Executive Pay-Performance Relationship Among Listed Deposit Money Banks in Nigeria

Abdulkadir Rihanat Idowu[1]

ABSTRACT

This paper examines the executive pay-performance relationship among listed deposit money banks in Nigeria. It also investigates other possible determinants of executive pay, as well as factors that moderate the pay-performance relationship. Results from the dynamic panel GMM regression indicate that excessive pay does not match performance, as pay rises with declining performance. Other factors that explain the executive pay of the sampled banks include board size, board independence and CEO ownership. Findings further reveal that the pay-performance relationship is negatively moderated by board independence, as executive pay is found to rise with increase in performance when there are more independent directors on the board. The study findings provide support for the managerial power hypothesis. However, no evidence is found in support of the agency theory.

Key words: *Executive Compensation, Dynamic Panel, Performance, Return on Assets, Stock Returns, Managerial Power*

INTRODUCTION

Executive compensation has received considerable attention in the literature due to its important role in motivating highly skilled and professional managers for the overall attainment of firm objectives. Compensation systems should therefore be designed in a way that focuses on long-term sustainability of firms as opposed to short-term results. The process of designing or setting compensation packages varies from country to country.

The importance of understanding how the compensation packages of executives are set cannot be overemphasized. This is because firm executives are very powerful and can either add value to the firm or destroy it through their actions (Joe-Ueng, Wells, & Lilly, 2000). Their actions can destroy the firm when they act contrary to the best interest of shareholders. It is widely held that executives have an insatiable demand for large compensation packages, which may not align with the interest of shareholders. However, the conflicting interests of executives and owners can be aligned when the performances of the executives are duly recognized and they are compensated accordingly. Adequate compensation will thus make them act in line with the interest of the shareholders, and this will further enhance the firm's performance (Boyd, 1994; Erick, Kefah, & Nyaoga, 2014). The board of directors is responsible for aligning these conflicting interests as they set the compensation policies. Sometimes, firm executives also form part of the board that sets these policies. Policies on compensation can affect the firm positively by generating more returns for the firm. They can also affect the firm negatively when huge compensation is paid despite weak

[1]Abdulkadir Rihanat Idowu -Lecturer at the Department of Finance, Faculty of Management Sciences, University of Ilorin, Kwara State, Nigeria.
E-mail of corresponding author: abdulkadir.ri@unilorin.edu.ng (+234-803-435-514-4)
Business Management Review: Volume 24, Number 2, Pages 1-15, ISSN 0856-2253 (eISSN 2546-213X)

performances. Consequently, efficient corporate governance mechanisms must be put in place when setting compensation policies.

This study is premised on certain motivating factors. First, it is widely held that the process of setting compensation packages for firm executives is unclear and not transparent. The board of directors decides the pay of executives without the involvement of shareholders. Considerable discretion is involved in some elements of executive compensation, but the boards do not disclose how they exercise such discretion (Ferri & Maber, 2013). As earlier mentioned, sometimes executives form part of the board that sets the compensation policies, and what this suggests is the absence of an independent board. Boards also sometimes assign this task of setting compensation policies to the remuneration committee which is usually composed of non-executive directors. However, the reciprocal relationship shared with executive directors may deter the committee from playing their role independently (Main, O'Reilly & Wade, 1995). Such relationship emanates from weak corporate governance mechanisms, which worsen agency problems and lead to the excessive compensation of executives.

Second, corporate failures experienced by high-profile companies in recent times and as an aftermath of the global economic crisis have revealed the excessive compensation received by firm executives. Anecdotal evidence suggests that bank executives in Nigeria have been receiving excess compensation packages. Even amidst economic downturn, they continue to receive huge compensation packages.

Table 1. Top Highest Paid Nigerian Banking Executives for 2020

Bank	Amount (Naira value)
UBA	143,000,000
Stanbic-IBTC	158,000,000
Union Bank	164,000,000
Zenith Bank	230,000,000
Guaranty Trust Bank	399,700,000

Source: Business Insider Africa 2020

The most worrisome part of the 'excessive compensation' is that the pay rise does not match the expected increase in performance (Gregg, Jewell & Tonks, 2005). Proshare (2020) reports that only about half of top CEO pay in Nigeria can be explained by performance, as a correlation of 0.49 was found between the earnings of the executives and their performances. Proshare (2020) further reports that the CEO pay of one of the top companies listed on the Nigerian Stock Exchange continued to grow despite the losses recorded by the company for three consecutive years. The non-alignment of huge pay with company performance leads to 'fat cat', described by Lin, Kuo, and Wang (2013) as firms that grossly underperform while their executives get fat compensation packages. In addition, it is widely held that excessive compensation can lead to excessive risk taking which can ultimately trigger financial crises (DeYoung, Peng & Yan, 2013; Lin et al., 2013; Rajan, 2008; Suntheim, 2011).

This study thus examines the pay-performance relationship by ascertaining whether performance determines executive pay among deposit money banks in Nigeria. Other possible determinants including corporate governance variables, and other firm characteristics of executive pay are also examined. The study further examines the moderating role of external monitoring and board independence on the pay-performance relationship of listed deposit money banks in Nigeria.

Nigeria is considered ideal for this study, as Tomar and Korla (2011) note that emerging countries are usually characterized by weak corporate governance structures. Despite the considerable number of studies on the determinants of executive compensation, limited research on this has been conducted in the emerging markets (Raithatha & Komera, 2016). This dearth of knowledge on what determines executive pay packages is even more prominent in the Nigerian context. Results from other regions may not be applicable to Nigeria due to regional differences in regulation. More so, Cadman, Klasa, and Matsunaga (2010) note that differences in the environment in which firms operate can influence the determination of compensation packages. Most related studies are conducted in developed markets. However, this current study is conducted in an emerging market setting with different regulatory requirements, different corporate governance structures and different population characteristics.

Second, while most related studies exclude financial firms due to their peculiar regulatory requirements; this study focuses on banks as they are most affected in terms of huge compensation packages for executives in Nigeria. Third, a considerable number of studies have examined how performance influences executive pay. However, these studies do not pay attention to the fact that other factors may influence the pay-performance relationship. This study therefore examines the moderating role of external monitoring and board independence in explaining the pay-performance relationship.

Findings of the study indicate that executive pay is not matched with performance as executive pay rises with declining performance. Consistent with extant literature, the empirical results suggest that managerial power hypothesis strongly explains the executive pay of deposit money banks in Nigeria. These findings do not provide support for the agency theory.

LITERATURE REVIEW

Theoretical Considerations

The agency theory advanced by Jensen and Meckling (1976) and Fama and Jensen (1983) has been used over time to explain the determinants of executive compensation. The theory explores the nature and causes of conflicts between owners and managers of firms. The separation of ownership and control may cause managers to act in ways that deviate from 'the best interest of shareholders.' The agency theory thus provides for the alignment of conflicting interests of owners (principals) and managers (agents) in order to minimize agency problems. According to proponents of this theory, setting a reward policy that will attach compensation to performance is one of the ways of minimizing agency conflicts as it helps to align the interests of owners and managers. In line with the theory, this study postulates that executive pay will rise as performance rises.

Unlike the agency theory, the managerial power theory argues that excessive compensation of executives emanates from the power they have which leads to rent extraction. According to the theory, managers possess the power to influence remuneration policies set by the board to their advantage. Thus, they use their power to extract rent in the form of excessive pay. This managerial power becomes prominent where corporate governance mechanisms are weak or not in place. In such situations, the executive remuneration will not be economically justified but rather driven by power. Having an independent board can go a long way in mitigating the effect of 'managerial power.' In line with the theory, this study postulates that performance will not significantly influence compensation if managerial power exists. On the other hand, the study hypothesizes that a negative relationship exists between board independence and executive compensation, as independent boards inhibit the exertion of managerial power. Also in line with this theory, it is

postulated that CEO ownership will lead to a higher compensation as a powerful CEO would influence pay to their advantage.

Empirical Review

Performance as a determinant of executive compensation

A considerable number of studies (such as Bouteska & Mefteh-Wali, 2021; Buigut, Soi, & Koskei, 2015; Fabian, Cristina & Ruben, 2020; Ghosh, 2006; Malik & Shim, 2019; Nulla, 2015; Rahman, 2018) report a positive relationship between performance and executive pay. These studies employ accounting performance measures such as ROA and EPS. However, Malik and Shim (2019) document that the relationship between accounting income and compensation cease to be significant post-crisis. Contrarily, Olaniyi and Obembe (2017) find that bank performance negatively influences executive pay. Using market-based measures of performance (such as stock returns; Tobin's Q), other studies (Bouteska & Mefteh-Wali, 2021; Gregg et al., 2005; Malik & Shim, 2019; Rahman, 2018; Scholtz & Smit, 2012) report a positive relationship between stock performance and executive compensation. Although Malik and Shim (2019) reveal that this finding holds in the pre- and post-crisis periods, the relationship is found to be stronger in the post-crisis period. Gregg et al. (2005) also document that executive pay is more sensitive to performance when stock returns are high. Unlike the aforementioned studies, Erick et al. (2014), Lin et al. (2013), and Shah, Javed, and Abbas (2009) do not find evidence of a significant relationship between accounting-based measures of performance and compensation. Similarly, Kim and Gu (2005) and Raithatha and Komera (2016) do not find evidence of a significant relationship between market-based measures of performance and compensation. As earlier noted, this study predicts that executive pay will rise with higher performance, in line with the agency theory.

Other determinants of executive compensation

Another prominent determinant of executive pay is firm size. Firm size has been found to have a positive and significant relationship with executive compensation (Chalmers, Koh, & Stapledon, 2006; Fabian et al., 2020; Jouber & Fakhfakh, 2011; Kim & Gu, 2005; Lin et al., 2013; Malao & Bussin, 2016; Olaniyi & Obembe, 2017; Rahman, 2018; Shah et al., 2009; Tosi et al., 2000; Zhou, 2000). Most of these studies opine that a huge amount of sales and profit induces firms to pay a higher compensation to executives. According to Lin et al. (2013), executives of larger firms should be rewarded for the greater complexities they encounter compared to smaller firms. Tosi et al. (2000) opine that executives may put in more effort to increase the size of the firm in order to maximize their compensation. From another perspective, Chalmers et al. (2006) submit that large firms employ executives with better qualifications and skills, and they are compensated accordingly. It is thus expected that executive compensation will be higher with a larger firm size.

Existing literature shows that board size is also significant in explaining compensation policies. Fung, Firth, and Rui (2001) find that firms with larger board sizes tend to limit executive remuneration. Guest (2008) notes that large board increases monitoring capability. Contrarily, other studies (such as Gregg et al., 2005; Ozken, 2007; Shah et al., 2009; Tomar & Korla, 2011) report that board size positively influences executive compensation. These studies have diverse arguments to support the positive relationship. According to Lin et al. (2013) and Tomar and Korla (2011), large boards usually have problems with coordination, communication and decision making. These problems weaken the effectiveness of the boards and lead to a higher compensation of firm executives. Similarly, Ozken (2007) opines that firms with larger board sizes are not as effective in monitoring as their counterparts, as they are more vulnerable to pressure from the

executives. Based on the argument that a large board increases monitoring capability, this study postulates a decline in executive pay with higher board sizes.

CEO ownership has also been found to have a positive influence on compensation (Buigut et al., 2015; Jouber & Fakhfakh, 2011; Lin et al., 2013). It is argued that powerful CEOs can influence the pay process to their own advantage. Contrarily, Cordeiro and Veliyath (2003) note that CEOs with larger shareholdings have better motivation to boost the firm's value. Thus, the CEOs will regard their shareholdings as substitute for CEO compensation. A negative relationship is therefore reported between CEO shareholdings and compensation. In line with the managerial power theory, it is postulated that CEO ownership will lead to a higher compensation, as powerful CEOs will influence pay to their advantage.

Studies have also reported the effect of independent directors on executive compensation. These studies (Parthasarathy, Menon & Bhattacharya, 2006; Rahman, 2018) argue that the effectiveness of a board is largely determined by the number of non-executive directors on the board. Rahman (2018) reports a positive relationship between the percentage of independent directors on the board and executive compensation. The author argues that the independent directors lack effectiveness in discharging their monitoring role, and this suggests weak corporate governance mechanisms. Contrarily, other studies (Buigut et al., 2015; Gregg et al., 2005; Parthasarathy et al., 2006; Shah et al., 2009; Tomar & Korla, 2011) find that the percentage of independent directors negatively influences executive compensation. These studies base their findings on the fact that non-executive directors are independent and more effective in serving the interest of shareholders. Thus, a higher proportion of independent directors enhances firm monitoring and limits managerial power to act contrary to the interest of shareholders (Gregg et al., 2005; Parthasarathy et al., 2006). As earlier noted, this study postulates a negative relationship between the percentage of independent directors and executive compensation.

Few studies (Palepu & Healy, 2007; Penman, 2007; Rahman, 2018) report a negative relationship between leverage and executive pay. On the other hand, Malik and Shim (2019) report that leverage is positively related to total compensation. This is premised on the fact that debt holders exert monitoring influence on the firm. Through this monitoring, they ensure that the actions of the management align with their debt holders' interests. Kim and Gu (2005) document an insignificant relationship between leverage and executive compensation. This study postulates that executive pay is lower when leverage is higher, due to increased external monitoring.

Previous pay of executives likewise exerts a significant positive influence on current pay (Olaniyi & Obembe, 2017; Raithatha & Komera, 2016). Raithatha and Komera (2006) refer to this as persistence in executive compensation, and document that this persistence exists irrespective of the size of the firm. In line with this, this study predicts a positive relationship between the previous pay and the current pay of executives. Other determinants that have been reported include: dual leadership, institutional shareholders, CEO tenure, crisis and sales growth. Tomar and Korla (2011) find dual leadership (where the CEO also chairs the board) to be positively related to executive compensation. The CEO will be more powerful in influencing decisions where he also chairs the board, leading to a higher CEO pay. Thus, agency problems tend to be higher with dual leadership, and this can be mitigated where the roles of board chair and CEO are separated.

Institutional shareholders have also been found to be significant in explaining executive compensation. Ozken (2007) and Rahman (2018) find a negative relationship between institutional

shareholders and executive pay. The authors argue that through their large shareholdings, institutional shareholders can influence the decision making of the management and compensation policies. Thus, a higher proportion of institutional shareholders will restrain the executives from awarding themselves excessive compensation. Contrarily, Ullah et al. (2020) find a positive and significant relationship between institutional ownership and CEO compensation.

Gomez-Mejia, Larraza-Kintana, and Makri (2003) find that the presence of family ties influences the size and composition of executive pay package. The authors observe that though family executives earn less relative to their counterparts, they are compensated for assuming higher uncontrollable risks. Such risks are due to the fewer employment options available to family executives in the labour market. Crisis is also important in understanding the determinants of executive compensation. Malik and Shim (2019) document that the composition of executive compensation and its economic determinants differ significantly between the pre- and post-financial crisis periods. Their results reveal a significant reduction in the mean value of total compensation during the crisis. CEO tenure has also been reported to positively influence their pay (Jouber & Fakhfakh, 2011; Olaniyi & Obembe, 2017). Jouber and Fakhfakh (2011) specifically report that an increase in CEO tenure by one year increases executive compensation by 14%. Jaiswall and Raman (2019) also find that sales growth positively influences CEO pay arrangements.

Gap in existing literature

As earlier mentioned, there is a dearth of knowledge on the determinants of executive pay in Nigeria, and results from other regions may not be applicable to Nigeria due to regional differences in regulation. In addition, most of the existing studies focus on non-financial firms, while financial firms are excluded. This study is therefore centered on the financial firms which have not received much attention in this area. More so, a considerable number of studies have examined how performance influences executive pay. However, these studies have not paid attention to the fact that other factors may influence the pay-performance relationship.

Although Olaniyi and Obembe (2017) also examine factors that determine executive compensation in Nigerian banks, this current study employs a market-based measure of performance in addition to the accounting-based measure employed in the previous study. In addition, the current study introduces moderating variables to check for factors that could possibly influence the pay-performance relationship even though past studies (Fabian et al., 2020; Raithatha & Komera, 2016) find that larger companies strengthen the pay-performance relationship. Also, other studies (Garvey &Milbourn, 2003; Gregg et al., 2005) have shown that riskier firms tend to have a lower pay-performance relationship. This study brings in two new variables that could possibly explain the pay-performance relationship: external monitoring (proxied with leverage) and board independence. The study postulates that with enhanced external monitoring (when leverage is high), executive pay will be matched with performance. That is, in the presence of increased monitoring, executive pay rises when performance rises, and vice-versa. Also, in line with the managerial power hypothesis, this study postulates that with a higher number of independent directors on the board, executive pay will be matched with performance. Thus, when the percentage of independent directors is high, higher performance will lead to higher pay.

DATA AND METHOD

The study centers on the 14 deposit money banks quoted on the Nigerian Stock Exchange over the period 2009-2019. Two of the banks are however excluded from the analysis due to non-availability of data related to executive compensation. The sample period is chosen to cover years of consistent rise in compensation packages as suggested by anecdotal evidence. Data is obtained from the annual reports and accounts of the deposit money banks obtained from the website of the Central Bank of Nigeria. Annual data is employed for all variables. The general specifications for the functional relationship examined in this study are as given below:

$$ECOMP = f\ (ROA;\ FSIZE;\ LEV;\ BSIZE;\ BIND;\ CEOWN;\ ECOMP\_1;\ LEV*ROA;\ BIND*ROA) \quad (1)$$

$$ECOMP = f\ (SRET;\ FSIZE;\ LEV;\ BSIZE;\ BIND;\ CEOWN;\ ECOMP\_1;\ LEV*SRET;\ BIND*SRET) \quad (2)$$

Specifically, the models estimated are given in equations (1) and (2). The dependent variable *ECOMP* represents executive compensation. It has two components—cash and non-cash. Previous studies employ the use of cash compensation (Buigut et al., 2015). This study however employs the use of total compensation, which consists of salary, bonus and long-term compensation.

The main explanatory variable *PERF (*which represents performance) is included in the model to test for the pay-performance relationship. Related studies have argued between the use of accounting variables and market-based proxies in measuring performance. Results obtained may also differ based on the performance measure employed. Besides the widely held opinion that accounting performance may be subjected to manipulations using accruals accounting (Jaiswall & Raman, 2019; Tomar & Korla, 2011), market-based measure is very important as it may better align the interests of shareholders and managers. Thus, this study adopts the accounting-based measure of performance (return on assets) in Model 1, and the market-based measure (stock returns scaled by market value) is adopted in Model 2. Leverage (*LEV*) is included in the model to examine how external monitoring affects executive compensation. Leverage is measured as total debts to total assets of the bank (expressed in percentage). Another firm-specific characteristic included in the model is firm size (*FSIZE*) and it is measured as natural logarithm of total assets of the bank.

In order to examine how corporate governance impacts on executive compensation, variables which include board size, board independence and CEO ownership are also included in the model. *BSIZE* represents board size, which is the total number of directors on the board of the bank. *BIND* represents board independence, and it is measured as the percentage of the boards' directors that are not executives of the bank. *CEOWN* represents the percentage of shares held by the CEO.*ECOMP_1* is the lag of executive compensation, and it is included in the model to test for persistence in pay of executives.

In line with the argument that certain factors may influence the pay-performance relationship, the study includes *LEV*ROA and LEV*SRET* in equations 1 and 2 respectively to see whether external monitoring (proxied with leverage) can influence the pay-performance relationship. *LEV*ROA* is the interaction of external monitoring and the accounting-based measure of performance. *LEV*SRET* is the interaction of external monitoring and the stock market-based measure of performance. Similarly, *BIND*ROA and BIND*SRET* are included in equations 1 and 2 respectively to see whether there is any change in the explanatory role of performance with a higher number of independent directors on the board. *BIND*ROA* is the interaction of board

independence and the accounting-based measure of performance. *BIND*SRET* is the interaction of board independence and the stock market-based measure of performance.

The dynamic panel generalized method of moment (GMM) is employed using the two-step estimator. GMM is employed for this study as it is preferred when the lag of the dependent variable is included among the explanatory variables. In addition, the method is well-suited to address any potential endogeneity issue. Specifically, the two-step GMM is preferred due to its use of optimal weighing matrices. As a post-estimation specification test, the validity of the explanatory variables is confirmed using Sargan test of over-identifying restrictions. Similarly, Arellano-Bond test is employed to test for the presence of serial correlation or otherwise. The following dynamic panel models are therefore estimated:

$$y_{it} = \alpha y_{i,t-1} + \beta x_{it} + \eta_i + \varepsilon_{it}; \quad i = 1, \dots \dots N, t = 1, \dots \dots T$$

$$ECOMP_{it} = \beta_0 + \alpha_1 ECOMP_{i,t-1} + \beta_1 ROA_{it} + \beta_2 FSIZE_{it} + \beta_3 LEV_{it} + \beta_4 BSIZE_{it} + \beta_5 BIND_{it} + \beta_6 CEOWN_{it} + \beta_7 LEV * ROA_{it} + \beta_8 BIND * ROA_{it} + \eta_i + \varepsilon_{it} \quad (3)$$

$$ECOMP_{it} = \beta_0 + \alpha_1 ECOMP_{i,t-1} + \beta_1 SRET_{it} + \beta_2 FSIZE_{it} + \beta_3 LEV_{it} + \beta_4 BSIZE_{it} + \beta_5 BIND_{it} + \beta_6 CEOWN_{it} + \beta_7 LEV * SRET_{it} + \beta_8 BIND * SRET_{it} + \eta_i + \varepsilon_{it} \quad (4)$$

Where η_i= unobserved time-invariant heterogeneity and ε_{it} is the idiosyncratic error.

RESULTS AND DISCUSSION

In Table 2, the descriptive statistics of the variables in the regression model are presented. In line with Wooldridge (2002), the variables are scaled down by six zeros to prevent measurement unit error.

Table 2. Descriptive Statistics

Variables	Obs	Mean	Std. Dev.	Min	Max
Executive Compensation	132	8.700	3.410	3.434	13.722
Return on Assets	132	2.613	5.654	-31	26.38
Stock Returns	132	8.336	9.317	0.15	41.5
Firm Size	132	16.901	3.253	11.232	22.566
Leverage	132	63.837	52.182	0	219.05
Board Size	132	14.656	3.355	6	25
Board Independence	132	9.779	2.164	5	15
CEO Ownership	132	1.836	1.875	0	8.89

Note: Executive compensation is scaled down by six zeros to prevent measurement unit error

The dynamic regression results are presented in Table 3. In Model 1, the main explanatory variable (financial performance) is proxied with return on assets (ROA), which is an accounting-based measure. As earlier mentioned, the study employs the market-based measure of performance in Model 2 as it is believed that this measure better aligns the interests of shareholders and managers.

Thus, stock returns is used as a measure of performance in Model 2 as a robustness check to ascertain whether our results from the initial model holds when the variable (performance) is redefined.

Table 3. System Dynamic Panel Data Estimation Results

DV= Executive Compensation	Model 1 *Performance= ROA*	Model 2 *Performance = Stock Returns*
Constant	14.66 (0.34)	1.122 (0.54)
Return on Asset	-2.672* (-0.25)	-
Stock Returns	-	-0.254*** (-2.57)
Firm Size	0.085 (0.07)	0.605* (1.67)
Leverage	0.003* (0.05)	0.003 (0.67)
Board Size	-1.130* (-0.55)	-0.290** (-0.44)
Board Independence	-0.147*** (-0.25)	-0.845** (-2.21)
CEO ownership	0.240*** (0.52)	-0.094 (-0.71)
Executive compensation (previous year)	0.166 (0.67)	0.139 (0.51)
Leverage*ROA	-0.006** (-0.22)	-
Board Independence*ROA	0.295*** (0.25)	-
Leverage*SRET	-	0.0003 (0.60)
Board Independence*SRET	-	0.035*** (2.67)
Model Diagnostics		
AR(1)	0.014 {0.07}	-1.745 (0.08)
AR(2)	-0.328 (0.641)	0.032 (0.974)

Sargan Chi x^2	2.439 {0.125}	2.657 (0.116)
Wald x^2	45.51 (0.000)	239.84 (0.000)
No of Obs	132	132

Note: The two models are estimated using two-step dynamic panel GMM estimations with robust standard errors. z-scores are in parentheses except for Sargan's test and AR test for serial correlation, where p-values are in parentheses. ***, ** and * indicate significance levels at 1%, 5% and 10% respectively.

Pay-Performance Relationship and Other Determinants of Executive Pay

The results in Table 3 show that there is a negative relationship between executive pay and performance in both models. This finding is consistent with the 'fat cow' argument which suggests that while firms underperform, their executives still get huge compensation packages. The negative relationship is stronger in Model 2. Thus, firms with lower market performance get even more pay. The findings corroborate that of Olaniyi and Obembe (2017) although their study only considers the accounting-based performance measure. However, the findings of this study contradict the positive relationship observed in earlier studies (Bouteska & Mefteh-Wali, 2021; Buigut et al., 2015; Fabian et al., 2020; Ghosh, 2006; Malik & Shim, 2019). The observation that pay does not match performance counters the agency theory, which suggests that pay should align with performance.

Firm size has little positive influence on executive pay as shown in Table 3. It is insignificant in Model 1 and only significant at 10% in Model 2. This finding conflicts with the results of earlier studies (Chalmers et al., 2006; Jouber & Fakhfakh, 2011; Kim & Gu, 2005; Lin et al., 2013). The conflict in results is likely to be as a result of differences in the definitions of firm size. The components of assets used in defining firm size in the case of the banks sampled in this study greatly differ from non-banks which most of the other studies focus on.

Contrary to expectation, findings show that with high leverage, executive compensation rises. However, the influence is very weak as it is significant at 10% in Model 1 and insignificant in Model 2. This supports the finding of Malik and Shim (2019) but opposes those of Palepu and Healy (2007), Penman (2007), and Rahman (2018) who report a negative relationship. The positive relationship observed suggests that debtholders are weak and cannot exert monitoring influence on the banks; thus, they are not effective monitors.

Consistent with the notion that large boards increase monitoring capability, the results in Table 3 show that the higher the board size, the lower the executive pay. This finding is stronger in Model 2, and matches those of Fung et al. (2001) and Guest (2008). It however contradicts the negative results obtained in some other studies (Gregg et al., 2005; Ozken, 2007; Shah et al., 2009).

Similarly, findings show that with a higher number of independent directors on the board, executives get lower pay. Thus, the independent directors are able to exert monitoring influence, thereby limiting the exploitative power of the executives. This matches earlier results obtained by Gregg et al. (2005) and Parthasarathy et al. (2006). The finding also supports the managerial power hypothesis, which suggests that an independent board inhibits the exertion of managerial power.

The results obtained in Model 1 indicate that with a higher percentage of CEO shareholdings, there is an increase in executive pay. This finding is consistent with earlier results by Buigut et al. (2015), Jouber and Fakhfakh (2011), and Lin et al. (2013). It however contradicts the negative relationship reported by Cordeiro and Veliyath (2003). The finding suggests that CEOs with large shareholdings exert pressure to influence pay process to their own advantage. The finding is also in support of the managerial power theory which suggests that powerful CEOs will influence pay to their advantage. Conversely, the results obtained in Model 2 show a negative relationship between CEO shareholdings and executive pay. However, the relationship is insignificant.

The study finds no evidence to support persistence in executive pay. This is so because previous compensation in both models is not significantly related to current compensation. This finding conflicts the persistence in executive pay reported in other studies (Olaniyi & Obembe, 2017; Raithatha & Komera, 2016).

Moderating Role of External Monitoring and Board Independence

Contrary to the expectation that the existence of external monitors will result in higher pay when performance is high, the results in Model 1 show a negative and significant relationship between pay and performance in the presence of external monitoring. Despite the presence of external monitoring, low performance attracts higher pay. Thus, external monitoring (proxied with leverage) exerts a negative influence on the pay-performance sensitivity. This result further strengthens the inference of a lack of effective monitors. Model 2 however shows insignificant results.

Board independence is found to positively influence the pay-performance relationship. This is confirmed in the two models, where the interaction term of board independence and performance is significant at 1% level. Thus, when there is a higher number of independent directors on the board, executive pay rises as performance rises, and vice-versa. This suggests that the independent directors ensure that hard work is compensated and they prevent the prominence of 'fat cows' that earn high pay with low performance. Thus, with a higher number of independent directors on the board, pay is matched with performance. This finding is in line with the results obtained on board independence and shows that independent directors exert monitoring influence and prevent misuse of managerial power. This is also in line with the managerial power theory.

In summary, findings show that the most important determinants of executive compensation include performance, board size and board independence, as these variables are found to be significant in both models. The strength of significance obtained suggests that board independence is stronger than the other variables in explaining executive pay. External monitoring negatively influences the pay-performance sensitivity. However, the relationship is weak and only holds true for the accounting-based measure of performance. Consistent findings in both models reveal that board independence positively influences the pay-performance sensitivity.

A post-estimation specification test is conducted to test for residual serial correlation. The results from Table 3 show that the null of no first order serial correlation (AR 1) is rejected at 10% significance level for the two models, while the null of no second-order serial correlation cannot be rejected for both models. Thus, the models are free of second-order serial correlation. Sargan test is also carried out to test for the validity of over-identifying restrictions. As revealed in the table, the Sargan test shows an insignificant p-value for both models. This implies that the null

hypothesis of 'over-identifying restrictions are valid' is accepted. Thus, the IV estimator is unbiased and consistent for both models. Similarly, the Wald $x^2$is significant at 1% and this further confirms the validity of the models.

CONCLUSION AND RECOMMENDATIONS

This study examines the pay-performance relationship and other determinants of executive pay for listed deposit money banks in Nigeria. The study also examines whether the pay-performance relationship is influenced by external monitoring and board independence. To achieve this, annual data is employed on a sample of 12 banks from year 2009to 2019. Empirical results from the dynamic panel generalized method of moments (GMM) using the two-step estimator suggest that executive pay is not matched with performance as pay increases, even when the banks record a decline in performance. Other determinants of executive pay identified in the study include board size and board independence. Findings further reveal that the pay-performance relationship is negatively affected by external monitoring and positively affected by board independence. However, board independence plays a greater moderating role as the results hold true for both models. The study thus concludes that even though pay is not positively matched with performance, the pay-performance sensitivity is entirely reversed when there is a higher number of an independent director on the board. With more independent directors, executives are compensated for hard work as pay increases with performance. It is further concluded that executive pay is not economically justified but driven by managerial power. Thus, the managerial power hypothesis is very relevant in explaining the executive pay of listed deposit money banks in Nigeria. The findings of the study do not support the agency theory.

These results have a number of implications to stakeholders and policyholders. Boards of directors will be guided on important factors to consider in setting optimal pay structures. Specifically, regulators will be guided on the possible need for additional regulations to guide compensation policies. In addition, other stakeholders—shareholders, management, lenders—will be better-informed about the factors that explain the executive pay of the sampled banks. Regulatory authorities should thus enforce the review of the pay setting process of the sampled banks to match with performance. This will ensure the alignment of the objectives of shareholders and owners. Regulators should also ensure that shareholders are empowered to monitor compensation policies, and more emphasis should be placed on efficient corporate governance mechanisms. This will help to curtail the 'fat cow' problem where firms that do not perform well pay high compensation. Regulations should be directed further at ensuring more board independence. This will prevent managers from extracting rent in form of excessive pay. This will also ensure that pay is aligned with performance. Boards of directors should exercise great caution in setting compensation packages, and board size should be considerably limited. Future research can look into other incentive components such as share options and long-term incentives.

REFERENCES

Bouteska, A., & Mefteh-Wali, S. (2021). The determinants of CEO compensation: new insights from United States. *Journal of Applied Accounting Research, 22* (4), 663-686. https://doi.org/10.1108/jaar-08-2020-0176

Boyd, B.K. (1994). Board control and CEO compensation. *Strategic Management Journal, 15(5),* 335-344. https://doi.org/10.1002/smj.4250150502

Buigut, K.K., Soi, N.C., & Koskei, I.J. (2015). Determinants of compensation: Evidence from UK public limited companies. *International Journal of Business and Management, 10* (1), 223-230. https://doi.org/10.5539/ijbm.v10n1p223

Cadman, B., Klasa, S., & Matsunaga, S. (2010). Determinants of CEO pay: A comparison of ExecuComp and non-ExecuComp firms. *Accounting Review, 85(5),* 1511-1543. https://doi.org/10.2308/accr.2010.85.5.1511

Chalmers, K., Koh, P.S., & Stapledon, G. (2006). The determinants of CEO compensation. Rent extraction or labour demand? *The British Accounting Review, 38,* 259-275. https://doi.org/10.1016/j.bar.2006.01.003

Cordeiro, J.J., & Veliyath, R. (2003). Beyond pay for performance: Determinants of CEO compensation. *American Business Review, 21(1),* 56-66. https://digitalcommons.newhaven.edu/americanbusinessreview/vol2/iss1/2

DeYoung, R., Peng, E., & Yan, M. (2013). Executive compensation and business policy choices at U.S. commercial banks. *Journal of Financial and Quantitative Analysis, 48(1),* 165-196. https://doi.org/10.1017/s0022109012000646

Erick, T.K., Kefah, B.A., & Nyaoga, R.B. (2014). The relationship between executive compensation and financial performance of insurance companies in Kenya. *Research Journal of Finance and Accounting, 5(1),* 113-122.

Fabian, B., Cristina, D.F., & Ruben, P. (2020). Executive remuneration determinants: New evidence from meta-analysis. *Economic Research-EkonomskaIstrazivanja, 33(1),* 2844-2866. https://doi.org/10.1080/13316677X.2019.1678503

Fama, E.F., & Jensen, M.C. (1983). Separation of ownership and control. *Journal of Law and Economics, 26(June),* 301-325. https://dx.doi.org/10.2139/ssrn.94034

Ferri, F., & Maber, D.A. (2013). Say on pay votes and CEO compensation: Evidence from the UK. *Review of Finance, 17(2),* 527-563. https://doi.org/10.1093/rof/rfs003

Fung, P.M.Y. Firth, M., & Rui, O.M. (2001). Corporate governance and CEO compensation in China. SSRN Electronic Journal. https://doi.org/10.2139/ssrn.337841

Garvey, G., & Milbourn, T. (2003). Incentive compensation when executives can hedge the market: Evidence of relative performance evaluation in the cross section. *Journal of Finance, 58(4),* 1557-1581.

Ghosh, A. (2006). Determination of executive compensation in an emerging economy. Evidence from India. *Emerging Markets Finance and Trade, 42(3),* 66-90. https://doi.org/10.2753/REE1540-4966X420304

Gomez-Mejia, L.R., Larraza-Kintana, M., & Makri, M. (2003). The determinants of executive compensation in family-controlled public corporations. *The Academy of Management Journal, 46(2),* 226-237. https://doi.org/10.2307/30040616

Gregg, P., Jewell, S., & Tonks, I. (2005). Executive pay and performance in the UK 1994-2002 CMPO working paper series. No. 05/122. University of Bristol and University of Exeter.

Guest, P.M. (2008). The determinants of board size and composition: evidence from UK. *Journal of Corporate Finance,* 14(1), 51-72. https://doi.org/10.1016/j.jcorpfin.2008.01.002

Jaiswall, S.S. & Raman, K.K. (2019). Sales growth, CEO pay and corporate governance in India. *Journal of Accounting, Auditing & Finance, 36(2),* 249-277. https://doi.org/10.1177/0148558X19825672

Jensen, M., & Meckling, W. (1976). Theory of the firm: managerial behavior, agency costs, and ownership structure. *Journal of Financial Economics, 3,* 305-360. https://doi.org/10.1016/0304-405X(76)90026-X

Joe-Ueng, C., Wells, D.W., & Lilly, J.D. (2000). CEO influence and executive compensation: Large firms vs. small firms. *Managerial Finance,* 26(8), 3-12. https://doi.org/10.1108/03074350010766800

Jouber, H., & Fakhfakh, H. (2011). The institutional determinants of CEO compensation: An international empirical evidence. *International Journal of Business Science and Applied Management, 6(3),* 43-57. https://www.econstor.eu/handle/10419/190628

Kim, H., & Gu, Z. (2005). A preliminary examination of determinants of cash compensation in the U.S restaurant industry from an agency theory perspective. *Journal of Hospitality and Tourism Research, 29,* 341-355. https://doi.org/10.1177/1096348004273428

Lin, D., Kuo, H.C., & Wang, L.H. (2013). Chief executive compensation: an empirical study of fat cat CEOs. *The International Journal of Business and Finance Research, 7(2),* 27-42. https://ssrn.com/abstract=2149110

Main, B.G.M., O' Reilly, C., & Wade, J. (1995). The CEO, the board of directors and executive compensation: *Economic and psychological perspectives*. Industrial and Corporate Change, 4(2), 293-332. https://doi.org/10.1093/icc/4.2.293

Malao, F. & Bussin, M. (2016). Determinants of executive compensation in South African State-Owned enterprises. *South African Journal of Labour Relations, 40(1),* 8-24. https://10.4102/sajhrm.v18i0.1250

Malik, M., & Shim, E.D. (2019). An empirical examination of economic determinants of financial CEO compensation: A comparative study on pre and post financial crisis period. *In Burney, L.L and Malina, M.A. (Ed.) Advances in Management Accounting,* Emerald Publishing Limited, Bingley, 31, 23-53. https://doi.org/1018/51474-78712019000001003

Nulla, Y.M. (2015). Pay for performance: An empirical review. *Corporate Ownership and Control, 12(4),* 69-79. https://doi.org/10.22495/cocv12i4p5

Olaniyi, C.O., & Obembe, O.B. (2017). Determinants of CEO pay: empirical evidence from Nigerian quoted banks. *International Journal of Business Performance Management, 18(3),* 327-349. https://doi.org/10.1504/IJBPM.2017.10004094

Ozken, N. (2007). Do corporate governance mechanisms influence CEO compensation? An empirical investigation of UK companies. *Journal of Multinational Financial Management, 17,* 349-364. https://doi.org/10.1080/1331677X.2020.1867214

Palepu, K. & Healy, P. (2007). *Business analysis and valuation (4thed.).* Thomson, South Western.

Parthasarathy, A., Menon, K., & Bhattacharya, D. (2006). Executive compensation, firm performance, and corporate governance: An empirical analysis (January 2006). https://dx.doi.org/10.2139/ssrn.881730

Penman, S. (2007). *Financial statement analysis and security valuation*. McGraw-Hill: Irwin.

Proshare (2020). CEO remuneration 2020 report-paying the CEO in a pandemic: The unanswered questions. Retrieved from https://www.proshareng.com/news/People/CEO-Remuneration-2019--1----Paying-the-CEO-in-a-Pandemic--The-Unanswered-Questions/5247a

Raithatha, M., & Komera, S. (2016). Executive compensation and firm performance: Evidence from Indian firm. *IIMB Management Review, 28,* 160-169. https://doi.org/10.1016/j.iimb.2016.07.002

Rahman, M.M. (2018). Determinants of CEO compensation: Empirical evidence from listed banks of Bangladesh. *Dhaka University Journal of Business Studies, 1(1),* 127-161.

Rajan, S. (2008). Banker's pay is deeply flawed. Financial Times, 8 January. Retrieved from https://wwwft.com/content/18895dea-be06-11dc-8bc9-0000779fd2ac

Scholtz, H.E., & Smit A. (2012). Executive remuneration and company performance for South African companies listed in the Alternative Exchange (AltX). *Southern African Business Review, 16(1),* 22-38.

Shah, S.Z.A., Javed, T., & Abbas, M. (2009). Determinants of CEO compensation: Empirical evidence from Pakistani listed companies. *International Research Journal of Finance and Econometrics, 32*, 148-159.

Suntheim, F. (2011). Managerial compensation in the financial service industry. Working Paper, SSRN Electronic Journal. https://doi.org/10.2139/ssrn.1592163

Tomar, A., & Korla, S. (2011). Global recession and determinants of CEO compensation: An empirical investigation of listed Indian firms, Advances in Management, 4(12), 11-26.

Tosi, H.L., Werner, S. Katz, J.P., & Gomez-Mejia, L.R. (2000). How much does performance matter? A meta-analysis of CEO pay studies. *Journal of Management, 26(2*), 301-339. https://doi.org/10.1177/014920630002600207

Ullah, F., Jiang, P., Shabab, Y., Li, H.X., & Xu, L. (2020). Block ownership and CEO compensation: does board diversity matter? *Applied Economics, 52(6),* 583-597. https://doi.org/10.1080/00036846.2019.1659490

Wooldridge, J.M. (2002). Econometric analysis of cross-section and panel data. The MIT Press, Cambridge.

Zhou, X. (2000). CEO pay, firm size, and corporate performance: evidence from Canada. *Canadian Journal of Economics,* 33(1), 213-251. https://doi.org/10.1111/0008-4085.00013.