Executive Pay and Performance

in the UK 1994-2002

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Abstract
This paper examines the relationship between executive compensation and company performance for a sample of large UK companies over the period 1994-2002. The relationship is examined against a background of a series of reports into corporate governance mechanisms in UK companies. We provide evidence on the movement in the pay-performance sensitivity over time, and we identify an asymmetric relationship between pay and performance up to 2000. In years in which stock returns are high, pay-performance elasticities are high, but we find that executive pay is insensitive to performance in those periods when stock returns are low. This suggests that over time there is little relationship between pay and performance. We also explore the heterogeneity of the pay-performance relationship across firms, and find that board structure, firm size, industry and firm risk all have an effect on executive compensation.

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