TOP PAY IN THE UK: New evidence that CEO remuneration is linked to firm performance

There is a clear link between corporate success and senior executives’ pay, according to new research from the Centre for Economic Performance, LSE, which analyses data on firms making up 90% of the value of the UK stock market. But while there is also evidence of an impact of corporate failure on CEOs’ remuneration and the likelihood they will keep their jobs, the link between pay and performance is weaker.

The new investigation will be presented at a public event – ‘Top Pay in the UK’ – taking place in London today, Friday 4 November, as part of the Festival of Social Science run by the Economic and Social Research Council.

Recent figures indicate a resurgence in the growth of CEO pay in the UK at a time of austerity for most. Anger at these numbers is driven in part by a growing belief that such pay bears little relationship to how the companies that these CEOs manage actually perform. In other words, the argument goes, there is pay for no performance.

Dr Brian Bell and Professor John Van Reenen have created a new database of pay for CEOs, senior executives and workers covering over 400 firms since 2001. These firms account for just under 90% of UK stock market capitalization.

This is the first time that data covering everyone from the CEO to a cleaner in a large sample of firms have been collected in this country. It allows for a rigorous exploration of how pay across a company changes as the performance of the company varies. The research finds that:

- There are big differences in average pay. CEOs earn around 40 times more than the average worker – but this multiple rises to around 80 looking only at the very top companies – the FTSE 100.
- The majority of pay for CEOs comes from bonuses and stock incentive plans, whereas 95% of workers’ pay comes from basic salary.
- When firm performance improves, so does pay, but it goes up much more for CEOs than for ordinary workers. If the firm’s value increases by 10%, CEOs on average get an extra 3% in pay, while workers get only 0.2% more.
- This close pay-for-performance link among CEOs is a recent development. Evidence from the 1980s and early 1990s found almost no link between pay and performance for executives. The link is driven by bonuses and incentive packages, which have become more important in recent years.

John Van Reenen says:

‘Our evidence shows a strong link between CEO pay and company performance. It’s not just upside because when the firm does badly, CEO pay also goes down.

‘Poor performing firms are also much more likely to boot out their CEOs. But CEO pay cuts for failure are not as speedy as pay increases on the upside.’

Brian Bell adds:

‘The problem is that these average effects of performance on pay cover both well-governed firms that use pay to incentivize their CEO and poorly performing firms that overpay for questionable talent.

‘In addition, it is hard to claim that the majority of the pay gains for most CEOs over the last decade can be linked to performance given the relatively poor returns to shareholders over the period’.

The authors suggest that the onus must be on each and every Board to explain to shareholders and the public how the pay growth of their CEO is tightly linked to the performance of the company. Those that fail this test must be held to account by shareholders.

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Notes for Editors:

1. **Top Pay in the UK**
   
   - **Organiser:** Dr Brian Bell, Centre for Economic Performance, LSE
   - **Date:** 4th November 2011, 14.00-15.30
   - **Venue:** Centre for Economic Performance, London School of Economics
   - **Audience:** General
   
   For more information: [http://cep.lse.ac.uk/new/events/event.asp?id=144](http://cep.lse.ac.uk/new/events/event.asp?id=144)

2. This release refers to the findings from ‘Firm Performance and Wages: Evidence from across the Corporate Hierarchy’ funded by the Economic and Social Research Council and conducted by Dr Brian Bell and Professor John Van Reenen at the Centre for Economic Performance, LSE. (See Centre for Economic Performance Discussion Paper No.1088, [http://cep.lse.ac.uk/pubs/download/dp1088.pdf](http://cep.lse.ac.uk/pubs/download/dp1088.pdf)).

3. The Festival of Social Science is run by the Economic and Social Research Council which runs from 29 October to 5 November 2011. With events from some of the country's leading social scientists, the Festival celebrates the very best of British social science research and how it influences our social, economic and political lives - both now and in the future. This year's Festival of Social Science has over 130 creative and exciting events aimed at encouraging businesses, charities, government agencies; and schools or college students to discuss, discover and debate topical social science issues. Press releases detailing some of the varied events are available at the Festival website. You can now follow updates from the Festival on twitter using #esrcfestival

4. The Economic and Social Research Council (ESRC) is the UK's largest organisation for funding research on economic and social issues. It supports independent, high quality research which has an impact on business, the public sector and the third sector. The ESRC’s total budget for 2011/12 is £203 million. At any one time the ESRC supports over 4,000 researchers and postgraduate students in academic institutions and independent research institutes. More at [www.esrc.ac.uk](http://www.esrc.ac.uk)