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A Critical Analysis of Stipulating Remuneration Pay in Bangladeshi Listed Companies

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Abstract: Executive pay in Bangladesh continues to be a topic of conversation. Executive or CEO pay continues to be exceedingly high and growing quicker than the pay of a typical worker. The basic problem with existing compensation system in Bangladesh listed companies is that they focus exclusively on how much CEOs are paid instead of how they are paid. Of course, executive compensation in Bangladesh scenes has attracted considerable public attention and academic interest because of both the magnitude of pay and its relation to corporate performance. This article condenses that charismatic, psychological, and political factors are likely involved in determining executive compensation. According to this logic, firms should strengthen the monitoring system to ensure that the executives do not abuse their power to influence the pay settings. Boards of directors, and more increasingly these days, large institutional investors, are expected to perform such monitoring. Moreover, when the firms strengthen the appearance of shareholder value orientation, executive behaviours need to be closely monitored to ensure that they act in a way that would maximise shareholder wealth.

Key words: Executive pay, charismatic, psychological, and political factors, shareholder wealth.

Introduction

In this paper the author try to exclusively investigate the role of corporate governance (CG) in influencing a public company's practices in relation to its senior executives' pay. Specifically, the author considers the level and form of that remuneration, and how it is disclosed in the firm's financial statements. These matters are investigated in the context of an emerging economy, Bangladesh, where agency conflicts involving managers and shareholders can be much more severe than in Western countries (Claessens, et al. 2000), which have been the setting for the majority of studies of corporate governance and agency costs to date. The main question in this paper is that why executive‘s remuneration figure is always higher that chairman and non-executive ones as presented in the annual reports of listed Bangladeshi firms, and how that remuneration package is determined, is it measured by pure performance/ achievement financially or other things.Studies have found that both board composition and ownership structure affect the occurrence of corporate fraud and the likelihood of enforcement actions (Chen et al. 2006; Chen et al. 2011a, b; Firth et al. 2011; Hou and Moore 2010; Jia et al. 2009). It has also been documented that firms committing fraud experienced strong negative stock market reactions at the time of enforcement actions (Chen et al. 2005; Firth et al. 2011). There is also evidence that firms committing fraud are associated with a larger probability of auditor turnover, board chair turnover, and CEO turnover (Chen et al. 2005; Ding et al. 2010; Firth et al. 2005, 2011). That is, CEOs, board members, and auditors are all more likely to be replaced in case of corporate fraud. Before going further it gives an overview of the economic, legal and regulatory frameworks that have influenced the evolution of corporate governance structures and processes, and financial reporting practices, in Bangladesh.

Literature Review

Dhaka Stock Exchange

Dhaka Stock Exchange is one of the most important and influential institutions of Bangladesh. Governments always monitor and control DSE's activities. It is the centre of this country's stock business operation. Thus people have great acceptance and trust about DSE. Thousands of people's income sources are based on DSE. But lately few share market collapse situations occurred which made the DSE's image and acceptance to people fury. The bullish market turned bearish during 2010, with the exchange losing 1,800 points between December 2010 and January 2011. Millions of investors have been rendered bankrupt as a result of the market crash. The crash is believed to be caused artificially to benefit a handful of players at the expense of the big players. So, Government is now focusing on re-establishing the image of DSE because gaining investors trust back is the only way to keep up and running the stock market. Government has established monitoring and surveillance system in order to track and prevent from such market collapse situations and corruptions.

The main objective of the Surveillance function of the Exchange is to promote market integrity in two ways, i.e., by monitoring price and volume movements (volatility) as well as by detecting potential market abuses at a nascent stage, with a view to minimizing the ability of the market participants to influence the price of the scrip/scrip's in the absence of any Meaningful information. Market Abuse is a broad term which includes abnormal price/volume movement, artificial transactions, false or misleading impressions, insider trading, etc. In order to detect aberrant behavior/ movement, it is necessary to know the normal market behavior. The department carries out investigation, if necessary, based on the preliminary examination/analysis and suitable actions are taken against members involved based on the investigation. All the instruments traded in the market come under the Surveillance umbrella of DSE.

Manipulation is a common word heard in the capital market nowadays. When the share price of a listed company increases or decreases abnormally without any price sensitive information, then the share price of the company is suspected to be manipulated. Investigation on market manipulation is a very wide and difficult task. It takes much time since a lot of documents are to be collected and verified to find out any sort of market manipulation. Therefore, the next section will discuss the regulation pertaining investor and business' behaviours in the market.

The Regulatory and Legal Environment in Bangladesh

Bangladesh is regarded as a common law country with many of its regulations being based on British law (World Bank 2009). In 1994, Bangladesh adopted the British 'Companies Act 1913, as amended' as its primary corporate law (Companies Act 1994). The Companies Act (CA) contains provisions for Bangladeshi firms' constitution, incorporation, and winding up; structure, appointment, and responsibilities of directors; and transparency and accountability, including the appointment and responsibilities of the external auditor. It also contains provisions relating to the power and responsibilities of regulatory bodies, for instance, the RJSC and the judiciary.

The Investment Corporation of Bangladesh (ICB) was established under the Investment Corporation of Bangladesh Ordinance (1976). The government-controlled ICB is the major institutional investor in the country. Its role is to: encourage and broaden the base of investments; develop the capital market; mobilise savings; provide for matters ancillary thereto; and promote and establish subsidiaries for business development. It plays a significant role in capital market development by creating both demand and supply of securities (Chowdhury and Chowdhury 1998). In 2002, the ICB reformed its business policies and operational strategies by establishing subsidiary companies –ICB Capital Management, ICB Asset Management, and ICB Securities Trading –to pursue its three main activities of merchant banking, mutual fund operations, and stock brokerage (Haque 2007). Additionally, the responsibilities and functions of this are to ensure proper issuance of securities, protect the interest of investors in the securities and develop and regulate the capital market on a much more manageable market platform.

Bangladesh Securities and Exchange Commission (BSEC)'s Principal Acts, Rules and Regulations, 1987 to 2012

Acts, Rules and Regulations
• BSEC Rules Year: 1987 Objective: to regulate the activities of all listed companies
• BSEC Act Year: 1993, amended in 1997, 2000 and 2012 Objective: to establish the Bangladesh Securities and Exchange Commission, to protect the interests of investors in securities, to develop the securities markets
• BSEC (Meeting) Rules Year: 1994 Objective: to regulate meetings of the Securities and Exchange Commission
• BSEC (Stock-broker, Stock dealer, and Authorised Representative) Rules Year: 2000, amended in 2012 Objective: to regulate activities of stock-brokers, stock dealers and authorised representatives
• BSEC (Issue of Capital) Rules Year: 2001 Objective: to regulate issues of capital by companies or proposed companies
• BSEC (Mutual Funds) Rules Year: 2001, amended in 2011 Objective: to regulate activities of mutual funds
• BSEC (Public Issue) Rules Year: 1998, amended in 2006 and 2011 Objective: to regulate initial public offerings and secondary public offerings

- BSEC (Merger and Takeover) Rules
  Year: 2002
  Objective: to regulate mergers and takeovers
- BSEC (Security Custodial Service) Rules
  Year: 2003
  Objective: to regulate activities of securities custodians
- BSEC (Asset Backed Security Issue) Rules
  Year: 2004
  Objective: to regulate issuance of asset backed securities in the securities markets
- BSEC (Rights Issue) Rules
  Year: 2006
  Objective: to regulate new share offerings to shareholders of listed companies
- BSEC (Private Placement of Debt Securities) Rules
  Year: 2012
  Objective: to regulate issuance of debt securities by the issuer

Source: the Bangladesh Securities and Exchange Commission

A professional self-regulating body, the Institute of Chartered Accountants of Bangladesh (ICAB), regulates auditing firms, which are expected to ensure that the financial statements are prepared in accordance with a specified set of accounting standards. In 1999 ICAB adopted a number of International Accounting Standards (IASs), International Financial Reporting Standards (IFRSs) and International Standards of Auditing (ISAs) as Bangladesh Accounting Standards (BASs), Bangladesh Financial Reporting Standards (BFRSs) and Bangladesh Standards of Auditing (BSAs) respectively. This adoption of IASs was initiated following a WB grant to develop accounting and auditing standards. Since then these standards have been mandatory for listed companies and recommended for all other entities, and the responsibility lies with the BSEC for monitoring the level of compliance with these standards.

Securities of any companies are not allowed to transact stock market dealings at the Exchanges, unless the company or the securities have been listed and permission for such dealing has been granted in accordance with these regulations which only deal with the listing of the companies with the stock exchange. To get them enlisted, the applications from the companies have to be approved in the manner prescribed by the Exchange which, in granting such permission, will sufficiently consider, among other things of public interest in the company or the securities as determined by the Council of the Exchange in a well-defined procedure.

Research Method

This research adopted a case study approach to take advantage of rich information and analysis, and to provide an in-depth elucidation of it. The researchers will concern to the unique of features of the case. In order to give a representative review of works, a literature search was conducted to identify influential papers. The central issue of concern is the quality of the theoretical reasoning in which the case study researcher engages. The researchers will identify what is the main root cause of stipulating remuneration package – a dampening effect on large compensation packages threatening executive performance, and then, I will consider what is unique and what is the common across cases, that frequently promotes theoretical reflection on the findings. The focus of this study is on the cases and the unique contexts by relying on theoretical framework. In order to conduct a review of influential papers, a literature survey was done. The researchers identified the most prominent articles that discuss remuneration package, especially in Bangladesh contexts. For literature search, we used ISI Web of Science, Emerald text, Science Direct and Inderscience which we consider provide sufficient information on articles in leading scholarly journals in the area.

Findings and Conclusion

Executive Remuneration in Bangladesh

As already noted above, agency problems arise when the objectives or goals of the shareholders conflict with those of their appointed managers, especially the CEO. It has been recognised for many years that a well-designed remuneration package can play an important role in mitigating these problems (e.g. Berle and Means 1932; Jensen and Meckling 1976; Jensen and Murphy 1990; Kerr, 1975). However, the issue of how executives are best rewarded has gained greater attention over the years. Several factors underlie the increased attention. First, executives are generally perceived as recipients of overly generous pay (Cornell 2002; Geren, 1994). Second, a series of corporate collapses in the USA (for example, Enron and WorldCom) and Australia (for example, HIH, One-Tel and Harris Scarfe) have highlighted the level and nature of payments to executives and directors (Clarkson, et al, 2006; Hanrahan, et al,2007). Third, there are pronounced differences in how remuneration information is disclosed across countries.

Fourth, prior studies (for instance, Jensen and Meckling 1976; Verrecchia 1983) report managers’ incentives influence the nature of the firm’s financial reporting, even when disclosure is mandatory (Ho and Wong, 2001); and executives may use their discretionary power to vary the way information about their remuneration is disclosed. As a result, shareholders are not able either to scrutinize senior executives’ pay (Andjelkovic, et al, 2002) or to determine, accurately, how their performance and remuneration are related (Lobo and Zhou 2001).

The same situation also occurs in Bangladeshi companies that why executive‘s remuneration figure is always higher that chairman and non-executive ones as presented in the annual reports of listed Bangladeshi firms, and how that remuneration package is determined, is it measured by pure performance/ achievement financially or other things. Conventional wisdom, supported by research, is that CEOs have strong effects on organizations (Reinganum, 1985; Smith and White, 1987; Thomas, 1988).Recognizing this point, many researchers and practitioners have agreed with Bennis and O’Toole’s (2000)call for boards of directors to choose more effective CEOs by focusing on leaders with more than just standard managerial competencies and who demonstrate ‘‘integrity, provide meaning, generate trust, and communicate values’’. The basis for this argument, therefore, this paper attempts to critically analyse the characteristics associated with stipulating remuneration packages for executives among listed Bangladeshi firms. This is because Maulidi’s study in 2017 found that “in this concern, the executive‘s remuneration figures are being a sceptical thing in corporate governance scene if there is no adequate justification. In other words, executive remuneration seems closely associated with psychological factors and CEO power than firm performance”.

Executive charisma and remuneration packages

Boards of directors generally have considerable discretion in designing senior executive pay packages, which has implications for their firms’ future performance (Armstrong et al, 2012; Harris, and Bromiley, 2007). The scope of the remuneration disclosure requirements in Bangladesh is narrower and less detailed than the requirements in developed economies such as Australia, or in some other developing economies such as Hong Kong and Singapore. In Australia, the Corporations Act requires a listed firm to disclose details of its executive remuneration policies in a remuneration report, which is subject to an advisory vote by shareholders. There is no doubt that the success of stipulating CEOs’ remuneration packages in Bangladeshi listed companies can be attributed to their charisma. This has been evidenced by previous studies for example, Murphy’s, (1999) work.

In practice, most board members engage in both advising and monitoring. Of course, director‘s pay packages are determined by remuneration committees, but affirmatively, it has an impact on the persons who are being paid, and, obviously this context will lead to agent problem/dilemma. Some evidence suggested that the relationship between director/executive pays and company performance is often tenuous (Murphy, 1999), because social, psychological, and political factors are likely involved in determining executive compensation (Dogan, and Smyth, 2002).This is surprising in view of the fact that labour costs, in this company, are considered costs which are having significant impact on reducing firm‘s profit, with more than half of total costs, while in another condition shareholders need high returns from their invested money. Jensen and Meckling (1976), claimed that remuneration contract, in the agency theory framework, is one of ways to ensure that directors act in the shareholders‘ interests, but many scientists have proved that remuneration packages intended to encourage executive to act in shareholder‘s interests frequently fail (Patton, 1972).For example in remuneration report 2015, how can shareholders measure short and long-terms incentives for executives have been appropriate for their (shareholders) interests?, if they did not justify why executive pay packages substantially increase from previous year, and the chairman‘s remuneration figure is not disclosed in that report.

To support this judgment, recently, the Citigroup shareholders handed the bank a scathing rebuke, rejecting a board-approved compensation package for its senior executives [because] the bank has not anchored rewards to performance (Devers et al. 2007). For too long, business pundits and others have complained that executives are not paid in a way that links compensation to company performance. Indeed, in a *Harvard Business Review* article published over 20 years ago, financial performance in the context of a “value-maximizing entrepreneur” was touted as the most relevant basis for executive compensation:

> There are serious problems with CEO compensation, but “excessive” pay is not the biggest issue. The relentless focus on how much CEOs are paid diverts public attention from the real problem—how CEOs are paid. In most publicly held companies, the compensation of top executives is virtually independent of performance. On average, corporate America pays its most important leaders like bureaucrats. Is it any wonder then that so many CEOs act like bureaucrats rather than the value-maximizing entrepreneurs companies need to enhance their standing in world markets? (Jensen, and Murphy, 1990).

Furthermore, the author seek to shed further light on the relationship (or lack thereof) between executive compensation and firm performance. Studies on executive remuneration have found that tying remuneration to firm performance helps to motivate executives to undertake value-maximizing decisions (Jensen and Murphy 1990;

Mehran 1995; Murphy 1999; Core, Guay and Larcker 2003; Croci, 2012). For example, Mehran (1995) provides evidence that firms tend to produce higher returns to shareholders when the CEO’s remuneration is tied to corporate performance, a proxy for unobservable managerial effort or productivity. The use of compensation contracts tied to both accounting-based and market-based measures of financial performance has been suggested in prior research. For example, Dechow and Sloan (1991, p.52) claim “the existence of both performance measures in top executive compensation contracts suggests that neither measure alone provides for optimal incentive contracting. This, in turn, suggests that each measure possesses its own costs and benefits from a compensation perspective”. Relying on this logic, however, consensus about the value implications of utilizing compensation schemes laden with incentive-based pay remains elusive (Devers et al., 2007). One reason for this elusiveness is the neglect, thus far, of a multi-dimensional approach, which this paper intends to offer by investigating the relationship between executive compensation packages and risk-adjusted performance.

CEO pay in listed Bangladeshi firms is today so out of kilter with average wages that the negative side effects – demoralization, destroying the sense of community that today’s high-performing organizations need – are beginning to outweigh the oft-stated reasons for paying top dollar for executives - such as specialized expertise that will propel a company to the top of the heap.CEO pay continues to be very, very high and has grown far faster in recent decades than typical worker pay, the authors found CEO compensation in textile industries in Bangladesh, in average has risen by 617 or 938 percent (it is measured—using stock options granted or stock options realized, respectively) from 1978 to 2016. At 938 percent, that rise is more than 70 percent faster than the rise in the stock market. A typical worker’s annual compensation over the same period in average rose at the rate of 11.2%.According to these findings, the author view the CEO compensation game as an important bulwark of capitalism. Although this may be true, inflated CEO pay scales are also a sign of impending rot. While capitalism has many positives (in light of the alternatives), free market ideas in unrestrained forms have serious dysfunctional effects on society.

There is also relevant evidence from the research on transformational leadership, of which charisma is the most important element. Transformational leaders have been shown to have a strong effect on the followers’ values, self esteem, trust, confidence in the leader, and motivation to perform above and beyond the call of duty (Firth, 2007). A meta-analysis showed significant relationships between transformational leadership and effectiveness and, for our purposes here, that the specific charisma dimension of transformational leadership had stronger associations with the performance of managers in the firm than the other dimensions of transformational leadership (Gerhart, et al. 2009).

To the best of our knowledge, there are only two systematic studies that address the relationship between firm performance and CEO charisma. In one study, Waldman, et al. (2001) examined the relationship between transactional and charismatic CEO leadership and financial performance in 48 Fortune 500 firms. They found that perceived charisma had only small direct relationships with performance, but did have larger associations under conditions of uncertainty. The other study, by Francis et al.(2005), examined the underlying psychological models that boards of directors used in the search and selection of 40 CEOs. The search criteria, he concluded, are articulated in terms of such critical selection criteria as the (1) current position of a candidate, (2) performance of a candidate in his or her current position, (3) stature of the candidate’s firm, and ultimately, (4) charisma of the candidate. Using such criteria, the boards that he studied did not select CEOs who improved firm performance.

Therefore, the executive rewards and governance landscape listed Bangladeshi firms is increasingly complex. However, that transparency explains why it is hard for compensation committees to swing the axe on pay unilaterally, for fear that managers will go elsewhere. If executives do leave, firms are jolted into action. Whether performance is measured by quarterly earnings, stock prices, or something else. And yet from a review of the research on incentives motivation and charisma, it is wholly unclear why such a large proportion of these executives’ compensation packages would need to be variable. Research by Duke Professor Dan Ariely and his colleagues, for example, has shown that variable pay can substantially enhance people’s performance on routine tasks; the higher the reward, the more productive people who were working on routine jobs became. However, for people working on creative tasks — where innovative, non-standard solutions are needed – results showed that a large percentage of variable pay hurt performance. For the latter group, even when individuals could earn an additional month’s salary for performing well, variable pay reduced their ability to fulfil their task. Additionally, it have shown that, in work situations where learning is important, performance or outcome goals can have a deleterious effect on performance. In other words, workers in a wide variety of jobs are paid based on performance, which is commonly seen as enhancing effort and productivity relative to non-contingent pay schemes. However, psychological aspects suggest that excessive rewards can, in some cases, result in a decline in performance.

Company Size and the Level of Executive Remuneration

It is well-known that one of the variables most highly correlated with executive compensation is the size of the company. It does not matter whether company size is measured as assets, market value, sales revenue or number of employees — bigger firms may pay more. In other words, the link between the size of the company and the pay of the executive is one that is nearly impossible to make go away —firm size was a more risky basis for setting executives' pay than performance, which was subject to many uncontrollable forces outside the managerial sphere of influence. There was substantial evidence that firm size was a major determinant of CEO pay (Deckop, 1988; Ellig, 1984; Rosen 1982; Kostiuk 1990; Dalton et al., 2007; Pavlik et al, 1993; Roberts, 1956). Finkelstein and Hambrick (1989) believed that bigger firms tend to pay more because CEO oversees substantial resources, rather than because of their number of hierarchical pay levels. Similarly, Ellig, 1984 and Sloan (1993) believed that CEOs were paid more in larger firms primarily due to its leadership demand and more hierarchical layers exist in the larger firms. However, Finkelstein and Hambrick (1989) found that the results have varied from nil to strong positive correlations between CEO compensation and larger firms. However, Adithipyangkul and Zhang (2011) and Firth and Rui (2006) argued that using firm size as a compensable factor for CEOs were also good for board members. Sigler (2011) found that firm size appears to be the most significant factor in determining the level of total CEO compensation. His examination was based on 280 firms listed on the New York Stock Exchange from 2006 through 2009.

The basic problem with existing compensation system in Bangladesh listed companies is that they focus exclusively on how much CEOs are paid instead of how they are paid. Of course, executive compensation in Bangladesh scenes has attracted considerable public attention and academic interest because of both the magnitude of pay and its relation to corporate performance. Early studies of managerial pay schemes are focused on the determinants of pay level, particularly, the role of firm size on CEO earnings. According to the allocation theory of control, "in a market equilibrium, the most talented executives occupy top positions in the largest firms, where the marginal productivity of their actions is greatly magnified over the many people below them to whom they are linked" (Rosen 1992). This provides the theoretical ground for a 4 positive relationship between executive pay and firm size. Evidence has been reported that unanimously supports a strong positive pay-size relation (Roberts 1956; Cosh 1975; Murphy 1985; Kostiuk 1989). Another argument has put forward for the positive relation between firm size and CEO pay as larger firms may employ better qualified and better-paid managers (Rosen 1982; Kostiuk 1990).

Critics of high executive pay in Bangladeshi listed firms may say that it is not the amount so much as executives being paid no matter how well or how poorly the company does. But efforts to make pay based on performance are also often flawed. Take this example, an oil company paid its executives based on the success of the company. Of course, its success is highly dependent on the price of oil, a factor that the CEO has zero control over. In cases like these, the executive is paid more or less based on luck. In other words, the standard justification for the high pay of CEOs and other top executives is that the market demands it. It is argued that if you do not pay CEOs at or above the market, they will leave and go to a competitor. One measure of the company-size-to CEO-pay relationship is called elasticity by economists. Elasticity can be summarized as how much (in percentage terms) one thing changes due to a 1-percent increase in something else. Perhaps less frequently noted are the pay plans that provide such a big performance incentive for individuals that they can lead people to take risky and even illegal actions in order to make their pay -for-performance compensation plans pay off. Economists like to measure elasticity for all sorts of things. This led to a cultural shift that made executives (at least appear to be) more corrupt.

Theoretical framework on executive pay

The rapid rise in executive pay for Bangladeshi listed companies since the 1970s has sparked a lively debate about the determinants of executive pay. One end of the spectrum, analysed in this section, views CEO pay as the efficient outcome of a labour market in which firms optimally compete for managerial talent. The other end views that institutional factors have contributed significantly to the rise in pay.

The shareholder value view proposes that CEO contracts are the outcome of shareholder value maximizing firms that compete with each other in an efficient market for managerial talent. This view broadens what is commonly referred to as the optimal contracting view, which typically focuses on the details of bilateral contracts. We use the term shareholder value view for two main reasons. First, it emphasizes the need to take into account additional dimensions such as market forces and competitive equilibrium. Second, in reality boards are unlikely to choose the perfectly optimal contract, even if they are concerned with shareholder value rather than rent extraction. One reason is a preference for simplicity, which may restrict them to piecewise linear contracts. The theoretically optimal contract is typically highly nonlinear and never observed in reality; under a strict definition of optimal contracting, this view would be immediately rejected. A second is bounded rationality, which may lead to boards not being aware of certain (potentially non-obvious) performance measures that could theoretically improve the contract if included.

Since executive compensation is only one of a number of corporate governance issues that companies now face, we need to consider how to foster greater accountability by removing impediments to the market for the transfer of corporate control. In today's paradoxical world of maximizing shareholder value in Bangladesh the situation is the reverse. CEOs and their top managers have massive incentives to focus most of their attentions on the expectations market, rather than the real job of running the company producing real products and services. A pervasive emphasis on the expectations market actually has reduced shareholder value, created misplaced and ill-advised incentives, generated in authenticity in our executives, and introduced parasitic market players. The moral authority of business diminishes with each passing year, as customers, employees, and average citizens grow increasingly appalled by the behaviour of business and the seeming greed of its leaders. At the same time, the period between market meltdowns is shrinking, Capital markets – and the whole of the Bangladeshi capitalist system – hang in the balance. In this point, maximizing shareholder value can be viewed as the biggest concern in business. You/ firms cannot overpay a good CEO and you/firms cannot underpay a bad one. The bargain CEO is one who is unbelievably well compensated because he is creating wealth for the shareholders. If his compensation is not tied to the shareholders’ returns, everyone is playing a fool’s game. Therefore, the principal-agent problem occurs, the article argued, because agents have an inherent incentive to optimize activities and resources for themselves rather than for their principals.

These different perspectives reflect divergent views on the way that executive pay is set. Critics claim that executive compensation is essentially a rigged game, in which boards packed with insiders parcel out rewards to their friends. Defenders argue that the market is setting pay, as firms strive to keep hold of talented executives in a competitive world. Agency theory suggests that firms adopt governance mechanisms in order to mitigate this problem and to reduce the inefficiencies. Two types of governance mechanisms are widely proposed. First, executive behaviours need to be closely monitored to ensure that they act in a way that would maximise shareholder wealth. A board of directors is traditionally responsible for such a monitoring task. Since shareholders do not and cannot actively involve themselves in the day-to-day operations of the company, they elect directors to monitor the business, advise the management, and advocate shareholder interests. Their primary duties and rights include the decisions about the appointment, compensation, and termination of executive managers. In sum, a board of directors is considered one of the most important governance mechanisms to mitigate the agency problem and to advocate shareholder value, at least in theory.

To strengthen the monitoring power of boards of directors, agency theorists and shareholder value advocates argue for board independence, which in practice means appointing more outsiders to the board (Fama and Jensen, 1983). Agency theory has been widely studied by organization researchers (Dalton et al., 2007;Eisenhardt, 1989; Gomez-Mejia and Wiseman, 1997). Applied to compensation, agency theory addresses the potential lack of alignment of goals, preferences, and actions between agents (managers) and principals (shareholders) (Berle and Means, 1932). Lack of alignment results in agency costs, such as shirking, perquisites consumption, or other opportunistic behaviour by managers (Fama, 1980; Fama and Jensen, 1983a; Jensen and Meckling, 1976).The advocates maintain that outsiders are better able to monitor, evaluate, and challenge managers than are insiders; thus, boards composed largely of outsiders function as an effective monitoring mechanism. Therefore, agency theorists suggest that firms with more powerful, independent boards would more effectively prevent excessive executive pay packages and more tightly link executive pay to actual performance, compared to firms with weaker boards. In a meta-analysis of 219 studies, Vanessenet al. (2012) showed that the proportion of outsiders on the board is positively associated with the sensitivity of CEO pay to firm performance.

Another flaw in the Bangladesh system is imperfect information. Most parts of the labour market suffer from this problem, but it is particularly hard to measure how an executive’s decisions affect a firm’s performance. As a collective norm or ideology, shareholder value orientation urges top managers to focus solely on maximising financial returns for corporate investors. For example, the increased focus on financial metrics, such as share prices and dividends, is an integral part of financialisation, in which non-financial firms reallocate their investment and business operations away from traditional production processes and increasingly towards finance-related activities. As a result, understanding how such non-financial firms have become increasingly more finance-oriented in their strategies and structure requires an analysis of the incentives and rewards for the top decision-makers at these firms. Such valuation analysis must factor in the track record of the CEO; his or her potential; competing job offers; personal enticements; what he or she is leaving behind; their reputation on the street; and the team of other executives he or she is likely to bring or attract.

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