



BANK OF ENGLAND

Financialization, Corporate Governance and Employee Pay: A Firm Level Analysis

Discussion for ERFIN Workshop,
Warsaw School of Economics

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16 September 2016

Research question and hypotheses

- Effect of bank shareholder value orientation (SVO) and leverage on bank employee pay
- Higher SVO → lower employee pay
 - Plausible and of empirical interest
 - Though shareholder vs. employee distinction not clear cut, because of employee share options
- Higher leverage → lower employee pay
 - “banks use leverage strategically to renegotiate labour contracts and impose the reduction of wages”
 - Unclear if plausible in banking (cf. e.g. after a real-sector LBO / distressed takeover)?
 - Higher leverage can also increase the surplus (in boom years) to be shared between shareholders and employees (bonuses).



Econometric specification

$$\log\left(\frac{\text{pay per employee}}{\text{employee}}\right)_{ict} = \beta_{SVO}SVO_{ict} + \beta_{lev}Leverage_{ict} + \text{controls} + \varepsilon_{ict}$$

- Sample
 - 1988-2015; 4,184 banks; 121,161 bank-years
 - Mixes many firm types, and spans crisis → subsample analysis?
- Controls
 - FE provides some control for heterogeneity in business model – but business models may change over 27 years → subsample?
 - Diversification → should this be *delta* rather than level?
 - Employer size ✓ (though less important in FE specification)
 - Employee productivity ✓
- Unclear why lagging RHS vars will help – need IV if concern is simultaneity bias (e.g. Reed 2015, OBES)



Measurement issues

- Shareholder value orientation (SVO)
 - Not clear that ROAE or ROAA are good proxies
 - Alternative interpretation of the ‘within’ variation
 - Business model – time-varying activity mix and risk-taking within activity
 - Performance – potentially big variation (xsect and time) around the crisis
- Diversification
 - NII / gross revenue
 - Alternative interpretation of the ‘within’ variation
 - Changes in lending rates
 - Changes in pricing structures (split of interest income vs. fees)



Summary

- Interesting research question
- Suggest focusing on measurement and identification

