

Directors' Remuneration and Firm's Performance: A Study on Malaysian Listed Firm under Consumer Product Industry

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Abstract

Remuneration is broadly used as an incentive that affects decisions made and strategies planned by directors which cause great impact on firm performance and profitability. This study aims to investigate the directors' remuneration of the consumer products sector focusing particularly on Malaysian listed companies under Consumer Product Industry. These firm's performances are measured by return on assets (ROA) and return on equities (ROE). This study consists a sample of 40 Malaysian listed companies for the period of 2012 to 2014. After controlling for board size, CEO duality, firm size, firm age, and leverage; the regression results show director remuneration has positive relationship with firm performance (measured by ROA and ROE). This suggests that high remuneration is able to motivate and retain directors in order to perform their duty and work harder for the best interest of shareholders. The result also shows all variables affect firm performance differently. For future research, we recommend that this study be expanded using more samples from other industries and other measurement of firm performances such as growth and ratings.

Keywords: remuneration, director and firm's performance

1. Introduction

Directors can generally be classified as executive directors and non-executive directors. The executive directors are highly responsible for the operation of the business which involves developing and implementing strategic plans to create sustainable value for firms in term of firm performance on behalf of the firm's shareholders. In contrast, the non-executive directors play a role in monitoring the executive directors as well as providing consultation and recommendations on running the organization. In this paper, remuneration data of both the executive and non-executive directors are jointly termed as directors' remuneration. The total remuneration received by directors can be in various components including fixed pay portion and variable short term incentives to recognize individual merit. This study includes only cash-based remuneration.

Remuneration is broadly used as an incentive that affects strategies planned and decisions made and adopted by directors which cause great impact on firm performance and profitability. It may also be simply known as a reward to the directors in realization of their efforts and hence it can motivate directors to perform their duties well and work harder for the best interests of shareholders.

Remuneration not only shapes how directors behave but also help to retain talent through attractive remuneration since directors are viewed as a scarce asset. Remuneration policy is one of the key factors in an organization's success. However, majority of these organizations are not exploiting this tool to the fullest.

As level of directors' remuneration and its relationship to firm financial performance has become a very controversial issue, public and policymakers such as governments, firms, and regulatory bodies have become more concerned on the impact of director remuneration on firm performance. Public has been highly focused on the growth of the levels of remuneration in contrast to the growth of firm performance. Therefore, there is a need to sensitize the executives to align their remuneration to firm's accounting performance measures as their pays are directly linked to shareholder's wealth maximization. According to Bebchuk and Fried (2004), they found that CEO salary has not been closely linked to firm performance. Bebchuk and Grinstein (2005) further suggested that the increase of executive pay beyond the growth of performance was observed from the year of 1993 to 2003.