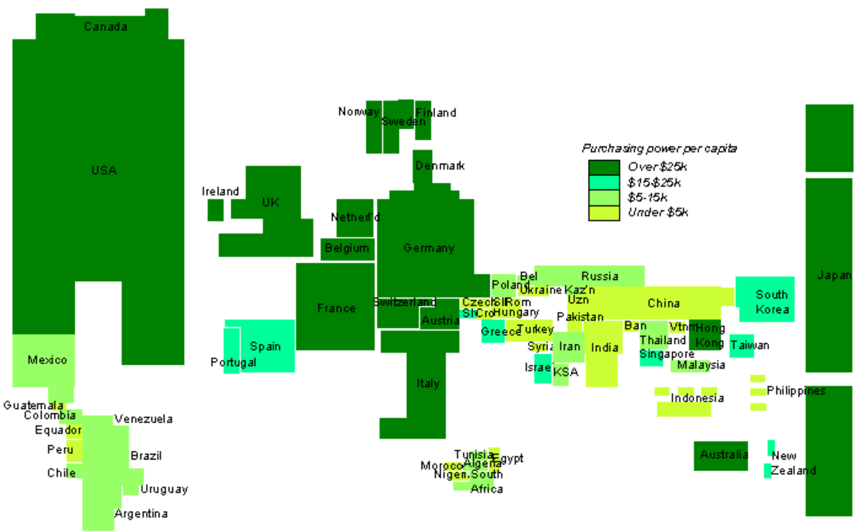


Figure 2: The World, with Nations represented in proportion to their GDP

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Big economies equal big consulting markets, thus it’s no surprise that the US represents the single largest consulting market, or that the UK, France and Germany between them make up over 70% of Europe’s $50 Billion consulting market. Conversely, despite India having a population nearly 4 times that of the US, its GDP is only 6% that of the US. India presents a high growth opportunity, certainly, and therefore high potential for consulting, but as a developing market it will clearly be some time before India becomes a critical source of revenue for the international consulting firms.

Figure 2 adds a further dimension to our analysis, that of GDP per capita. This ranges from something over $40,000 in the US to barely $600 for India. Note that the GDP figures we are quoting here are in absolute dollar terms, rather than Purchasing Power Parity (PPP), which is often used for international comparisons. PPP is useful in reflecting relative cost of living or disposable income between countries, but we are addressing salary comparison amongst a consistently-skilled international population; people who may find themselves working alongside colleagues from several other countries, on a project which is being billed in dollars from yet another location; in this scenario, PPP has limited relevance. Consultants compare income in absolute terms.

So returning to our original question: “How does strategy consulting – this highly mobile, highly educated and highly international population – accommodate such massive variation?” To find an answer we have taken data from a range of territories, all with viable and sustainable Strategy Consulting markets, and for which Vencon Research has comprehensive consultant earnings data. For this exercise we have used data from Brazil, France, Germany, India, Spain, the UK and the USA.

First of all, we have set out the relative ‘wealth’ of these countries. Table 1 establishes the GDP per Capita - again in absolute, rather than PPP terms. These are then ranked to give relative GDP/Capita compared to a base-line country, which we have set as India.

Table 1 - Sample Countries – Basic Data

	GDP ($ Bn)	Pop. (Mio.)	GDP/capita	
			(in $)	Rel. to India
INDIA	650	1,064	620	**1**
BRAZIL	493	182	2,790	**5**
SPAIN	972	41	23,700	**38**
GERMANY	2,687	82	32,770	**53**
FRANCE	1,997	60	33,280	**54**
UK	2,115	60	35,250	**57**
USA	11,664	290	40,220	**65**

Of course, in ‘buying power’ terms, the average consumer in the US doesn’t really have 65 times the resources of his Indian counterpart, but when paying International salaries and remitting International revenues we need this fixed reference. This does not ignore the fact that a five figure salary will go a lot further in Mumbai than in Manhattan.

To see how this translates into earnings relativities in the general market, we have used data produced by Swiss Economic Research on behalf of UBS AG.

Using this study, we created a composite ‘management professional’ profile, averaging the gross income of a Graduate Engineer with 5 years experience and of an Operations Manager of a 100 person production unit, across the same geographies. Taking an average for these two roles smoothes certain local market anomalies: for example, the comparatively poor status of professional engineers in the UK, or of large operations managers in India. These data have then been corrected to reflect latest exchange rates.

Table 2 below shows how our ‘Management Professional’ fares in absolute income per country, and again ranks this against a base-line figure for India. The range here is much less than that seen with GDP/Capita, our highest earning professional now earning ‘only’ 14 times as much as his Indian counterpart. We have also included comparison data which averages earnings for a ‘basket’ of 13 different jobs, mostly at more junior levels, which shows how much the salary variation in lower paid jobs can skew the result.

Table 2 - Relative Earnings for Equivalent Management Roles

	GDP($ Bn)	Mgmt. Professional		'Basket' of 13 jobs – Rel. to India
		(in $ Gross)	relative to India	
INDIA	650	4,430	1	1
BRAZIL	493	16,600	4	3
SPAIN	972	30,525	7	13
GERMANY	2,687	48,525	11	23
FRANCE	1,997	53,600	12	19
UK	2,115	59,755	13	20
USA	11,664	61,200	14	29

The pattern that emerges is of the ‘affluent West’ achieving significant consistency in professional earnings, with the US, UK, France and Germany, having broadly similar levels of GDP/Capita, all paying within +/-10% for our management professional role. Interestingly, even in the West, the earnings spread doubles to +/- 20% once the basket of jobs – including lower paid - is included.

It is clear, then, that it is in lower paid jobs where the greatest discrepancy arises between ‘affluent West’ and Developing World – their inclusion in the ‘basket‘ of jobs produces an average income nearly 25 times higher than similar roles in India.

We are now in a position to overlay data from the Vencon Research surveys, to see how these international comparisons look for a population of Strategy Consultants.

For this we have taken data collected in the third and final quarter of 2004, and used it to construct an Actual Total Cash Compensation (aTCC) line. For those unfamiliar with the Vencon Research International survey format, the studies tabulate earnings for up to 12 designated career points for a pre-partner consultant. In each country data are presented for up to 18 strategy consulting firms, giving base salary, actual and theoretical bonus and career timescale for each position per firm.

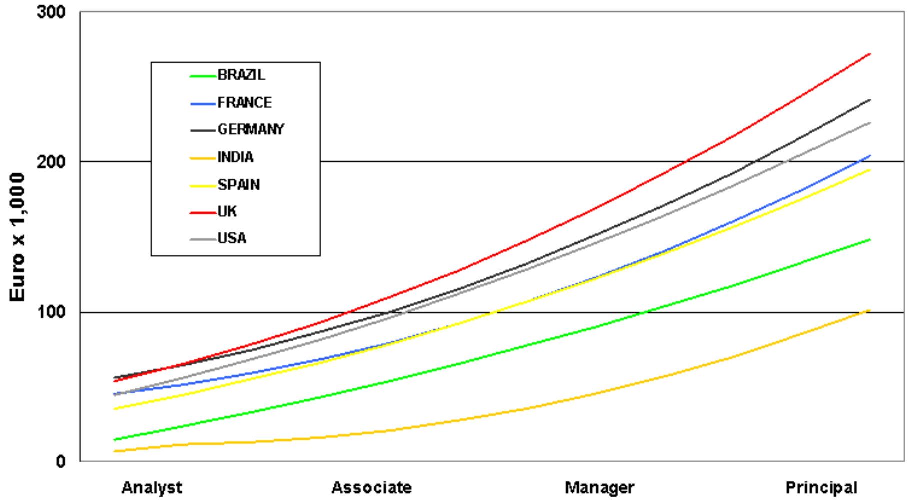

Figure 3: Strategy Consulting – Actual Total Cash Compensation (Regression Line)

For Figure 3 we have taken the average of the aTCC data – that is, base salary plus actual bonus paid – and applied polynomial regression to give an accurate trend line. The data are presented in Euros, converted at the rate obtaining at the time of the Q4/2004 survey.

Immediately we can identify some key attributes of Strategy Consulting. Even at the most junior level (entry Analyst) the difference between the lowest paying country (India) and the highest (Germany) shows a relative earnings ratio of 8:1, as opposed to the 14:1 we saw with our composite ‘Management Professional’, or the 29:1 ratio seen for the ‘basket’ of jobs.

In relative earnings terms this differential then closes throughout the consultant’s career. By the time we reach the ranks of an experienced Principal the maximum earnings differential is less than 3:1 between the highest paying country (UK) and the lowest (India). Given the differentials we have seen not just in GDP/Capita, but even in the ranks of Management Professionals, Strategy Consulting starts to look notably egalitarian!

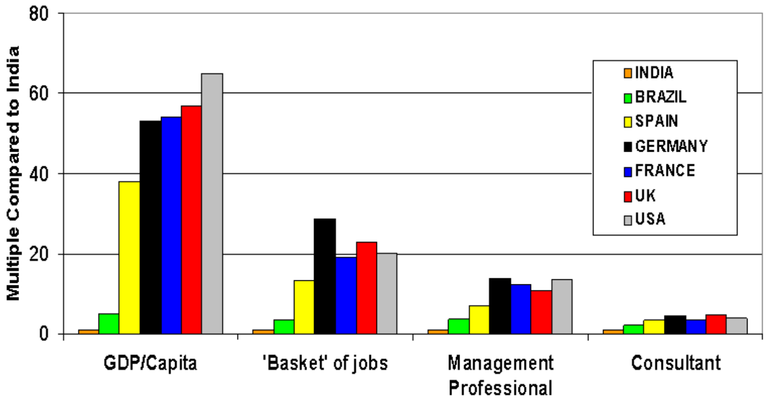

Figure 4: Relativities between sample countries

In fact Figure 4 above shows the extent to which Strategy Consulting has succeeded in achieving a consistent international compensation policy. Here we have taken the Actual Total Cash Compensation (aTCC) for a mid-track Strategy Consultant, scaled it against our standard reference value of India, and compared the variation against the other factors we have examined. It is immediately apparent that, although the variance in Consultant earnings can be significant between countries, it is dramatically less than the variation in any other market dimension.

Returning, then, to our opening premise: Strategy Consulting should be, by its very nature, an industry that will migrate to the most cost-efficient location. But if this is not the case, then how, with probably the most geographically mobile workforce in the World, does Strategy Consulting accommodate the huge variation in Salaries between New World and 'Developing World'?

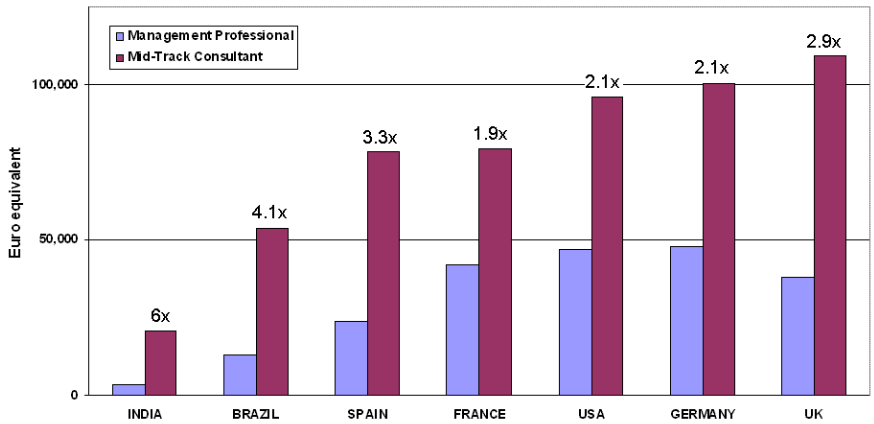

Figure 5: Relativities between sample jobs

In fact, as we see from Figure 5, if we compare the annual dollar earnings of a mid-track Consultant with a generic 'Management Professional' contemporary we find that in India the consultant is earning 6 times as much as the Management Professional, whereas a counterpart in the 'affluent West' is on a mere 2 to 3 times multiple (Figure 5). Strategy Consulting has therefore achieved an impressive balance – by paying its 'Developing World' staff disproportionately well against the local market it can be confident they are more than content with their compensation and status, but can still deliver substantial cost benefits against 'affluent West' pay-scales. In effect, against local market rates, consultants in India are much better off than their counterparts in the US – by a factor of 3 times.

So will this lead to substantial off-shoring of research and analysis? And what is the impact on local billing rates? Further research, and future articles, may hold the answers ….

Sources: Vencon Research International; OECD; World Bank: CIA World Factbook: UBS; Financial Times; FEACO.