Electing left-leaning governments reduces CEO pay by almost 6%

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Elections that bring left-leaning, pro-equality political leaders to power significantly lower CEO pay by almost 6% on average, according to new research from Durham University Business School and Sabanci Business School.

Furthermore, when a left-leaning political leader is voted out of power and a non-left-leaning political leader is voted in, CEO pay increases by almost 3% on average.

This research was conducted by Dimitris Petmezas, Professor of Finance at Durham University Business School, alongside Dr Nan Xiong, also Durham University, and Bunyamin Onal, Sabanci Business School, Turkey. The researchers were interested in understanding the impact of various governments ideologies, and their societal equality sentiment, on wider executive compensation.

To do so, the researchers used the Database of Political Institutions (DPI) – a database which provides a classification of all political parties around the world, and their tenure in government – as well as developing a model to identify a shift in ideology from non-left to left, or vice versa, in governments. The study focused on political movements between 2000-2017, in 23 different countries.

The researchers then compared this to data on firm characteristics and executive pay from the Standard & Poor’s Capital IQ database from the same time period. The final sample consists of 64,385 firm-year observations, with 10,942 unique firms.

Through this comparison, the researchers found that, on average, CEO pay drops by almost 6% when a left-leaning government is voted into power, in the year of the election. Yet, when a country moves from a left-leaning government to a non-left leaning government, CEO pay increases on average by almost 3%.

The researchers state that the biggest change is not in CEO base-level pay, but actually in the form of bonuses, which are scrutinised much more heavily when a left-leaning government comes into power.

Professor Dimitris Petmezas says,

“Wealth inequality has been widening and becoming an increasingly greater concern around the world – particularly when it comes to income inequality. Though left and non-left-leaning governments have different approaches to tackling this, our research shows that left-leaning policies, in particular pro-equality sentiment, are more effective in reducing the inequality between employers and their CEOs, and tackling the widening inequalities in their respective countries.”

Dr Nan Xiong states that “this evident shift in CEO pay, caused by wider political ideologies, can happen for two reasons.

Firstly, compensation committees for firms can be influenced by the pro-equality sentiment in the country and therefore look to directly reduce CEO pay.

Secondly, there are significant reputational issues tied to compensation packages of senior executives, given the public's ability to scrutinise CEO pay, as such information must be publicly disclosed. This in turn can force firms to pre-emptively adopt a more equal internal pay structure to avoid any societal backlash."

The researchers state that this paper expands our understanding not just of the real-life impact of government policies and sentiment on businesses, but wider inequalities too. These findings showcase that different political ideologies can have a clear impact on wealth inequalities, and gives food for thought for those who may be having to choose between a left or non-left leaning government in upcoming elections.

This study was published in the Journal of Corporate Finance.

If you would be interested in receiving the full research paper, or speaking to the researchers, please contact Peter Remon at BlueSky Education – peter@bluesky-pr.com +44 (0) 77 235 228 30.