Workers Get Paid More When They Work For Powerful CEOs

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For workers at publicly held companies, it literally pays to have a very powerful boss. A new study found that entrenched CEOs – those who have more control rights in their company than all other shareholders combined -- pay their workers about 6 percent more than do other managers. That equals about $2,200 in higher wages per year for these employees.

“Entrenched CEOs give higher pay, not only to themselves, but also to the firm's other employees, such as its janitors or engineers,” said Henrik Cronqvist, co-author of the study and assistant professor of finance at Ohio State University's Fisher College of Business.

But CEOs who have a larger financial stake in their companies – those who own more stock – actually pay their employees less than do managers who don't own as large a share of the company, the study found.

In this case, the CEO would bear more of the financial cost of paying extra to workers, so wages of workers tend to be lower, Cronqvist said.

Overall, these results show that when companies give too much power to their CEOs, these leaders will act in ways that benefit themselves over the shareholders, Cronqvist said.

“When managers are entrenched, it can cost the company not only in terms of higher wages for the CEO, but for salaries of many other employees as well,” Cronqvist said.

The study is available as a working paper at the Social Science Research Network, among other places.

The study includes data on Swedish employees and firms from 1995 to 2002, all compiled by the government of Sweden . All together, the researchers were able to study 585,311 employees working for 286 public firms. Researchers used this data set because in Sweden , unlike the United States , pay data for workers is a public record available through tax reports.

While other studies have shown that entrenched CEOs tend to pay themselves more, Cronqvist said this is one of the first to show that these powerful CEOs also tend to pay higher wages to other workers in their organizations. This result held up even after they took into account other factors that may affect average wages within a company, such as the education and gender of workers.

Why do entrenched CEOs pay more to their employees?

“We believe these CEOs get a private benefit from paying these workers more, a benefit that other shareholders don't receive,” Cronqvist said.

The major benefit for CEOs would be improved relationships with workers, particularly unionized employees.

“CEOs benefit if they don't have to spend as much time and energy bargaining with employees about their pay,” he said. “If a CEO could afford to pay workers more, just to avoid a major conflict, he or she would probably do that.”

If this is the case, pay for unionized workers should probably increase more than pay for non-unionized workers under a powerful CEO, since union pay negotiations are usually most contentious.

While the data set in this study does not identify unionized vs. non-unionized workers, Cronqvist and his colleagues did compare blue-collar workers – who are more likely to be unionized – to white-collar workers.

And, as expected, blue-workers had a larger average boost in wages (8.8 percent) than did white-collar workers (5.2 percent) under entrenched CEOs.

Another group of employees who should benefit under a powerful CEO would be the top executives of the firm who work directly with the CEO himself. And this study showed that to be true.

The researchers found that a company's top executives, such as the Chief Financial Officer and divisional managers, received 19.7 percent higher pay when they worked for a CEO who had controlling share in the company.

“These are the executives the CEO interacts with the most at work, and who may have relationships with the CEO even outside the office,” Cronqvist said. “That's a good reason why the CEO would pay them particularly well if he could.”

The results of this study show the dangers – from the shareholders' perspective – of giving a CEO too much control within a company.

“CEOs with a lot of power may benefit by paying higher-than-average wages to employees and avoiding conflict with unions, but that is not a benefit to other shareholders,” Cronqvist said. “These other shareholders would say that they hired the CEO to try to hold wages in check.”

That's why CEOs with a larger financial stake in their companies didn't pay workers as much as did corporate leaders who had less share of the profit.

“When you own a larger share of the company, you will work harder to keep costs, like wages, down because that benefits you personally,” he said.

While this research was done in Sweden, Cronqvist said the overall results should apply to public companies worldwide, including those in the United States.

Source: Ohio State University