

The nexus between executive compensation and performance: Case of Islamic Banks

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ABSTRACT

The aim of this study is to investigate the nexus between executive compensation and performance in Islamic banks (IBs). The relationship was examined through the direct effect of performance and the joint effect of governance and performance on pay. This study used static and dynamic panel regressions. These models are applied to determine the impact of performance on executive compensation using two different approaches: traditional and dynamic. The generalized method of moments (GMM) model was employed to avoid endogeneity biases in the regression estimation. Econometric models use different performance measures. (Accounting and market-based measures). The results support a dynamic relationship between pay and performance. Executive pay in Islamic banks depends mainly on ROE as a performance measure. The results reveal that independent directors on the board perform a monitoring task, which lessens their reliance on pay to mitigate agency problems. This study confirms the hypothesis that larger IBs and those with high growth opportunities hire talented executives with higher compensation packages. This study provides the first comprehensive empirical study on the pay-performance relationship in Islamic banks through cross-country analysis. These findings contribute to a better understanding of the dynamic connectedness between pay and performance by incorporating the moderating effect of governance.

Keywords: compensation, performance, corporate governance, Islamic bank, GMM.

JEL Classification: G30, M12, G21, C33

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