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An exploration of executive compensation in Croatia - what are its implications within corporate governance?

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Introduction

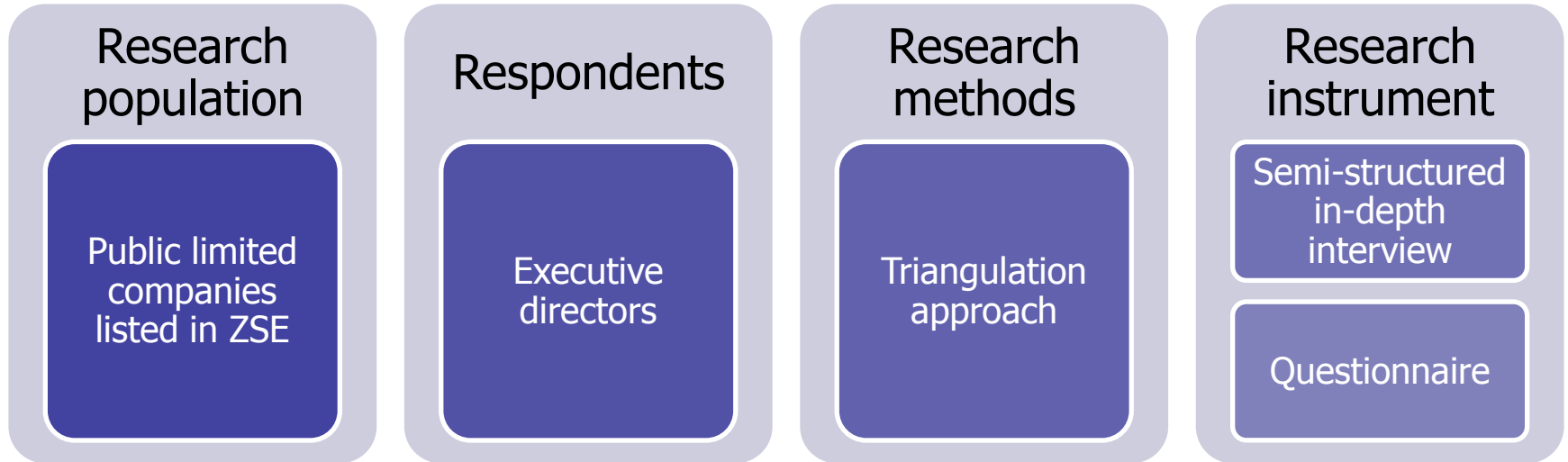
- Executive directors influence firm performance (Chingos et al., 2004.)
- How to structure executives' compensation package?
- The importance of compensation setting processes
- Open issues in executive compensation
- **Agency theory as the basis for executive compensation**

Executive compensation in transition economies

Table 1: Description of senior executive compensation in transition economies

Slovenia	Bulgaria	Czech Republic	Slovakia
<ul style="list-style-type: none"> •Ratio senior executive pay to employee pay: 5,8 (Slapničar et. al., 2005) •Bonus to total compensation of senior executives: 15% (Slapničar et. al., 2005) •In about 25% of the sampled companies the second performance-contingent part of compensation is managerial profit sharing •Stronger ownership concentration does not bring to a stronger link between pay and performance (Slapničar et. al., 2005) 	<ul style="list-style-type: none"> •During 1995 the annual CEO compensation was about 3,07 times the average workers wage (Jones&Kato, 1995) •The only performance variable which is found to influence changes in CEO pay is total assets (sensitivity of 0,00004) (Jones & Kato, 1996) 	<ul style="list-style-type: none"> •CEOs earn 60-80% more than executives at the next level of the hierarchy in the firm (Eriksson, 2005) •Managers in Czech state-own firms obtain the same pay as in privately owned firms (Eriksson, 2005) •statistically significant and a positive relationship between the changes in pay and change is corporate performance measured in profit/sales (Eriksson, 2005) 	<ul style="list-style-type: none"> •CEOs earn 30-40% more than executives at the next level of the hierarchy in the firm (Eriksson, 2005) •Ownership structure affects executive compensation (Eriksson, 2005)

Methodology of research



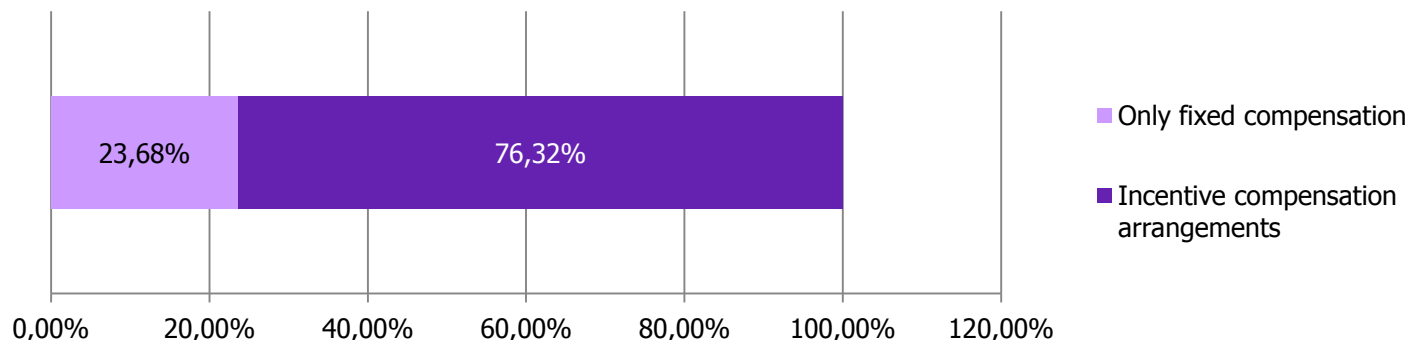
- ✓ Response rate: 18,44% (22,33% including in-depth interviews)
- ✓ Research time line: single research, December 2010-February 2011

Executive compensation in Croatia (1)

- Ownership structure of sampled firms:

Ownership indicator	Mean
Ownership amount of top block holder	55,23%
Ownership concentration (5 major owners)	79,93%
Ownership concentration (10 top owners)	85,75%
State owned	10,80%
Owned by institutional investors	14,52%
Owned by foreigners	12,10%

The use of variable compensation among sampled firms:



Executive compensation in Croatia (2)

Figure 1: Relative amounts of fixed and variable compensation

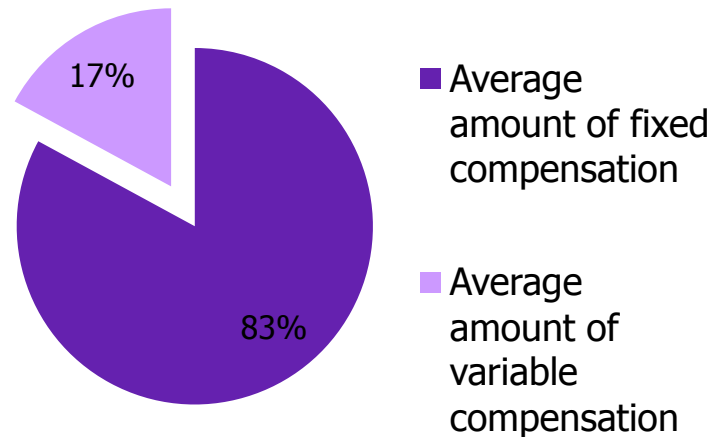
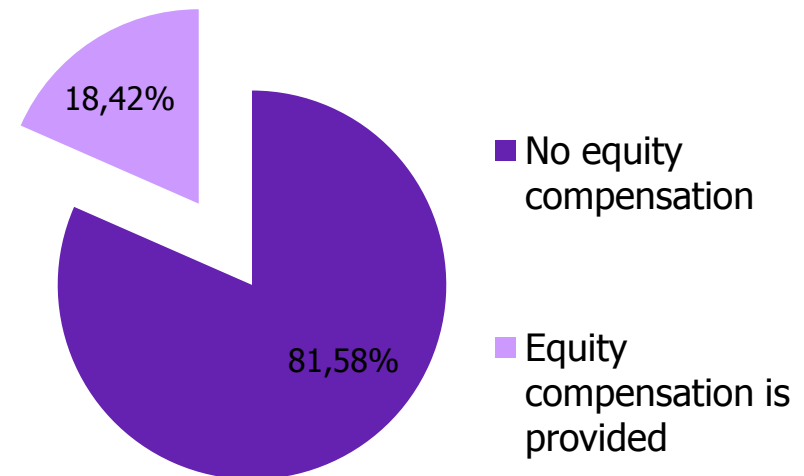


Figure 2: The use of equity based compensation



Executive compensation in Croatia (3)

Table 2: Descriptive statistics of executive compensation in Croatian firms

	% of total compensation in 2009			
	Fixed compensation (base pay)	Variable compensation	Cash bonus	Equity based compensation
Average	82,92	17,08	13,34	3,47
Median	80,00	20,00	12,50	,00
Std. dev.	14,026	14,026	12,600	10,547
Variance	196,723	196,723	158,772	111,229
Minimum	43	0	0	0
Maximum	100	57	50	57

Executive compensation in Croatia (4)

Table 3: Correlation coefficients among relative amounts of compensation components and performance indicators

% of total compensation in 2009			EPS	ROA	ROE	ROS	Net profit
Spearman's rho	Fixed compensation (base pay)	Corr. coef.	-,289*	-,253	-,316*	-,295*	-,399**
		Sig. (2-tailed)	,078	,126	,053	,073	,013
	Variable compensation	Corr. coef.	,289*	,253	,316*	,295*	,399**
		Sig. (2-tailed)	,078	,126	,053	,073	,013
	Cash bonus	Corr. coef.	,034	,073	,067	,154	,227
		Sig. (2-tailed)	,839	,663	,688	,356	,171
	Equity based compensation	Corr. coef.	,167	,116	,136	,142	,116
		Sig. (2-tailed)	,317	,490	,417	,396	,490

* $p < 0,1$, ** $p < 0,05$, *** $p < 0,01$

Executive compensation in Croatia (5)

Table 4: The ratio of executive pay to average firm pay

Pay ratio	Percent (%)	Cumulative Percent (%)
2:1	18,4	18,4
4:1	31,6	50,0
6:1	21,1	71,1
8:1	18,4	89,5
10 or more :1	10,5	100,0
Total	100,0	

Discussion

- How to explore and research executive compensation in transition economies?
- Is there any path of convergence among executive compensation in transition economies?
- Can we apply existing knowledge on executive compensation to transition economies and countries with continental system of governance?
- What role(s) does executive compensation take in transition economies?
- What to do about executive compensation in state-owned firms?

Conclusions

- Executive compensation is accepted mechanism of corporate governance but how about executive compensation within continental system of corporate governance
- The role of executive compensation in Croatia is defined by firm ownership structure
- Executive compensation versus internal monitoring?
- The importance of executive compensation for firm performance

Thank you for your attention

Q&A