

## **GM, Fedex Pay Cuts Add to Deflation Risk as Economy Staggers**

By Jeff Green and Alex Ortolani



Feb. 11 (Bloomberg) -- General Motors Corp., FedEx Corp. and Wynn Resorts Ltd. are among companies slashing pay for more than 100,000 employees, contributing to U.S. deflation that could worsen the economic slump.

GM will reduce salaries for about 26,000 U.S. workers and fire 3,400 more to reduce costs, the Detroit automaker said yesterday. FedEx in December announced a 5 percent reduction for 36,000 workers to offset fewer packages delivered, and dwindling gambling revenue prompted Wynn to trim pay this month for all salaried workers in Las Vegas.

“Pay cuts are the last steps companies make,” said John A. Challenger, chief executive officer of the Chicago-based placement company Challenger, Gray & Christmas Inc. “Watching salaries get cut like that is a signal of deflationary pressures out there.”

Smaller paychecks, \$3.3 trillion in lost home value last year and 649,506 U.S. jobs eliminated since Nov. 4 may work together to deflate prices. The thinner pay stubs mitigate the economic benefits of plunging fuel prices and tax reductions expected this year as part of the stimulus package.

“We’re going to have a lot of slack in the economy and that slack is going to force prices to fall,” said Desmond Lachman, an economist at the American Enterprise Institute. “When you cut wages, what it means is that people don’t go out and buy and then companies are forced to make deeper cuts.” Deflation is the opposite of inflation. It means a general drop in prices, often as part of a severe economic slowdown.

GDP Declines

The U.S. gross domestic product, the market value of all final goods and services produced in the country, declined 3.8 percent in the fourth quarter and is forecast to fall 1.5 percent this year, the median estimate of 60 economists surveyed by Bloomberg.

Newspaper chains such as Gannett Co. Inc. have ordered employees to take unpaid one-week furloughs. Home Depot Inc., the world's largest home-improvement retailer, said Jan. 26 it was demoting some of its officers to non-executive classifications as part of a 2 percent reduction in staffing as consumer spending slowed.

On Wall Street, bonus earnings also will drop. UBS AG was told to reduce bonuses after the Swiss government gave the country's biggest bank a \$59.2 billion lifeline. Bank of America Corp. is under pressure to scale back payouts after New York Attorney General Andrew Cuomo subpoenaed executives two weeks ago for information on compensation.

The January consumer price index numbers, due next week, will likely show a decline for the previous 12 months that may continue for the next several months, said Comerica Bank Senior Economist Dana Johnson. Consumer prices fell 0.7 percent in December after dropping 1.7 percent the prior month.

In a Jan. 28 statement, the Federal Open Market Committee warned of a prolonged global economic slowdown that may push the U.S. to the brink of deflation.

### Deflation Risk

"We're definitely going to hear concern for the next six months by people at the Fed that deflation is a clear risk," Johnson said. "Even if they aren't cutting pay, a lot of companies are holding the line, freezing pay and bonuses. Even freezing pay is pretty harsh. Cutting pay is rare."

About 33 percent of U.S. companies may freeze pay this year, an increase from 25 percent last year, according to a Jan. 22-29 survey of 400 mid-size and large companies released Feb. 9 by Mercer, a compensation consulting company in New York. The survey did not include questions about pay reductions.

Hewlett-Packard Co., the world's largest personal computer maker, announced a pay freeze in December and United Parcel Service Inc., the world's largest package-delivery company, froze worker pay Feb. 3 after U.S. volume plunged the most in nine years.

**"Pay cuts will work better in 2009 than in any time in the last 70 years," said Van Conway, managing partner of Conway MacKenzie, a restructuring consulting firm in Birmingham, Michigan.**

## **'Saving a Company'**

**“In the past, they might have been able to find another job. Not in these times. In the short term it’s painful, but it’s about saving a company,” said Conway, who said most of the 30 companies with which he consults, ranging from \$30 million to \$4 billion in revenue, are considering or asking for pay trims to survive.**

Steelcase Inc., the world’s largest maker of office furniture, said Feb. 2 it will diminish salaried worker pay by at least 5 percent in North America, where the Grand Rapids, Michigan, company has 3,300 non manufacturing workers. Lincoln Electric Holdings Inc., the world’s largest welding-equipment maker, said the same day it would reduce executive pay as much as 45 percent.

Auto-parts makers Visteon Corp., ArvinMeritor Inc. and Tenneco Inc. also have cut pay for senior executives amid losses in the fourth- quarter due to lower vehicle production at GM, Chrysler LLC and Ford Motor Co.

“This is probably one of the most significant problems that is out there,” said Brian Bethune, chief financial economist at IHS Global Insight in Lexington, Massachusetts. “There was a lot of deflationary momentum built up in 2008 and now we’re just seeing the negative consequences from that.”

## Spending and Production

The drop in household net worth and the fall of asset prices is combining “to restrain both spending and production,” he said. “Once you get into that spiral it’s very hard to extricate yourself from it.”

“A deflationary tidal wave is what I call it,” he said.

Prices for clothing, new automobiles, airline fares and recreation all decreased in December. The 3.2 percent drop in new-car prices in 2008 was the biggest since 1971.

The firings may have peaked in January though the pay declines probably will continue as companies try to wait out the decline, Challenger said. When the recovery begins, workers with less money will be slower to increase discretionary spending.

“The pay cuts make it harder to bounce back,” Challenger said. “It is the most sticky of cuts a company can make. If we cut into muscle, it robs an individual company or the economy of its rebound potential, its springback.”