Executive compensation and firm performance: Evidence from Nepalese commercial banks

Ms. Inju Gyawali[1]

Abstract

NRB provision to relate executive's fixed annual compensation with staff salary and total assets of the respective Banks is different from those of other country (Bhatta, 2010). This is the first study to examine the relationship between executive compensation and firm performance in Nepalese banking industry. Data are collected from 21 commercial banks from the study period 2014/15 to 2020/ 21. Panel data are analyzed through pooled OLS and fixed effect model by using three control variables (i.e. Leverage, size and risk). Result showed that executive compensation is not influenced by firms performance in Nepalese commercial banks. Result also revealed that pay performance relationship is not influenced by size of the firms. It is concluded that possible reason for this insignificant relationship is contradict and impractical compensation directives issued by NRB, as claimed by (Bhatta,2010)

Key words: Compensation, performance, commercial banks, ROE, ROA

I. Introduction

The issue of executive compensation is of central importance as executive incentive misalignment has been advanced as one driver of the financial crisis of 2007–2008 (Gordon, 2010), although (Kaplan, 2013) argues that, despite high, executive paylevels have been constrained to less than 1% of company earnings for the period from 1993 to 2011. Inaddition, the effect of executive pay on market performance has declined since the financial crisis of 2008 in South Africa (Bussin & Modau, 2015). The relationship between executive pay and firm performance has been one of the most widely studied questions in the corporate governance literature (Frye, 2004; Jensen & Murphy, 1990; Murphy, 1999; Rosen, 1992). There has been an enormous growth in research on executive compensation over the last two decades with primary focus on compensation of chief executive officer (CEO). Much of this research focuses on the question whether executive compensation contracts can be justified in terms of their contribution to the firm financial performance (Devers et al. 2007; Essen et al., 2013).Despite a large literature, the global empirical evidence on the existence and strength of the relationship between firm

[1]Ms. Inju Gyawali is Asst. Professor at Lumbini Banijya Campus, Butwal, Nepal

performance and executive pay is inconclusive (Frydman & Jenter, 2010). The mixed findings are attributed to the variety of methodologies used by researchers (Callan & Thomas, 2014) and the lack of consensus on the most applicable theoretical perspective (Frydman & Jenter, 2010). Before the recent global financial crisis of 2007-2008, most empirical work on executive compensation focused on firms in the non-financial industries. However, the aftermath of the financial crisis shifted attention to financial industries (Omoregie & Kelikume, 2019.

Nepal has a short history of the modern banking practices that started from the establishment of Nepal Bank Limited as a first commercial bank in 1937. The establishment of Nepal Rastra Bank in 1956 as a central bank gave new dimension to Nepalese financial system. In the Nepalese context, banks are the major financial institutional system in Nepal, which accounted for more than 70% of the total assets of all the financial institutions (Poudel, 2005).Nepalese scenario also updated through series of the development, regarding executive compensation, specially in financial sector. The changes in the management structure of the central bank, the Nepal rastra bank (NRB) also change its policy regarding free market economy and executive compensation is one of the primary and important targets in this process. In 2011 (oct 26) NRB issued directives with the guidelines related with executive compensation. With regard to NRB provision of executive's compensation first component is fixed annual compensation or base salary. A unique formula for fixed salary is 5% of three years average salary expenses for all the staff or 0.025% of bank's assets as of the last fiscal years. Second component is performance based pay , which includes the bonus. NRB stated that if performance based pay is greater that 40% of fixed compensation, then bank should make a payment of 40% this year and remaining 60% must be paid in coming 3 years at equitable basis. Third component includes Other perquisites, in which bank can provide Mobiles or telephone expenses, vehicle and fuel expenses, internet and newspapers facilities to their chief executive officers. However these all expenses should not be greater than 0.5 % of fixed compensation.

While the literature on pay–performance has been largely focused on the Anglo-Saxon economies. Systematic research on executive compensation outside of the U.S., in particular in Asia, is still relatively scarce mostly due to the limited data availability. Specifically, unlike in the U.S., Asian firms have not been required to disclose information oncompensation for any individual executives (Kim et al., 2004).The Asian socioeconomic and behavioral peculiarities and institutional settings are different from Western World and studies conducted in Western World have limited implications for Asian countries (Fan, Wei, & Xu, 2011; Ghosh 2006; Gibson 2003;Sun, Zhao, &Yang 2010; Van Essen et al., 2012a). Although there are some evidence can be found for executive compensation and firm performance from other Asian countries.

Nepalese context is different for number of reason. First, NRB provisions for executive compensation is different from those of other emerging country like with India and others. NRB relate executive's fixed annual compensation with staff salary and total assets of the respective Banks. Formula for fixed annual compensation is either 5% of three years average salary expenses for all the staff or 0.025% of bank's assets as of the last fiscal

years. (Bhatta,2010) claimed that this unique formula for fixed compensation is rare anywhere in the world. Even in India RBI banks are flexible to determine the base salary of their CEO. (Bhatta,2010), in his paper also claimed that linking compensation with bank's assets will increase the non performing loan of the bank and currently stable banking sector will see a leading to increased bankruptcy and financial crisis. Second, NRB considered bonus as a component of performance based payment, whereas in Indian context as per the RBI regulation bonus neither considered as a part of fixed pay nor as a variable pay. Given above differences, in NRB provision for executive compensation this study provides a unique context to examine the impact of firm performance on CEO compensation in Nepalese banking sector. But till now we cannot find the study about pay performance relationship in Nepalese context, where regulation regarding the executive compensation is different from other country, (Bhatta,2010). This study therefore is an attempt to bridge this research gaps by examining the relationship between executive compensation and firm performance in Nepalese banking sector. Results of this study will be useful for NRB to formulate and change the regulations about executive compensation. It also be beneficial to human resource practitioners to formulate compensation policies for the executives.This study is focused only for banking sector of Nepal, result of this study may not be applicable to other financial sector.

II. Literature Review

Corporate governance and executive compensation disclosures in Nepal

In Nepal at the micro-level, the disclosure regime applicable to listed companies comprised of (a) accounting standards issued by Accounting Standards Board (ASB) of Nepal, (b) requirements of Securities Board of Nepal (SEBON) based on Securities Act 2006, (c)provisions of Companies Act 2006, Banks and Financial Institutions Act 2006 (BFIA), (d) listing requirements of the Nepal Stock Exchange (NEPSE), and (e) the directives from Nepal Rastra Bank (NRB) — the Central Bank of Nepal (Sharma, 2013). The banking and financial companies had a two-pronged regulatory regime requiring them to make disclosures: one by their specific regulator, Nepal Rastra Bank, and another as a public company. All banks and financial institutions registered as public companies are required to obtain a license from Nepal Rastra Bank to conduct banking business (Nepal Rastra Bank [NRB], 2010).

Nepal Rastra Bank regulates the banking sector in Nepal. The Banks and Financial Institutions Ordinance initially as an interim measure in 2005 provided the basis for regulation after being ratified by the parliament in 2006. Although, the Act has twelve chapters, the ninth chapter is the most pertinent chapter for this paper as it deals with the accounts, records, information, and reports. This act requires all registrants to follow double entry system of accounting and prepare their financial statements in the format specified by Nepal Rastra Bank (Section 59). The companies have to get their financial statements audited within five months after the end of the fiscal year. The financial statements are to be signed at least by two directors, chief executive officer, and the auditor. The auditors, upon completion of the audit, submit the audit report to Nepal Rastra Bank as well as the concerned company (Nepal Government [NG] 2006a, 2006b).

Another significant basis for mandatory disclosure was the revised Companies Act 2006. The new Companies Act came into effect from October 9, 2005 as an ordinance, ratified by the rejuvenated parliament in the year 2006 as Companies Act 2006. A major shift in the law was its orientation towards good corporate governance, improved status of the shareholders, and a better framework for financial transparency of the company affairs (Nepal Government [NG], 2006a; Shrestha, 2006). There are several provisions relating to disclosure especially the sections 76, 108 and 109 of the companies Act. Similarly, in 2011 (oct 26) NRB issued directives with the guidelines related with executive compensation. With regard to NRB provision of executive's compensation first component is fixed annual compensation or base salary. A unique formula for fixed salary is 5% of three years average salary expenses for all the staff or 0.025% of bank's assets as of the last fiscal years. Second component is performance based pay , which includes the bonus. NRB stated that if performance based pay is greater that 40% of fixed compensation, then bank should make a payment of 40% this year and remaining 60% must be paid in coming 3 years at equitable basis. Third component includes Other perquisites, in which bank can provide Mobiles or telephone expenses, vehicle and fuel expenses, internet and newspapers facilities to their chief executive officers. However these all expenses should not be greater than 0.5 % of fixed compensation.

A theoretical approach to executive compensation

There has been much debate as to the likely cause of the surge in executive pay since the mid-1980s. The academic debate has proposed several theories to address the determinants of executive compensation (Frydman and Saks 2010). Four main economic theories have been presented to explain the significant rise in executive compensation, these are: (1) the managerial rent extraction theory, (2) the scale of firms (3) the provision of incentive, and (4) increasing returns to general rather than specific skills.

The first grouping of theories associate executive compensation to managers' ability to extract rents (Bertrand, Mullainathan, 2001; Kuhnen and Zweibel, 2007). The basic view is that poor corporate governance has allowed managers to skim profits from the company thus leading to significant increase in CEO compensation. Also given that it is normally easier for executives to extract rents in the form of compensation that are more difficult for shareholders to observe or value, an explanation which could provide the justification for the recent growth in the use of stock options (Frydman & Saks, 2010). This theory suggests that the level of pay and the use of forms of remuneration that are easier to conceal (e.g. stock options) would be higher in periods when corporate governance is weaker. The second theory relates the level of compensation to firm size. Theories on the span of control and competitive assignment of CEOs to heterogeneous firms suggest a positive cross-sectional correlation between firm size and compensation (Tervio 2008; Gabaix & Landier, 2008). The premise of these models is that the variation incompensation overtime should be positively associated with increases in firm size because competition for talent raises the equilibrium level of pay when the size of all potential employers expand (Gabaix & Landier, 2008). Thus the level of pay should increase at the same rate as the expansion of the aggregate firm size. The third theory- the provision of incentives- associate the increase in compensation since the 1980s to the simultaneous increase in incentive pay

given that higher remuneration may be required to compensate risk adverse executives for a riskier stream of income. Finally, researchers have associated the recent rise in compensation to changes in the type of managers.One explanation suggested by (Murphy & Zábojník, 2004) is that CEO pay has risen due to the increasing importance of general managerial skills relative to firm specific abilities. The explanation is that we should expect a higher average and more dispersion of pay across executives as managerial skills become more general (Frydman & Saks, 2010).

Executive compensation and firm performance

In one of the earliest studies, (Jensen & Murphy,1990) empirically examined the relationship between CEO compensation and firm performance. They considered a large sample of US firms during the period of 1974–1986. They computed an estimate of the pay for performance sensitivity (PPS) and reported that firm performance positively influences CEO compensation. (Hall & Liebman, 1998) found a significant positive relationship between firm performance and CEO compensation. They observed that such a relationship has been the result of changes in the value of CEO holdings of stock and stock options. Similarly, A number of studies (e.g. Bayless 2009; Buck, Liu, & Skovoroda 2008; Conyon and He 2011; Conyon and He 2012; Ozkan 2011) find evidence that there is a significant positive relationship between executive compensation and firm performance. (Smirnova & Zavertiaeva 2017) produced evidence that indicated the link between the bonus payment and accounting-based measures in European firms. The Sharpe ratio, as a measure of market performance, influenced all compensation components except benefits. (Pereira & Esperanc¸2015) found that the magnitude of the variable compensation of Portuguese executives was not associated with the performance of firms. Instead, firms with lower productivity levels were found to pay higher levels of variable compensation. (Sakawa et al. 2012) found that firm profit of ROA and stock return were significant and positive related to the Japanese executives' short-term incentives. The authors also emphasized that foreign shareholders tended to adopt more long-term incentives rather than short-term incentives, indicating they were concerned with higher standards of corporate governance. According to (Croci et al. 2012), institutional investors from Continental European firms demonstrate a preference for the executive compensation structure to be more intensely linked to market metrics, which tends to raise share prices. (Beavers ,2018) found that the use of inside debits in executive compensation reduced agency costs between shareholders and debt holders. Also, the compensatory structure based on inside debits impacted the firms' debt structure.

The compensation–performance relationship reaches very specific outlines in emerging countries, in which concentrated ownership prevails (Gallego & Larrain, 2012). (Larkin et al. 2018) and (Moshirian et al. 2017) emphasize that capital markets in less developed countries tend to not be translated into efficient mechanisms for transmitting information between the various economic agents. Because of these specificities, market metrics may not be the most suitable indicator for managers' compensation. (Sheikh et al. 2018) highlight that the volatility of the Pakistan stock market restricts the linking of market metrics to the executive compensatory contracts. The findings of(Raithatha and Komera ,2016) did not show a pay–performance relationship among Indian firms when their performance was

proxied by market-based measures. In Brazil, on the other hand, (Aguiar & Pimentel, 2017) found a positive association between the variable incentives and market- and accounting-based performances. The authors emphasized the positive relationship between the stock-based compensation and the price-to-equity ratio, suggesting that the long-term incentive played its role in creating long-term value. (Abraham & Singh, 2016) found a robust positive association between executive remuneration and the growth in the rates of return of controlling shareholders . As highlighted in the above literature it is expected that there is a positive relationship between executive compensation and firm performance.

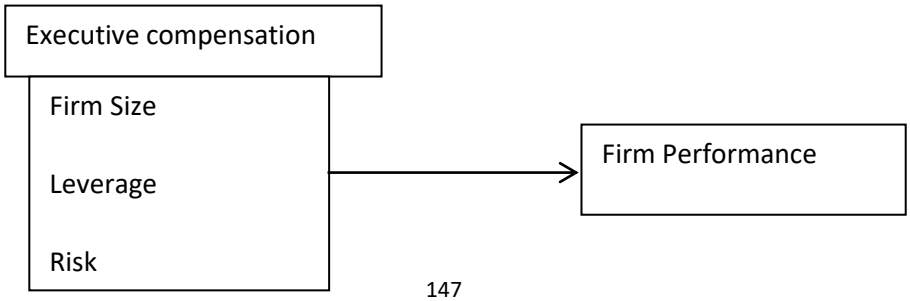
Executive compensation and firm specific characteristics

Firm specific characteristics such as size, leverage, and risk are expected to influence executive compensation. (Rosen ,1992) provides a theoretical justification for the positive relation between executive pay and firm size. Empirical studies such as (Murphy,1985), (Zhou ,2000), and (Ryan & Wiggins 2001) reported that firms' size positively influences their executive compensation. (Murphy ,1999), on the contrary, reported that pay performance sensitivity is weaker among the larger US firms. several researchers have empirically documented a strongly negative relationship between firm size and pay–performance sensitivity, including (Jensen & Murphy,1990a; Garen, 1994; Hadlock & Lumer, 1997; Schaefer, 1998; Murphy,1999; Jin, 2002). In particular, (Hadlock & Lumer,1997) provide compelling empirical evidence that not properly controlling for firm size yields a misspecification of the model, potentially resulting in invalid inferences from regression results. In the light of this mixed evidence on the relationship between executive compensation and firm size, sensitivity of pay performance relationship is examined by classifying the sample firm into large and small size.

Studies such as (Palepu & Healy, 2007) and (Penman,2007) empirically support the argument that there is a negative association between firms' leverage ratios and their executive compensation. (John &john, 1993) also argued that there is negative relation between the debt level and the use of incentive pay.Firm specific risk is another potential determinant of executive compensation. This study consider beta as a measure of risk for the firm with respect to market. (Brick et al.,2012) find that cash flow risk has significant negative association with cash compensation of the CEO.Jin (2002) also finds a negative relation between risk and pay–performance sensitivity in an augmented model.Thus three variables (ie, size , leverage and risk) are used as control variable. Conceptual framework is presented below:

Figure 1

Conceptual Framework



III. Methodology

There are 27 commercial banks in Nepal till mid July 2021. Among them three government owned commercial banks are operated in Nepal. As per the NRB directives, provision of executive compensation is not apply for the government owned banks. Those three government owned banks are excluded from the sample. Similarly, this provision also not applies for those joint venture commercial banks, which are operated under, technical service agreement (TSA) with foreign subsidiary and their CEO's are non-Nepali citizens. Thus three more joint venture commercial banks (ie, Nepal SBI bank Standard chartered bank and Everest bank) also excluded from sample. Final sample consist of 21 commercial bank. Since most of the commercial banks started to disclose their executive compensation details from fiscal year 2014/15 onwards. Study period is from 2014/15to 2020/2021. Data are collected from annual report of respective banks. These panel data are analyzed through pooled OLS and fixed effect model.

Here executive compensation is used as a proxy for pay. Accounting measures is used to represent firm performance (Antle & Smith, 1986; Lambert & Larcker, 1987; Raithatha & Komera, 2016)). Following (Murphy,1985; Jensen and Murphy 1990; Gibbons and Murphy, 1990; Raithatha & Komera, 2016), (Sheikh et al., 2018), (Shrestha, 2020)return on equity (ROE) and ROA are used as the accounting based measures of firm performance. Further, firm specific variables such as size, leverage, and risk are considered as control variables, they could influence the pay–performance relationship. Since (Harford and Li,2007) find evidence that merger and acquisition insulate pay-performance sensitivity. Dummy variable is also used to consider the pre and post merger period. Where 0 is used for pre merger period and 1 is used for post merger period.

Description of the variables is provided in following table:

Table 1

Description of variables considered in the study.

Variables	Description
ROA	Ratio of net income to total assets
ROE	Ratio of net income to book value of equity
Size	Natural logarithm of total assets
LEV	Ratio of total debt to total equity
Risk	It refers to company's beta calculated considering NEPSE as the market index

Estimation procedure and discussion

The model that is used to analyze the data is as follows;

$$\ln(\text{compensation}_{it}) = \alpha_i + \beta_1 Y_{it} + \gamma Z_{it} + \tau_t + \varepsilon_{it}$$

Where *Ln (compensation)* is the natural logarithm of executive compensation. *Yit* is a measure of performance of the *i th* firm in *t th* year. *Z* is a vector of other firm specific variables that affect executive compensation. τ refers to time dummies and ε is a error term. Equation is estimated by using pooled ordinary least squares (POLS) and panel fixed effects (FE) estimators. The FE estimator effectively controls the sample firms' unobservable fixed effects. Study considers firm's accounting (ROA and ROE) as performance measures. Other firm specific variables are firm size, leverage, and market risk are used as control variables.

IV. Analysis and Discussion

Table 2

Descriptive statistics of variables

Variable |	Obs	Mean	Std. Dev.	Min	Max
lncompensa~t |	126	16.44867	.390272	15.57686	17.48576
ROA_t |	126	.0174274	.0183127	.0054929	.2044094
ROE_t |	126	.1501518	.1486138	.0055751	1.727967
Leverage_t |	126	7.94095	2.112599	.0149665	13.76892
size_t |	126	24.80398	1.496492	18.25526	26.33594
Beta_t |	126	.6668874	.2873561	.16734	1.179401

Table 2 summaries the descriptive statistics of the dependent and independent variables. Average of ROA for sample firm is 1.742% as compared to 1.669 % reported by (Bhattrai, 2016), 1.49% reported by (Budhathoki et al. 2020) and 1.82% by (Shrestha, 2019) for Nepalese commercial banks. Table depicts the wide range of leverage which is the ratio of total debt to equity. It ranges from minimum value 0.149665 to 13.76892, with mean value of 7.94095. Similarly mean value of size and beta is 24.80 and 0.666 respectively.

Table 3 shows relationship between dependent variable (ie CEO's compensation) with independent variable (ROA), using the control variables leverage, size and risk. Coefficient of independent variable (ROA) is found positive , which means there is the positive relationship between banks performance and CEO's compensation. But this coefficient is not significant. Thus no statically significant relationship can be found between CEO's

Table 3

Estimation of relationship between CEO's compensation and firm performance (ROA)

	Pooled ordinary least square	Panel fixed effect
ROA_t	2.726923 .6304734	
	(0.180)	(0.708)
Leverage_t	-.0381918	-.0425916
	(0.021)**	(0.016)
size_t	.0708585	.3871019
	(0.011)**	(0.000)***
Beta_t-.2061953	-.0937155	
	(0.092)	(0.0925)
Dummy variable	-.0736977	.0407181
	(0.444)	(0.719)
Constant	15.14227	7.206221
	(0.000)***	(0.000)***
No.Of Observatio	(126)	(126)
R- Squared	0.1080	
Adj- R squared	0.0708	
Prob > F =	0.0164	

Depended variable is CEO's compensation, is measured by natural logarithm of total compensation. ROA is measured as ratio of net income to total assets. Leverage is measured as ratio of total debt and total equity. Size indicate the natural logarithm of firm's total assets. Beta is beta calculated considering NEPSE as the market index. Dummy variable take value 1for the period , in which firm's goes under merging. And 0 otherwise.
***, **, and * refer to 1%, 5%, and 10% significance level, respectively. The numbers in parenthesis are corresponding p-values

compensation and performance of firms. The result is consistent with , (Pereira & Esperanca 2015; Yusuf & Abubakar 2014; Keller 2014 ; Jegede 2012; Elayan et al. 2003) who found there is no significant relationship between executive compensation and firm's performance. Similarly, coefficient of leverage is found negatively significant relationship with CEO's compensation. which means increase in firm's leverage leads to decrease the CEO's compensation. This result is consistent with (Raithatha & Komera 2016; Seo et al. 2018) . There is positive and significant relationship between firm's size and CEO's compensation. Such a finding is consistent with those reported by (Rosen ,1992; Murphy 1985; Zhou ,2000; Ryan &Wiggins, 2001) (from the US market). Since the coefficient of dummy variables is not significant, it can be said that CEO's compensation does not differ in merger and pre merger time.

Since VIF value shows that there is a multicolinarity problem between both measure of accounting performance (ie ROA and ROE). Data are separately analyzed for both measures. But result for both measure is found similar. Both table (ie table no. 3 and 4) shows that there is no significant relationship between CEO's compensation and bank's performance.

Table 4

Estimation of relationship between CEO compensation and firm performance (ROE)

	Pooled ordinary least square	Panel fixed effect
ROE_t	.2958598	.0061684
	(0.235)	(0.976)
Leverage_t	-.0445249	-.0441758
	(0.009)**	(0.010)
size_t	.0688521	.382464
	(0.013)**	(0.000)***
Beta_t	-.1973151	-.0867561
	(0.107)	(0.0825)
Dummy variable	-.0741632	-.0399067
	(0.442)	(0.725)
Constant	15.239877	.206221
	(0.000)***	(0.000)***
No.Of Observation	(126)	(126)
S- Squared	0.1051	
Adj- R squared	0.0678	
Prob > F = 0	.0192	

Depended variable is CEO's compensation, is measured by natural logarithm of total compensation. ROA is measured as ratio of net income to total assets. Leverage is measured as ratio of total debt and total equity. Size indicate the natural logarithm of firm's total assets. Beta is beta calculated considering NEPSE as the market index. Dummy variable take value 1for the period , in which firm's goes under merging. And 0 otherwise.

***, **, and * refer to 1%, 5%, and 10% significance level, respectively. The numbers in parenthesis are corresponding p-values

Since the various literature (Jensen & Murphy, 1990a; Garen ,1994; , Hadlock & Lumer, 1997; Schaefer, 1998; Murphy, 1999; Jin, 2002) Shows that pay performance relationship is influence by firm size. Researcher is attempt to empirically validate the heterogeneity in the magnitude of pay–performance relationship by classifying the firm year observations based on the firms' size. Sample firms are classify into quartile groups based on the value of firms' assets. Firms that fall in the first and second quartile as small, and those that fall in the third and fourth quartile as large firms. Eq. (1) is separately estimated using both the small and large firms.

Table 5

Relationship between compensation and firm performance in small and large firms

Small firms		Large firm	
ROA_t	.6443638	1.385884	
	(0.681)	(0.898)	
Leverage_t	-.0592562	-.0172499	(0.000)***
	(0.511)		
size_t	.0542977	.6771168	(
	0.048)*	(0.000)***	
Beta_t	-.0671712	-.2519495	
	(0.640)	(0.059)	
Dummy variable	.0804057	-.0572474	
	(0.436)	(0.663)	
No. Of Observation	(62)	(64)	
R -Squared	0.3124	0.3674	
Adj- R squared	0.2510	0.3129	
Prob > F = 0.0001			

Depended variable is CEO's compensation, is measured by natural logarithm of total compensation. ROA is measured as ratio of net income to total assets. Leverage is measured as ratio of total debt and total equity. Size indicate the natural logarithm of firm's total assets. Beta is beta calculated considering NEPSE as the market index. Dummy variable take value 1for the period , in which firm's goes under merging. And 0 otherwise.

***, **, and * refer to 1%, 5%, and 10% significance level, respectively. The numbers in parenthesis are corresponding p-values

The above table also shows the similar result as shown by table number 3 and 4. This table also depicts that there is no significant relationship between executive compensation and firm performance in large and small firms. Thus it can be concluded that pay performance relationship in Nepalese banking industry does not influence by their size.

V. Conclusion

This study is conducted to empirically examine the pay performance relationship among Nepalese commercial banks between the period of 2015 to 2020 by taking the sample of 21 commercial banks.The variable used to represent the bank performance are ROA and ROE. And natural logarithm of total compensation of CEO is used as a proxy for pay. Panel data are analyzed through pooled OLS and fixed effects model. Result shows that , there is no significant relationship is exist between CEO's compensation and performance in Nepalese commercial banks which is consistent with the findings of (Pereira & Esperanca 2015; Yusuf & Abubakar 2014; Keller 2014 ; Jegede 2012; Elayan et al. 2003). The

possible reason for insignificant relationship between compensation and performance is that the compensation directive issued by NRB is contradict with internationally acceptable principal and it is also proved impractical as claimed by (Bhatta ,2016). It also can be concluded that CEO's compensation does not differ in merger and pre merger time.

Further research can be carried by taking the data of all Nepalese financial institutions . Since It may also be argued that the firm's performance is also influenced by the previous executive compensation. The potential simultaneous relationship between executive compensation and firm performance may cause the endogeneity problem. Further research also can be carried by using system-GMM estimator (Blundell & Bond, 1998) to address the issue of simultaneous bias (endogeneity).

References

Abraham, E., & Singh, G. (2016). Does CEO duality give more influence over executive pay to the majority or minority shareholder? (A survey of Brazil). *Corporate Governance: The International Journal of Business in Society*, *16*(1), 96–115. https://doi.org/10.1108/CG-05-2015-0073

Aguiar, A. B. de, & Pimentel, R. C. (2017). Executive compensation and performance in the Brazilian market: Contemporary and lagged relationships/Remuneracao de executivos e desempenho no mercado brasileiro: relacoes contemporaneas e defasadas. *RAC - Revista de Administracao Contemporanea*, *21*(4), 545–569.

Antle, R., & Smith, A. (1986). An Empirical Investigation of the Relative Performance Evaluation of Corporate Executives. *Journal of Accounting Research*, *24*(1), 1–39. https://doi.org/10.2307/2490802

Bahadur, Rai, C., Kumar, K., Prasad, R., Budhathoki, P., Lamichhane, K., Bhattarai, G., & Rai, A. (2020). The Impact of Liquidity, Leverage, and Total Size on Banks' Profitability: Evidence from Nepalese Commercial Banks. *Journal of Economics and Business*, *3*, 545–555. https://doi.org/10.31014/aior.1992.03.02.219

Beasley, J. S. (2012). *Research Handbook on Executive Pay*. Edward Elgar Publishing.

Beavers, R. (2018). What Matters Most in CEO Compensation? *SPU Works*. https://digitalcommons.spu.edu/works/131

Bebchuk, L. A., & Fried, J. M. (2003). Executive Compensation as an Agency Problem. *Journal of Economic Perspectives*, *17*(3), 71–92. https://doi.org/10.1257/089533003769204362

Bertrand, M., & Mullainathan, S. (2001a). Are CEOs Rewarded for Luck? The Ones Without Principals Are*. *The Quarterly Journal of Economics*, *116*(3), 901–932. https://doi.org/10.1162/00335530152466269

Bertrand, M., & Mullainathan, S. (2001b). Are CEOs Rewarded for Luck? The Ones Without Principals Are*. *The Quarterly Journal of Economics*, *116*(3), 901–932. https://doi.org/10.1162/00335530152466269

Bhatta, K. P. (2012). *Is the Central Bank Gone Mad: Executive Compensation with Reference to the Nepalese Banking Industry* (SSRN Scholarly Paper ID 2138732). Social Science Research Network. https://papers.ssrn.com/abstract=2138732

Bliss, R. T., & Rosen, R. J. (2001). CEO compensation and bank mergers. *Journal of Financial Economics*, *61*(1), 107–138. https://doi.org/10.1016/S0304-405X(01)00057-5

Blundell, R., & Bond, S. (1998). Initial conditions and moment restrictions in dynamic panel data models. *Journal of Econometrics*, *87*(1), 115–143. https://doi.org/10.1016/S0304-4076(98)00009-8

Brick, I. E., Palmon, O., & Wald, J. K. (2012). Too Much Pay-Performance Sensitivity? *The Review of Economics and Statistics*, *94*(1), 287–303. https://doi.org/10.1162/REST_a_00142

Buck, T., Liu, X., & Skovoroda, R. (2008). Top executive pay and firm performance in China. *Journal of International Business Studies*, *39*(5), 833–850. https://doi.org/10.1057/palgrave.jibs.8400386

Business Analysis and Valuation: Using Financial Statements—Text Book—Faculty & Research—Harvard Business School. (n.d.). Retrieved August 22, 2021, from https://www.hbs.edu/faculty/Pages/item.aspx?num=31772

Bussin, M., & Modau, M. F. (2015). The relationship between Chief Executive Officer remuneration and financial performance in South Africa between 2006 and 2012: Original research. *SA Journal of Human Resource Management*, *13*(1), 1–18. https://doi.org/10.4102/sajhrm.v13i1.668

Callan, S. J., & Thomas, J. M. (2014). Relating CEO Compensation to Social Performance and Financial Performance: Does the Measure of Compensation Matter? *Corporate Social Responsibility and Environmental Management*, *21*(4), 202–227. https://doi.org/10.1002/csr.1307

Conyon, M. J., & He, L. (2011). Executive compensation and corporate governance in China. *Journal of Corporate Finance*, *17*(4), 1158–1175. https://doi.org/10.1016/j.jcorpfin.2011.04.006

Corbet, S., Meegan, A., Larkin, C., Lucey, B., & Yarovaya, L. (2018). Exploring the dynamic relationships between cryptocurrencies and other financial assets. *Economics Letters*, *165*, 28–34. https://doi.org/10.1016/j.econlet.2018.01.004

Croci, E., Gonenc, H., & Ozkan, N. (2012). CEO compensation, family control, and institutional investors in Continental Europe. *Journal of Banking & Finance*, *36*(12), 3318–3335. https://doi.org/10.1016/j.jbankfin.2012.07.017

Dias, A., Vieira, V., & Figlioli, B. (2020). Tracing the links between executive compensation structure and firm performance: Evidence from the Brazilian market. *Corporate Governance: The International Journal of Business in Society*, *20*(7), 1393–1408. https://doi.org/10.1108/CG-05-2020-0199

ELAYAN, F. A., LAU, J. S. C., & MEYER, T. O. (2003). EXECUTIVE INCENTIVE COMPENSATION SCHEMES AND THEIR IMPACT ON CORPORATE PERFORMANCE: EVIDENCE FROM NEW ZEALAND SINCE COMPENSATION DISCLOSURE REQUIREMENTS BECAME EFFECTIVE. *Studies in Economics and Finance*, *21*(1), 54–92. https://doi.org/10.1108/eb028769

Essen, M. van, Engelen, P.-J., & Carney, M. (2013). Does "Good" Corporate Governance Help in a Crisis? The Impact of Country- and Firm-Level Governance Mechanisms in the European Financial Crisis. *Corporate Governance: An International Review*, *21*(3), 201–224. https://doi.org/10.1111/corg.12010

Fan, J. P. H., Wei, K. C. J., & Xu, X. (2011). Corporate finance and governance in emerging markets: A selective review and an agenda for future research. *Journal of Corporate Finance*, *17*(2), 207–214. https://doi.org/10.1016/j.jcorpfin.2010.12.001

Frye, M. B. (2004). Equity-Based Compensation for Employees: Firm Performance and Determinants. *Journal of Financial Research*, *27*(1), 31–54. https://doi.org/10.1111/j.1475-6803.2004.00076.x

Frydman, C. and Jenter, D. (2010), "CEO compensation", Annual Review of Financial Economics, Vol. 2 No. 1, pp. 75-102.

Gallego, F., & Larrain, B. (2012). CEO compensation and large shareholders: Evidence from emerging markets. *Journal of Comparative Economics*, *40*(4), 621–642. https://doi.org/10.1016/j.jce.2012.02.003

Ghosh, A. (2006). Determination of Executive Compensation in an Emerging Economy. Evidence from India. *Emerging Markets Finance and Trade*, *42*(3), 66–90. https://doi.org/10.2753/REE1540-496X420304

Gibson, M. S. (2003). Is Corporate Governance Ineffective in Emerging Markets? *Journal of Financial and Quantitative Analysis*, *38*(1), 231–250. https://doi.org/10.2307/4126771

Gordon, J. N. (2010). *Executive Compensation and Corporate Governance in Financial Firms: The Case for Convertible Equity-Based Pay* (SSRN Scholarly Paper ID 1633906). Social Science Research Network. https://doi.org/10.2139/ssrn.1633906

Hadlock, C. J., & Lumer, G. B. (1997). Compensation, Turnover, and Top Management Incentives: Historical Evidence. *The Journal of Business*, *70*(2), 153–187. https://doi.org/10.1086/209714

Hall, B. J., & Liebman, J. B. (1998). Are CEOs Really Paid Like Bureaucrats?*. *The Quarterly Journal of Economics*, *113*(3), 653–691. https://doi.org/10.1162/003355398555702

Harford, J., & Li, K. (2007). Decoupling CEO Wealth and Firm Performance: The Case of Acquiring CEOs. *The Journal of Finance*, *62*(2), 917–949. https://doi.org/10.1111/j.1540-6261.2007.01227.x

Healy, Paul M., and Krishna G. Palepu. *Business Analysis and Valuation: Using Financial Statements*. 4th ed. Mason, OH: Thomson South-Western, 2007.

Jensen, M. C., & Murphy, K. J. (2015). Performance Pay and Top-Management Incentives. *Journal of Political Economy*. https://doi.org/10.1086/261677

Jha, S., & Hui, X. (2012). A comparison of financial performance of commercial banks: A case study of Nepal. *African Journal of Business Management*, *6*(25), 7601–7611. https://doi.org/10.5897/AJBM11.3073

Jin, L. (2002). CEO compensation, diversification, and incentives. *Journal of Financial Economics*, *66*(1), 29–63. https://doi.org/10.1016/S0304-405X(02)00150-2

Kaplan, S. N. (2013). CEO Pay and Corporate Governance in the U.S.: Perceptions, Facts, and Challenges. *Journal of Applied Corporate Finance*, *25*(2), 8–25. https://doi.org/10.1111/jacf.12013

Kato, T., Kim, W., & Lee, J. H. (2007). Executive compensation, firm performance, and Chaebols in Korea: Evidence from new panel data. *Pacific-Basin Finance Journal*, *15*(1), 36–55. https://doi.org/10.1016/j.pacfin.2006.03.004

Kim, W., Kato, T., & Lee, J.-H. (2004). *Executive Compensation and Firm Performance in Korea* (SSRN Scholarly Paper ID 480544). Social Science Research Network. https://doi.org/10.2139/ssrn.480544

Kuhnen, C. M., & Zwiebel, J. H. (2008). Executive Pay, Hidden Compensation and Managerial Entrenchment. *SSRN Electronic Journal*. https://doi.org/10.2139/ssrn.972622

Murphy, K. J. (1985). Corporate performance and managerial remuneration: An empirical analysis. *Journal of Accounting and Economics*, *7*(1), 11–42. https://doi.org/10.1016/0165-4101(85)90026-6

Murphy, K. J. (1999). Chapter 38 Executive compensation. In *Handbook of Labor Economics* (Vol. 3, pp. 2485–2563). Elsevier. https://doi.org/10.1016/S1573-4463(99)30024-9

Murphy, K. J., & Zábojník, J. (2004). CEO Pay and Appointments: A Market-Based Explanation for Recent Trends. *American Economic Review*, *94*(2), 192–196. https://doi.org/10.1257/0002828041302262

Omoregie, O. K., & Kelikume, I. (2019). *Executive Compensation and Insurance Sector Performance: Evidence from Nigeria* (SSRN Scholarly Paper ID 3506634). Social Science Research Network. https://papers.ssrn.com/abstract=3506634

Ozkan, N. (2011). CEO Compensation and Firm Performance: An Empirical Investigation of UK Panel Data. *European Financial Management*, *17*(2), 260–285. https://doi.org/10.1111/j.1468-036X.2009.00511.x

Paudel N. P. (2005). Financial system and economic development. Nepal Rastra bank in 50 years. Kathamndu: Nepal Rastra Bank.

Penman, S. H. (2007). Financial reporting quality: Is fair value a plus or a minus? *Accounting and Business Research*, *37*(sup1), 33–44. https://doi.org/10.1080/00014788.2007.9730083

Pereira, I. N., & Esperança, J. P. (2015a). Top executive compensation in less developed capital markets. *Corporate Governance*, *15*(1), 122–133. https://doi.org/10.1108/CG-11-2014-0128

Pereira, I. N., & Esperança, J. P. (2015b). Top executive compensation in less developed capital markets. *Corporate Governance*, *15*(1), 122–133. https://doi.org/10.1108/CG-11-2014-0128

Performance Pay and Top-Management Incentives | Journal of Political Economy: Vol 98, No 2. (n.d.-a). Retrieved August 21, 2021, from https://www.journals.uchicago.edu/doi/abs/10.1086/261677

Performance Pay and Top-Management Incentives | Journal of Political Economy: Vol 98, No 2. (n.d.-b). Retrieved August 22, 2021, from https://www.journals.uchicago.edu/doi/abs/10.1086/261677

Raithatha, M., & Komera, S. (2016). Executive compensation and firm performance: Evidence from Indian firms. *IIMB Management Review*, *28*(3), 160–169. https://doi.org/10.1016/j.iimb.2016.07.002

Ryan, H. E., & Wiggins, R. A. (2001a). The influence of firm- and manager-specific characteristics on the structure of executive compensation. *Journal of Corporate Finance*, *7*(2), 101–123. https://doi.org/10.1016/S0929-1199(00)00021-3

Ryan, H. E., & Wiggins, R. A. (2001b). The influence of firm- and manager-specific characteristics on the structure of executive compensation. *Journal of Corporate Finance*, *7*(2), 101–123. https://doi.org/10.1016/S0929-1199(00)00021-3

Sakawa, H., Moriyama, K., & Watanabel, N. (2012). Relation between Top Executive Compensation Structure and Corporate Governance: Evidence from Japanese Public Disclosed Data. *Corporate Governance: An International Review*, *20*(6), 593–608. https://doi.org/10.1111/j.1467-8683.2012.00928.x

Schaefer, S. (1998). The Dependence of pay—Performance Sensitivity on the Size of the Firm. *The Review of Economics and Statistics*, *80*(3), 436–443. https://doi.org/10.1162/003465398557537

Sharma, N. (2013). Disclosure regime for mandatory disclosures by banks and financial institutions in Nepal. *International Journal of Accounting and Financial Reporting*, *3*(1), 64. https://doi.org/10.5296/ijafr.v3i1.2996

Sheikh, M. F., Shah, S. Z. A., & Akbar, S. (2018). Firm performance, corporate governance and executive compensation in Pakistan. *Applied Economics*, *50*(18), 2012–2027. https://doi.org/10.1080/00036846.2017.1386277

Shrestha, P. M. (2020). Determinants of Financial Performance of Nepalese Commercial Banks: Evidence from Panel Data Approach. *NRB Economic Review*, *32*(2), 45–59. https://doi.org/10.3126/nrber.v32i2.35300

Smirnova, A. S., & Zavertiaeva, M. A. (2017). Which came first, CEO compensation or firm performance? The causality dilemma in European companies. *Research in International Business and Finance*, *42*, 658–673. https://doi.org/10.1016/j.ribaf.2017.07.009

Sun, S. L., Zhao, X., & Yang, H. (2010). Executive compensation in Asia: A critical review and outlook. *Asia Pacific Journal of Management*, *27*(4), 775–802. https://doi.org/10.1007/s10490-010-9207-7

Tervio, M. (2008). The Difference That CEOs Make: An Assignment Model Approach. *American Economic Review*, *98*(3), 642–668. https://doi.org/10.1257/aer.98.3.642

Van Essen, M., P. P. M. A. R. Heugens, J. Otten, and J. Van Oosterhout. 2012a. "An Institution-Based View of Executive Compensation: A Multilevel Meta-Analytic Test." Journal of International Business Studies 43: 396–423.

Zhou, X. (2000). CEO pay, firm size, and corporate performance: Evidence from Canada. *Canadian Journal of Economics/Revue Canadienne d'économique*, *33*(1), 213–251. https://doi.org/10.1111/0008-4085.00013