

Compensation Schemes and Inclination towards Risk-Taking: A Comparative Study of Three Countries

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It has been documented in the literature that, one of the variables affecting management attitude towards risk is the nature of the decision-makers' compensation schemes. In this research we explore this association in three completely different environments: in Bangladesh, Croatia and the USA. We have examined the impact of the tie between decision-makers' compensation schemes to their performances on the degree of risk they incline to take. We have found that the risk behavior is different in the three dissimilar environments. In Bangladesh, the stronger the tie between the decision-makers' compensation schemes and their performances – the greater is their inclination to accepting riskier projects. In contrast, in Croatia we found no such a significant association. In the US there seems to be an optimal degree of tie between compensation and risk-taking, placed somewhere in the middle. Beneath and beyond this mid-level of tie – US decision-makers are less motivated to take the riskier projects. Risk is an integral part of any business and it can act as an important deterrent or motivation for economic development. Stimulating business development requires therefore, to a great extent, willingness for risk taking by the decision-makers. However, at the same time, decision-makers have to be careful not to assume an excessive amount of risk. Overly generous compensation may create incentives for managers to assume excessive amount of risk. This might have contributed to corporate scandals, such as those causing the current global financial crisis. The implication from this study is the recommendation to tie only partially executives' compensation schemes to their performances. It might enhance a country's economic development by encouraging decision-makers to take upon themselves risk, but up to a certain point, and to avoid assuming excessive amount of risk.

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