



# Purchasing Power Parity

It can be a difficult task to coordinate recognition programs and ensure your employees have equal opportunity to receive recognition of a similar value across international borders.

Thankfully it's easy to configure a recognition program in Awardco that allows employees to access high-quality redemption options of the same value as their peers around the world by establishing purchasing power parity (PPP) in your Awardco platform.

## What is Purchasing Power Parity?

Applying purchasing power parity in the Awardco platform ensures the purchasing power of \$1 USD is adjusted to account for the local economy and the local spending power provided by \$1 USD. To understand purchasing power parity, it is critical to understand what purchasing power is at its core. The following example further explains and illustrates the principle of purchasing power.

A platform user named Alexandra recognizes 5 coworkers around the globe. They all participated equally on a project and Alexandra wants each of her team members to receive the same reward. She submits a recognition for 100 points\* and each coworker is awarded 100 points.

Since the platform is based in USD, 100 points represents \$100 USD of purchasing power for each user. For her British coworker the \$100 represents £77, for her French coworker the 100 points represents €90, and for her Japanese coworker the 100 points represents ¥10,864. This is great, because they all get the same \$100 USD. One could easily argue that is a fair distribution of points!

Unfortunately, this recognition system did not account for how the purchasing power of \$100 USD changes in different locations. By leveraging a purchasing power index, we're able to see how much an individual can buy in different places with the same monetary value. Returning to the example above, if I exchanged \$100 USD to the British Pound, I would walk away with £77. Although \$100 USD and £77 carry the same monetary value, I can't necessarily buy the same things with £77 in London that I could with \$100 USD in New York City. With this purchasing power inequity, it makes sense to adjust the purchasing power of an award to account for local spending power. For example, in the UK the PPP index is roughly 0.91 or 91% of the US. This means that an item which costs \$1 in the US would only cost, on average, the equivalent of 91¢ in the UK. Conversely, in Japan the index is roughly 1.13 or 113% of the US. An item which costs \$1 in the US would generally cost the equivalent of \$1.13 in Japan.

Awardco systems are able to set a PPP ratio on a country-by-country basis to indicate how far the purchasing power of \$1 USD goes in the countries in which your organization is operating.

## How is Parity Achieved?

Awardco has 2 different ways to accomplish purchasing power parity: adjustment at reward and adjustment at redemption.

### Adjustment at Reward

The first way is to adjust the power of the points when the award is distributed. When a user rewards a coworker, the amount is immediately adjusted to account for the difference in spending power. Again, using the example of the UK which has a PPP ratio of 0.91, when a coworker in the UK is recognized for 100 points the reward is immediately adjusted by 91%. The user receives a 91-point award and the recognizer will see only \$91 USD removed from their budget. These 91 points represent the \$91 USD of purchasing power they have. When the user redeems their points, they will be able to buy \$91 USD of goods. Remember, \$91 USD will go just as far in London as \$100 USD would go in the US.

In utilizing this option, Awardco strongly recommends that all international countries on your platform have a PPP ratio that is less than 1. This is because if the user sending the recognition sent an award for 100 points to a user in a country with a PPP ratio higher than 1, the amount sent to the recipient would be greater than the amount the user agreed to award from their budget.

For example, in Japan the PPP index is approximately 1.13. This means it would take \$1.13 USD to buy the same item in Japan that could be purchased for \$1 USD in the US. To award the proper PPP adjusted value, \$100 USD would cost \$113 USD. If you configure your Awardco platform to achieve parity through this 'Adjust at Reward' method, when awarding to countries with a ratio higher than 1 the system will not adjust the award. In Japan, even though PPP dictates the award should be worth \$113 USD, the user would not be awarded \$113 USD but would be awarded \$100 USD. This may be unfortunate for the Japanese employee, but it helps keep budgets in check.

### Adjustment at Redemption

The second way to account for the difference in spending power is to adjust the power of the points at redemption. This means that when a user recognizes a coworker, no amount is adjusted at the time of recognition. The user receives the full amount of points. A UK user awarded 100 points would receive 100 points. When the user redeems those points, calculations are made based on the purchasing power index to adjust the power of the redemption according to the countries' index ratios. When redeemed, the 100 points would purchase \$91 USD worth of goods.

In this case, since the reward is not adjusted, the full value can be leveraged by the recipient, regardless of whether the final cost is greater than the intended spend. Again, as the index is 1.13 in Japan, at redemption, a Japanese user who was awarded 100 points would have \$113 USD of purchasing power. This can make it difficult to successfully budget your award spend. In Japan, the reward is being redeemed for 13% more than anticipated.

### Summary of How Parity is Achieved

There are two different ways to apply a purchasing power index to accomplish purchasing power parity: adjusting the points when the user is rewarded, and adjusting the points when the user redeems those points.

The 2 main differences in the two processes are:

1. What amount the user sees in their balance
2. Through the adjustment at reward method, users in countries with an index value greater than 1 will not receive the full value of their award but would receive the full value through the adjustment at redemption method.

## Where Do the Rates Come From?

### Exchange Rates

Awardco has a standardized approach to the applied exchange rate. These rates are based on current markets and are configured each year at the first of the year, holding constant for 12 months. Using a standardized exchange rate establishes consistency, especially with currencies with extreme rate fluctuation.

### Purchasing Power Ratio

Awardco provides a standard set of rates that are adjusted annually. These rates are sourced by Mercer's "standard market basket" calculations with the intent to provide a country-wide footing in establishing purchasing power as it relates to the United States.

Awardco is able to import custom rates and ratios should an organization choose to input their own values.

### Next Steps for Configuring PPP in Your Platform

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1. What amount the user sees in their balance
2. Through the adjustment at reward method, users in countries with an index value greater than 1 will not receive the full value of their award but would receive the full value through the adjustment at redemption method.

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\* In the examples contained in this document, a 1 point to \$1 USD platform point ratio is assumed.