Is there anything wrong with Executive Pay?

Francois Wilbers explores the growing unrest resulting from the disparity in executive pay and other workers

“In business leaders must take responsibility for ensuring that ethical considerations are factored into remuneration strategies”

In the last six months South Africa has witnessed an unprecedented number of wild cat strikes by workers for higher wages. These strikes inevitably lead to confrontation with the South African Police Force and as a result workers were killed. At the heart of this lays a struggle by workers who are trying to survive on their current wages which can be as low as R70 per day.

Forget for a moment whether the farmers at De Doorns complied with the minimum wage determined by the Minister of Labour. The question is who can survive under the current economic circumstances on R70 per day? This doesn’t even take into account the 25 per cent unemployed who
survive on far less than this.

One worker at the recent De Doorns strike commented that the farmer should not plead poverty and suggest he is unable to pay his workers a living wage while at the same time purchasing a new vehicle and visiting his beach house every weekend.

The core of the issue is that the income differential between workers and bosses is simply too large. Compensation for senior executives, especially CEOs, has climbed to levels, that for many, is seen as excessive. The perception is that the rich get richer, the numbers living in poverty is on the increase, the upper middle class is having trouble staying even, while the lower middle classes and working classes are losing ground.

The common motivation for the relatively high executive pay is that supply and demand determine the market price to attract and retain top talent. Some business leaders claim that you cannot pay a good executive too much. Successful CEOs are very influential. This influence comes at a price and organisations are willing to offer generous salary packages because of the investor confidence these CEOs bring with them. Unfortunately paying inflated pay packages does not come with a guarantee that a reputable CEO’s strategies will be successful.
EXECUTIVE PAY

Considering the body of research available and public opinion here are some of the interesting findings:

- Results of a review of the descriptive evidence for the operation of boards and two empirical studies suggest that social influence may be responsible for significant increments in CEO compensation beyond what economic theories predict. Generous pay awards, bearing only a weak connection to corporate performance, are explained in the context of the social psychology of the boardroom.

- The high income differential between executives and lower level workers at the same company lead to a sense of unfairness which negatively impacts morale and loyalty.

- Executive incentives have over-emphasised short-term performance, encouraged excessive risk-taking, and failed to penalise poor performance.

- In a survey conducted by Adcorp it was found that chief executives remuneration is not justified by several appropriate metrics, including but most importantly, profitability.

- Strikes in the petroleum and coal sectors, indicated that the excessive increases awarded to executive directors and heads of the relevant companies caused a serious breach of trust between employees and management.

- Some executives do earn obscene amounts of money by any standard and the yawning chasm between the pay of company directors and the lowest paid workers is too wide for comfort in a society where so many are unemployed and struggling to survive.

- After reviewing empirical research, the International Labour Organisation concluded that there is little or no evidence of a relationship between executive pay and company performance.

- The ethics of the growing differentials are rarely addressed in the literature on compensation. It is suggested that the lack of ethical scrutiny affects staff morale and performance by non-managerial employees adversely.

- There would appear to be no evidence to suggest that the growing gap between the pay of top executives and that of the average employee generates long-term enterprise value.

- A combination of shareholder impotence, director self-interest and CEO domination has rendered many board directors favorably disposed—if not beholden—to overpay their corporation's CEO at the expense of the stakeholders.

- Wealth and inequality awaken justice concerns. There are substantial gaps between what people think is fair and what they see around them. This in turn ignites feelings of injustice, setting in motion a train of negative consequences for individuals and society.

- Executive compensation and incentives systems have been shown to be dysfunctional, misaligned and short-sighted. Greed and narrow self-interest have thrived, and risk and stewardship have been too often ignored.

Considering the above the author shares the concern of the remuneration guru Drucker that the current extreme level of income inequality is not sustainable. If the moral and ethical implications of the inequality in remuneration between executive pay and average workers is ignored it has the potential for more serious civil unrest than what was experienced at Marikana and De Doorns.

Business leaders must take responsibility for ensuring that ethical considerations are factored into remuneration strategies for the long-term interest of all the stakeholders of the business and not only the short-term interest of executives and shareholders.