

EFFECT OF EXECUTIVE COMPENSATION ON FIRMS PERFORMANCE: EVIDENCE FROM NIGERIAN BANKING SECTOR

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Abstract

This study examines the effect of executive compensation on the operating performance of banks in Nigeria, adapting agency theory that relates pay to performance. It explores the measure of CAMEL incorporating banks assets, equity, loans, Interest rate spread and executive compensation in a model estimated in a balanced panel, employing the Generalised Least Squares and Fixed Effect Econometric methods. Samples used are based on annual data series of fourteen commercial banks in Nigeria for the period 2004-2015, derived from Central Bank of Nigeria statistical bulletin and Nigerian Deposit and Insurance Corporation, various issues. The results show that executive compensation and total assets significantly positively relate to banks performance in Nigeria. The study thus proposes formulation of relative policy option for good incentive package for executive officers of banks, germane to enhance banks performance in Nigeria.

Keywords: Agency theory, Banks, Executive compensation, Performance.

Introduction

Executives who are improperly compensated may not have the incentive to perform in the best interest of shareholders, which can be costly to the shareholders. Several empirical studies carried out in the fields of Economics and Managerial sciences on the effects of compensation of top management on firm performance have resulted in conflicting outcomes. While in some cases, the outcomes indicate a positive relationship between performance and remuneration, in other cases, the result is negative or finds no relationship between these two variables. These varying outcomes ascribe to differences in methods of data collection, statistical techniques used for data analysis, samples and periods under consideration and so on. The level of executive compensation and its relationship to a firm's financial performance are central issue of debate among corporate directors, economists, financial journalists and compensation professionals in recent time. This study seeks to continue and contribute to the existing literature on the issue.

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Executive compensation is how top executives of business firms or corporations are paid. The components of an executive compensation pay package include amongst others, base pay or basic salary, bonuses, shares, options, executive perquisites and other benefits such as long-term incentive and capital appreciation plans (Milkovich & Newman, 2002; Miller, Vandome & McBrewster, 2009). Globally, the issue of executive compensation is been given so much attention and concern following the financial crisis that erupted in 2008 in the United States of America. Experts and critics in the advanced economies are of the opinion that the compensation payout to executives of the companies worst hit in the financial crisis is a proximate factor for their failures (Bebchuk, Cohen & Spamann, 2010). Similar reason surfaced in the examination of the Nigerian financial sector by the Central Bank of Nigeria (CBN) to ascertain the impact of the global meltdown on banks and other financial institutions in the country. In the Nigerian situation, it was tacitly revealed that the banks were in "grave situation" as a result of infraction relating to conditions, among others, poor corporate governance structures, construed to include the excessive payout to executives of the banks, operating incentive scheme; excessive risk taking and ineffective risk management by directors and conflict of interest (CBN Annual Report, 2009). This narrative of the failure of banks in Nigeria is suggestive that excessive compensation leads to increased risk-taking behaviour and arguably, it is imperative to examine the potential effect of executive compensation on the financial performance of banks in Nigeria for effective policy formulation and implementation.

Literature on the effect of executive compensation on the financial performance of organisations is vast. For instance, Barkema and Gomez-Mejia (1998) assess the argument that to reduce agency costs arising from conflict of interest and self-serving behaviour on the part of agents, principals should link incentives not only to the agents' performance, but also to other informative signals of the agent's effort, since empirical evidence finds weak relationship between executive pay and performance. The empirical verification reveals simultaneous feedback (bi-directional effect) in that a firm's performance determines the extent of executive compensation and on the contrary, the shape of an executive pay package may influence firm performance.

In a somewhat obvious argument, Duffhues and Kabir (2008) carried out a study of the remuneration information using a sample of Dutch listed corporations over the period 1998-2001 and asserted that the offered theoretical framework and empirical studies in the past do not offer clear-cut information on the pay-performance relationship. These authors thus rely on the foremost widely acknowledged principal-agent theory, which postulates that compensation being a significant incentive mechanism would facilitate in orientating managerial interests with those of the shareholders. We perceived that the reward company executives typically get what would actually mirror company performance.

On the contrary, managerial power theory proposes that executive pay, being a sort of rent-seeking activity on the part of powerful managers, might not essentially demonstrate a pay-performance relationship. From the analysis, there is no systematic proof that executive pay is associated with company performance. Specifically, the authors found a statistically important negative pay-performance relationship.

Monetary incentives often times are recommended as a technique for motivating the performance of persons who use and have something to do with accounting data (Bonner & Sprinkle, 2002). These authors developed a framework in establishing the relationship between pay and performance. The framework indicates that there are varieties of accounting-related variables that may alter the consequences of incentives on performance. For instance, specific performance targets have additive positive effects on effort and performance over financial incentives. It thus, posited that unless organisations use performance targets in conjunction with incentives, workers would not be driven to larger productivity. This is indicative that pay, excessive or otherwise cannot suffice to motivate executives to influence financial performance of organisation. Sigler (2011) carried out research in this area, examining the relationship of executive officers pay and firms performance of 280 corporations listed on the New York Stock Exchange (NYSE) over the period 2006 to 2009. It is found that there exist a significant and positive relationship between executive officers pay and firms performance.

Thought concerning profit maximisation of banks relates to the risk and diversification of business. Shareholders balance their craving for increasing expected profits and minimising costs against the level of risk they are willing to accept and their consideration of the incentive structure. How pecuniary and non-pecuniary incentives are distributed between principal and agents is crucial to what is retained as profit in the bank (Bikker & Bos, 2008). Though incentive issues can help make a case for bank performance, empirical verification of whether or not they make a case for variations in bank performance seem inconclusive.

Against the background of the above discourse, some segments of the literature are of the view that executive compensation positively correlate with firms' performance while others conclude that executive compensation negatively correlate or find no relationship with firm's performance. The question is, what is the position in Nigeria banking sector arising from empirical analysis?

Literature Review

Empirical Studies

Evidence of pay-performance sensitivity in the banking sector was seen in a study carried out in UK by Gregg, Jewell and Tonks, 2012. The study examines the pay-performance relationship between executive cash compensation and firm performance for a sample of United Kingdom firms in the financial services sector. It was found that though pay within the financial services sector is high,

performance sensitivity of financial firms is not significantly higher in other sectors. Pay-performance sensitivity studies have also been explored in Africa. Adudu (2011) finds a statistically negative relationship between executive compensation and performance of commercial banks in Kenya. Similarly Erick, Kefah and Nyaoga (2014), examine the impact of executive compensation on the financial performance of insurance firms in Kenya and found a negative relationship between executive compensation and financial performance.

The Empirical studies of relationship between executive compensations and bank (firm) performance in Nigeria are scanty. Amongst a few others, Hassan and Ahmed (2012) reported a positive impact of executive compensation on firm performance in a sample of listed manufacturing firms. Kurawa and Saudi (2014) examine executive compensation and financial performance of 9 quoted banks in Nigeria over a period of five years spanning 2008–2012. The nine (9) quoted banks were selected using random and stratified sampling techniques. Multiple regression models were specified and STATA Version II software package was used for the estimation of relevant variables. The outcome of the regressions provides support for the prediction that executive compensation is relevant to the explanation of variation in banks performance. The study largely used indicators of bank performance as control variables as opposed to the use of complementary variables that reflect the effort of executive officers in enhancing bank performance. The outcome of the study may provide misleading picture of the relationship.

Olalekan and Bodunde (2015) examine the effect of CEO pay on performance of eleven (11) selected Nigerian quoted banks over the period 2005 and 2012, using a dynamic generalised method of moments (GMM). The study found that the CEO pay exerts significant negative influence on bank performance. This result upturns the earlier study on the subject that found positive relationship between executive compensation and bank performance in Nigeria. The authors argue that the incredible salaries and allowances of bank CEOs form the big drain on the banks. The study uses GMM estimator on a panel of 11 banks in Nigeria. GMM estimator uses internal instruments to deal with the correlation between the lagged endogenous variable and the time invariant components of the disturbance term. This approach has a major drawback: if the regressors display persistence overtime, their lagged levels may be very poor instruments for their differences. Thus, the outcome of the regression may not be optimal for policy formulation and implementation.

In the present framework, it would have been interesting to adopt the system GMM estimator proposed by Blundell and Bond (1998) to carry out the estimation of the models, but may not be possible due to lack of consistent data for long-time period. One way of overcoming the problem is to resort to the choice of fixed effect model that uses first differencing that handles regressors displaying persistence overtime. This is the route that is followed in the study. Another study with slight resemblance to those reviewed above is that of Bebeji, Mohammed and Tanko

(2015) which examine the effect of board size and composition on financial performance of banks in Nigeria. The study uses samples of five banks in Nigeria over the period of nine years. A judgmental sampling technique was used in selecting the five banks. Adopting multivariate regression analysis, two explanatory variables, board size and board composition were incorporated in the relationship equation. The study found that board size bears negative relationship with bank performance whereas board composition exerts positive effect on the performance of banks in Nigeria. In this study Returns on Equity (ROE) and Return on Assets (ROA) are used as indicators of bank performance (dependent variable) as opposed to other empirical studies on the issue that use the variables of ROE and ROA as control variables. The outcome of such studies could give misleading picture of the relationship between executive compensation and bank performance.

Several theoretical models make opposing predictions of the nature of correlation between pay and performance and thus imperative for empirical verification. In turn, several empirical studies using different data set and potentially misleading econometric methods fails to control for parameter heterogeneity that characterises banks operation and in many cases provide misleading picture. Financial analysis is one of the means of measuring the performance of banks and other business organisations. One major yardstick for assessing performance within the banking system is the Capital adequacy, Asset management, Earnings and Liquidity (CAMEL) approach. In CAMEL, capital adequacy is reflected by the adequacy of shareholders fund (equity) and market capitalisation (outcome or valuation of ordinary shares and market prices). Management efficiency in CAMEL is proxy by the performing loans, increase in earnings per share, deposit growth and return on equity. It shows that these variables perform due to the quality of Management in the bank. Liquidity is reflected by the high dividend payouts, interest rate spread and deposit. This approach is widely employed by the monitoring authority to assess the extent of performance of banks, before making any declaration on their soundness, solvency and liquidity position (Abdulrasheed, Adenola & Atanda, 2011). This study seeks to adapt the CAMEL framework, consistent with financial performance indicators of depository banks in Nigeria.

Against the backdrop, this study examines the effect of executive compensation on banks performance in a profitability equation of Nigerian listed commercial banks with standard policy on incentive package for executive officers over the period 2004-2015. In the process, the study determines factors that are relevant in explaining bank performance in Nigeria.

Theoretical Literature

Agency theory

Agency theory or principal-agent theory is an important, yet controversial theory used in explaining risk sharing among individuals or groups in organisation. Looking at some of the explanations put forth by early theorists like Jensen and Meckling (1976) agency relationship is seen as a contract that one or a lot of

persons (principal) contract another person (agent) to perform some services on their behalf that involves assigning some decision making authority to the agent. Consistent with these theorists, if each party to the relationship is utility maximisation, there is sensible reason to believe that the agent will not all the time act within the best interest of the principal. Here, the principal can limit divergences from his interest by establishing acceptable incentives for the agent and by acquisition monitoring costs designed to limit the aberrant activities of the agent. On the part of the agent, they also incur a bonding cost. Therefore, in most agency relationships, the principal and also the agent can incur positive monitoring and bonding costs (non-pecuniary likewise as pecuniary) and additionally, there will be some divergence between the agent's choices and those choices which surely maximise the welfare of the principal (Jensen & Meckling, 1976).

Managerial power theory

The inability of the optimal contracting model to accurately predict observed practices in executive compensation contracting gave opportunity for the exploration of optional explanations of executive pay practices (Anabtawi, 2005). The key proponents of the optimal contracting theory are Bebchuk and Fried (2003). This theory tends to be an extension of managerialism as used by Gomez-Mejia (1994) which provides a more adequate account of executive compensation. The theory argues, "that the separation of ownership and management in today's firms provides top managers virtually absolute power to use the firm to pursue their personal objectives". Bebchuk and Fried (2004) as cited in Chan (2008) argued that owing to managerial influence, arm's-length negotiation between the board and management over executive compensation has been lacking in publicly quoted corporations. For them, the arm's length contracting model is inadequate in providing an adequate account of executive compensation. However, just like the arm's length contracting view, they began the managerial power analysis by recognising the agency problem inherent within the manager-shareholder relationship. For them, the managerial power approach does not see executive compensation primarily as a remedy for the agency problem.

The theory espouse that given a particular amount of expected compensation, managers would like to possess compensation decoupled from performance. The more their compensation depends upon their performance, the more risk managers should bear, the more effort they have to exert, and the more they have to forgo self-seeking methods like empire building (Bebchuk & Fried, 2004). Consistent with the managerial power account of executive compensation contracting, managerial influence over weak boards of directors are often accustomed make a case for inefficiencies within the structure of executive compensation contracts (Anabtawi, 2005). Compensation arrangements are consistently structured to favour managers because of the absence of arm's-length bargaining between the executives and the boards of directors. This approach predicts that managers can succeed in systematically structuring their pays in ways in which are unrelated to

performance. Their ability to deal with the attributed to various strategic benefits that executives enjoy within the pay-setting method.

The benefits include (1) corporate executives influence over the director nomination process; (2) social and psychological forces which inspires directors to “go along” and “get along” with management; (3) time and informational limits on directors; (4) the flexibility of the CEO to direct economic benefits to board members on their favoured causes; and (5) the little personal costs to directors of cooperating with management. Anabtawi (2005) add that the vital building block of the managerial power approach is that of “outrage” costs. Once a board approves a compensation arrangement favourable to managers, the extent to which directors and executives bear economic and social costs can depend upon how the management is perceived by outsiders whose views pertain to the directors and executives. The more outrage a compensation arrangement is anticipated to come up with, the more reluctant directors are going to be to approve it and the more hesitant managers are going to propose it within the first place (Bebchuk & Fried, 2004).

In sum, the managerial power model of executive compensation contracting is inconsistent with the optimal contracting model since it is premised on the idea that management has captured the board of directors. This leads to pay structures benefiting managers at the expense of shareholders. Consequently, managerial power adherents advocate reforms designed to close the gaps that exist between the boards of directors and shareholders (Anabtawi, 2004).

Methodology

The study adopted a causal research design, which examines the effect as well as the relationship between executive compensation and financial performance of listed commercial banks in the Nigerian banking sector. The study employed secondary data, which was obtained from the financial statements of the audited commercial banks, various volumes of Central Bank of Nigeria (CBN) statistical bulletin and various issues of Nigerian Deposit and Insurance Corporation (NDIC). The data include annual dataset of individual bank Total Assets, Shareholders Fund, Total Performing Loan, Lending rate spread and Executive Compensation (incentive package). These sets of data are collected over the period 2004 to 2015, covering fourteen Nigerian commercial banks, namely – IBTC, UBA, Diamond, Zenith, Skye, Wema, GTB, Fidelity, Access, Union, FCMB, Ecobank, Unity and First Bank. The time scope of data collection was based on availability, consistency and usefulness in the study, particularly to have a balanced panel with greater flexibility in modelling disturbances in behaviour across individual banks (Baltagi, 2001).

Model Specification

Based on the CAMEL framework embedded in principal–agency theory, the model of bank performance in this study follows the reasoning that commercial bank

profit (proxy for performance) is a function of performing loan, value of total asset of bank, shareholders fund (equity shares), the spread between lending rate and deposit rate of the bank as well as the level of work remunerations to the executive officers. Thus, the following functional models are specified:

$$NPT = \partial_0 + \partial_1 TPL + \partial_2 TAS + \partial_3 SHD + \partial_4 IRS + \partial_5 ECP + e_1 \text{ ----- (3.1)}$$

$$NPT = \partial_0 + \partial_1 TPL + \partial_2 TAS + \partial_3 SHD + \partial_4 IRS + \partial_5 ECP + \partial_6 NPT (-1) + e_2 \text{ ---- (3.2)}$$

Where: $\partial_1 \dots \partial_6 > 0$ and,

NPT = Net Profit of Bank (Dependent variable) TPL = Total Performing Loan

TAS = Total Asset of the bank SHD = Shareholders Fund (Equity shares)

IRS = Interest Rate Spread ECP = Executive Compensation

NPT (-1) = lagged bank profit (for dynamic effect of the dependent variable)

Interest rate spread is measured by the difference between the average yield a financial institution receives from loans and other interest-accrued activities and the average rate it pays on deposits and borrowings. Data on executive compensation is limited to the components that include base salary, bonuses, profit sharing, perquisites and severance that are aggregated in the various banks audited annual reports. Data on all other variables of the model are obtained from CBN statistical bulletin and NDIC various issues as mentioned earlier.

For test of robustness of results, equation (3.2) is specified to estimate a dynamic bank operating performance model by including the lagged dependent variable. The lagged dependent variable is taken into account to allow for a possible dynamic structure in the dynamic variable. Besides, a possible advantage of adding a lagged term is that it may remove serial correlation in the model. This is expected to have positive effect on the operating performance of banks. The dependent variable is the net profit of the bank and all the other variables are taken as independent variables. Executive compensation constitutes the main variable of interest in the models.

Estimation Technique

The study is conducted using panel data. Panel data set has several advantages, one of which is that it allows greater flexibility in modelling disturbances in behaviour across individual banks (Baltagi, 2011). The prediction equations are estimated using Generalised Least Squares (GLS) with fixed effect model technique. The fixed effect model accounts for potential heteroskedasticity. It is assumed the banks are heterogeneous, thus time-invariant individual specific disturbance possibly correlate with the regressors. Based on this assumption, it is proper to estimate a Fixed Effect Model in order to account for individual specific effect. This path is followed because members of the pool (individual banks) are not selected on a random basis but rather on data consideration (consistency & availability).

To estimate the effect of executive compensation on commercial bank profits, data from the 25 Nigerian commercial banks was retrieved as at end of 2018. Considering data availability, consistency and continuity, the population was

screened further and we ended up with 18 banks. The population was screened further and ended up with a clean sample from 14 banks; whereby balanced panel data was generated at the close of business in 2015. It is from these 14 banks that the variables of the study are obtained.

Presentation and Analysis of Result

Table 1: Descriptive Statistics of the Model

Year	Mean SHD	Sd SHD	Mean TPL	Sd TPL	Mean TAS	Sd TAS	Mean IRS	Sd IRS	Mean NPT	Sd NPT	Mean ECP	Sd ECP
2004	23427.71	46226.02	44465.00	37527.18	106807.7	110056.6	14.10714	0.128388	14893.50	24248.98	98.85714	162.3078
2005	33127.21	45766.31	52865.43	48598.97	143539.7	128127.6	14.91429	0.102711	15965.36	24247.44	116.9286	165.8310
2006	55915.64	55524.26	95432.79	104613.0	293924.4	237898.4	14.08571	0.102711	17958.36	23923.71	142.7143	165.4525
2007	73265.21	61090.94	126201.3	77434.72	457035.8	283675.9	16.92143	0.157766	21604.00	23424.21	115.2143	65.94774
2008	149477.7	105087.4	235855.5	142590.8	779978.2	453558.6	10.09857	4.755316	28208.93	28816.76	191.0714	122.6261
2009	144021.5	98586.31	341111.4	264732.2	771654.8	517790.6	12.38857	6.591127	12996.93	10400.72	286.4286	178.9515
2010	146572.3	104706.2	338738.7	260346.1	814177.6	553557.3	17.98143	1.868479	33171.36	50452.29	355.4286	205.7309
2011	167360.6	115831.5	431697.9	368612.5	1061198.	670740.9	16.24143	3.179286	17102.57	18329.28	378.0000	207.9349
2012	197351.3	131190.7	774027.6	1425107.	1295068.	801404.8	13.89071	3.167291	40399.86	30944.43	340.9286	226.7515
2013	212109.6	142877.2	1273814.	2061262.	1633266.	999284.4	17.48786	3.827705	48922.29	43712.35	452.6954	248.9594
2014	240761.9	147914.3	1427132.	2090354.	1810151.	1137209.	14.78143	4.232869	50045.36	34924.87	509.0404	306.1147
2015	268945.2	163559.3	1435514.	2046041.	1852494.	1166722.	17.25143	5.477276	45356.86	39107.16	538.0996	305.4335
CAGR -Compounded annual growth rate									24.87%		18.94%	

Source: Author's Computation, 2020.

The descriptive statistics shown in the table 1 indicate that the average executive compensation was generally on the rise over the period of study except in 2007, which witnessed a dip, and accompanied by similar rise in its volatility as reflected by the increasing standard deviation. The same thing can be said of the other explanatory variables of the model (except interest rate spread) whose annual mean values in general moved in tandem with executive compensation. The mean bank performance rose relatively over the period of study up to 2008 in tandem with the executive compensation, though displayed 3years irregular pattern before levelling out to a priori trend. Hence, it can be concluded that bank performance positively relate with executive compensation in Nigeria banks. A cursory look at the table 1 also reveals that interest rate spread does not have a discernable relationship with bank performance in Nigeria.

The mean bank performance grew largely by 24.87 percent while the mean executive compensation grew by 18.94 percent on a compounded annual growth basis as shown in the table 1. In general, from the descriptive statistics, bank performance and the proximate explanatory variables of the model (except interest rate spread) have grown in tandem with executive compensation as measured by CAMEL.

Table 2: Correlation Matrix

	SHD	TPL	TAS	IRS	NPT	ECP
SHD	1.000000					
TPL	0.332869	1.000000				
TAS	0.886564	0.461317	1.000000			
IRS	0.081669	-0.037634	0.115803	1.000000		
NPT	0.599431	0.264310	0.490707	-0.004096	1.000000	
ECP	0.622037	0.120132	0.610885	0.204095	0.361912	1.000000

Source: Author's computation, 2020.

For preliminary assessment of the correlation between executive compensation and measures of bank performance, the correlation between them is examined. This is presented as correlation matrix in table 4.2. The table 4.2 reveals that all conventional measures of bank performance have positive linear correlation with executive compensation in Nigeria. In addition, the different proximate indicators do not appear to be strongly correlated with each other except for the bank total asset and shareholders fund whose correlation coefficient is 0.8865. Hence, there is little evidence of multi-collinearity among the explanatory variables incorporated in the subsequent regression analysis. Based on this bivariate correlation analysis, it is revealed that there is positive association between executive compensation and measures of bank performance in Nigeria.

Table 3: Pooled Estimate of Banks Performance Equation (Dependent variable: Banks Performance (NPT))

Variables	Model Variant i		Model Variant ii		Model Variant iii	
	Coefficient	Sig. Level	Coefficient	Sig. Level	Coefficient	Sig. Level
C	10623.40 (3034.6)	0.0006***	10997.39 (2740.)	0.0001***	13215.38 (2130.44)	0.0000***
SHD	0.040579 (0.0272)	0.1385	0.030089 (0.023)	0.2059		
TPL	0.000738 (0.0013)	0.5784	0.000727 (0.0012)	0.5606		
TAS	0.016634 (0.0035)	0.0000***	0.016923 (0.0032)	0.0000***	0.021081 (0.00207)	0.0000***
IRS	129.3724 (160.45)	0.4215	84.33667 (155.25)	0.5878		
ECP	0.024368 (0.0108)	0.0267**	0.021758 (0.009)	0.0269**	0.020077 (0.01105)	0.0717*
NPT(-1)	-0.034151 (0.0897)	0.7041			0.011488 (0.08423)	0.8917
R ²	0.75		0.77		0.75	
Adj. R ²	0.72		0.74		0.72	
D.W.Stat.	1.97		1.84		1.95	
S.E. of reg	18428.18		19282.07		18433.99	
Pool Obs	154		168		154	
Cross Section	14		14		14	

Source: Author's computation, 2020.

Notes on Table 3: Standard Errors are in Parenthesis and heterokedasticity consistent (Constant variance of error term in regression). One (*), two (**) and three (***) stars denote statistical significance at 10, 5 and 1 percent level

respectively. Based on the samples described above and the empirical model of the banks' performance, table 3 presents various pooled estimates of the basic equations to show the relationship between banks operating performance and executive compensation in Nigeria.

The column one (1) of table 3 presents pooled estimates in a Generalised Least Squares (GLS) incorporating variables that could influence banks operating performance. This model variant I report the Fixed Effect of a dynamic model of bank performance determinants equation. The results show that the relationship between the contemporaneous executive compensation and bank operating performance is positive. The outcome of the regression indicates that executive compensation offers statistical significance to the explanation of the variations in operating performance of banks in Nigeria. The results also reveal that all the variables of the model except total assets (TAS) are statistically insignificant in explaining variations in the operating performance of Nigeria commercial banks. In this model variant i, the lagged value of the dependent variable was estimated simultaneously with the standard regressors to examine the effect of inertia in the Performance variable. Specifically, the study considers the lagged dependent variable to allow for a possible dynamic structure in the candidate variables. The results obtained reveal that previous operating Performance of the bank has no precise effect on the contemporaneous performance of Nigeria commercial banks. Indeed, past period operating performance of banks cannot be reliably used to predict the future operating performance of banks in Nigeria.

For pedagogy and without loss of generality, the study considers the candidature of two key independent variables of Executive Compensation and Total Assets of banks (parsimonious model) to establish a discernible relationship between the operating Performance of Banks and Executive Compensation. The model variant iii of table 3 reports this relationship. The outcome of the estimation of the model reveals that Executive Compensation positively correlates with Bank operating Performance in Nigeria. In particular, the variable of executive compensation (ECP) is statistically significant at ten percent level with positive coefficient of 0.0201. This implies that a point rise in executive compensation at any given period would lead to 0.020 points improvement in the operating Performance of banks in Nigeria. This provides specific evidence for the empirical relevance of the managerial power and principal–agency theories, consistent with the earlier evidence by Hassan and Ahmed (2012) and Sigler (2011) that support the pay-performance postulate.

Similarly, Total Assets (TAS) has shown to be positively related to banks performance. Specifically, TAS is statistically significant at one percent level with estimated positive coefficient of 0.0210, suggesting that a point increase in the total assets of banks would cause an improvement in the operating performance by 0.0210 points. The model variant ii results corroborate the outcomes of the estimation in model variant i & ii in which total asset and executive compensation

are the variables that explain variations in operating performance of Nigeria banks. It could be observed from the models that the other explanatory variables; SHD, TPL and IRS though are positively signed as expected following CAMEL measure, they are not statistically significant to explain variations in operating performance of Nigeria banks.

It is noticeable in all the model variants that executive compensation (incentive package to banks executive) is statistically significant and positively relate to banks operating performance in Nigeria. In addition, it is observed that the diagnostic statistics are supportive of the adopted model specification. The R^2 provides evidence that the explanatory variables are capable of explaining variations in the dependent variables. The Durbin Watson Statistic (D.W. Stat.) suggests absence of higher – order auto – correlation. In general, table 3 outcomes suggest that Executive Compensation and Total Assets are significantly positively related to operating performance of banks in Nigeria. These multivariate regression results also appear consistent with the bivariate correlation earlier examined.

Conclusions

This study has examined the effects of executive compensation on banks performance in Nigeria. The evidence indicates that executive remunerations and total assets are significantly positively related to banks performance in Nigeria. Improvement in the operating performance of banks in Nigeria depends on the efficiency with which banks assets are managed. This of course can be achieved by providing the banks executives with good incentive packages (remunerations) that are geared toward improvement in the overall performance of the banks. This is an important policy option that has to be taken.

The problem of balancing incentives and the risk-taking behaviour of the executives by the principal/shareholder leads to agency problem. Thus, the challenge for future research rest on determining the threshold incentive package on executives for attainment of sustainable operating performance goals of banks.

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