



## CEO compensation in Australia A global benchmarking study

Ian D. Gow, James P. Kavourakis

21 August 2018

The remuneration of Australia's chief executives (CEOs) remains a highly charged political issue. Adding to Prime Minister Malcolm Turnbull's criticism of a cult of "excessive executive CEO compensation", Australian Labor Party President and ex-Commonwealth Treasurer Wayne Swan MP now claims that CEOs are "gorging themselves" on shareholder funds and calls for higher taxes for firms "overpaying" their executives. This development brings both sides of the Australian political spectrum together in seeking limits on the remuneration of CEOs.

Our earlier *Insights Series* piece "Cult of excess? A global perspective on CEO compensation" sought to provide evidence to inform the debate surrounding executive remuneration. There, we examined the remuneration of Macquarie Group, Commonwealth Bank of Australia, CSL and Woolworths. The examination challenged the conventional wisdom that Australia's CEOs are excessively paid, drawing evidence from the remuneration of global peers whom compete with Australian firms for top managerial talent.

In this piece, we extend our analysis to cover the 200 largest Australian firms, including almost all of the ASX 200 index.<sup>1</sup> As in our earlier analysis, for each firm, we construct a peer group of global firms drawn from the same industry.<sup>2</sup> We then use market capitalisation to identify the five peer firms closest in terms of size.<sup>3</sup> We use fiscal 2017 data throughout and measure compensation as reported in companies' remuneration reports.<sup>4</sup>

### Summary findings

We conduct preliminary analysis by examining remuneration data at the industry level.<sup>5</sup> In Exhibit 1, we find that CEOs in almost all industries receive lower compensation than their global peers. Many major industries exhibit considerable differences between their CEO remuneration and that of peer firms. Depository institutions (0.62), communications firms (0.52), insurance firms (0.49), oil & gas firms (0.52) and healthcare firms (0.34) all exhibit remuneration levels notably lower than global norms.<sup>6</sup> Surprisingly, metals and mining companies also exhibit sub-benchmark remuneration (0.85), despite Australian firms representing some of the largest mining firms in the world.

Collectively, only 47 firms in our sample of 200 exhibit CEO remuneration greater than that of benchmark firms. Figure 1 shows the distribution of relative CEO remuneration by relative firm size. This chart reveals that for firms where well-matched peer groups can be specified, a disproportionate amount of

observations exist below the "proportionate" line depicted, which captures a linear relationship between relative remuneration and relative firm size. We follow with a more in-depth examination of several industries.

### Engineering, Accounting & Management Services

This industry comprises six firms predominantly drawn from mining and construction services and listed in Exhibit 2. The average pay ratio of 0.96 belies variation across the six firms. CEOs at Monadelphous and McMillan Shakespeare are paid much less than their global peers. While, Cardno's CEO was paid slightly less. CEOs of Downer EDI and RCR Tomlinson were paid a bit more than global peers. However, the ratio is pushed very close to one by the pay for the (now former) CEO of Spotless Group, Martin Sheppard. Sheppard received \$4.8 million in remuneration, which is roughly double the pay for the CEOs of the nearly equal-sized peer firms. Much of this compensation related to amendments to option grants awarded under the CEO's long-term incentive plan. Shareholders were not overly happy with Sheppard's compensation, with 34% of shareholders voting down the remuneration report in October 2016, resulting in a "strike on pay" for Spotless.<sup>7</sup> Spotless is now 88 percent owned by Downer EDI, and compensation for the new CEO (\$1,866,000) falls below that of the peer group.

### Metals and Mining

Firms in Metals and Mining are shown in Exhibit 3, which provides mixed evidence. Larger Australian mining firms appear to pay their CEOs relatively less, while smaller miners provide remuneration at a premium compared to global benchmarks.

First, we consider larger firms with market values over \$1.0 billion. In 2017, Andrew Mackenzie of BHP received \$5.9 million compared to \$11.7 million for a peer group approximately one-third the size – a difference unlikely to be explained by the relatively lower stock returns of BHP.<sup>8</sup> Similarly, CEOs such as Bill Beament (Northern Star Resources), Mark Clark (Regis Resources) and Shane Stephan (New Hope Corp) are paid less, and this cannot be explained by differences in firm size or performance.

Other larger mining firms pay closer to global benchmarks. Nev Power (Fortescue) and Sandeep Biswas (Newcrest) were paid \$7.5 million and \$8.7 million respectively. Despite notional discounts in remuneration for these CEOs, it is likely these differences can be explained by the relatively smaller size of the Australian firms and

lower stock returns during the year.

Second, we consider the relative remuneration of the CEOs of smaller mining firms. Of the 11 firms in our sample with market values lower than \$1.0 billion, 10 have markedly higher compensation than that of benchmark firms. More significant cases are those of Saracen Minerals CEO Raleigh Finlayson, paid \$2.7 million against the \$596,000 of peers, and Pilbara Minerals CEO Ken Brinsden, paid \$3.3 million against \$879,000.

## Healthcare

Data on firms in the healthcare industry are shown in Exhibit 4. Without exception, the Australian CEOs appear to receive lower levels of compensation than the apparent global market rate. This theme is consistent for all seven of the healthcare firms in our sample.

The magnitude of the discount in CEO remuneration is substantial. Across the sample of healthcare companies, we find that the remuneration of Australian CEOs is approximately one-third that of foreign peers. For example, Sonic Healthcare CEO Colin Goldschmidt MD was remunerated with \$5.8 million, compared to some \$14.6 million for peer firms, despite the Australian firm having superior operating and stock performance in 2017. Similarly, CEO of hospital provider Healthscope, Robert Cooke received \$2.7 million compared to a benchmark of \$10.1 million. While these are the larger companies in the Australian market, their relative pay is representative of that of the industry.

## Communications, Television and Radio

Firms involved in communications, including television and radio broadcasting, are shown in Exhibit 5. Our results are consistent with those documented for the industries discussed above. Of six firms, only Nine Entertainment Co. provides compensation commensurate with the global industry. The five remaining firms all provide markedly lower levels of pay to their CEOs.

## Insights

Most of Australia's largest public companies pay their CEOs less than comparable global firms pay their CEOs. This evidence is consistent with the findings of our earlier *Insights Series* piece "Cult of excess? A global perspective on CEO compensation", where we focused on CEOs of four prominent firms.

Only 24% of Australian firms are paying their CEOs at or above the levels of their global peers. We find evidence that mining firms may provide remuneration in excess of that suggested by global peer firms. Given Australia's prominent position in mining, one possible explanation is that these firms need to attract managerial talent of the highest calibre drawn from a smaller pool of candidates with the needed specialised expertise.

We caution that our findings do not necessarily imply that Australian CEOs are "underpaid" or represent "good value" for their firms. Such a conclusion would require evidence on the value provided by these CEOs. One possible alternative explanation is simply that CEOs elsewhere are overpaid. Another explanation is that many Australian firms are not competing in a global market for CEO talent and local market conditions can therefore depart from global benchmarks. This is consistent with findings from our earlier *Insights Series* piece "CEO talent: Where do Australia's CEOs

come from?" There we found that few CEOs in Australia are recruited from abroad. Further research is needed to understand whether CEO pay levels are optimal for Australian firms.

---

Professor **Ian Gow** is Director of the Melbourne Centre for Corporate Governance and Regulation (MCCGR). **James Kavourakis** is a doctoral candidate in the Department of Accounting, Faculty of Business and Economics.

# Exhibits

## Exhibit 1: Relative executive pay by industry

CEO pay for fiscal 2017 (in thousands of Australian dollars). Market capitalization in millions of Australian dollars.

Industry	Number of Firms	CEO Pay	Peer Pay	Relative Pay	Relative Market Capitalisation
Engineering & Accounting & Management	6	2,209	2,303	0.96	1.04
Food & Kindred Products Mfrs	4	1,269	1,439	0.88	1.02
Real Estate	6	2,372	2,742	0.87	0.75
Metal Mining	19	2,579	3,038	0.85	1.30
Wholesale Trade & Durable Goods	4	4,103	5,193	0.79	0.96
Non-Depository Credit Institutions	3	2,068	3,118	0.66	0.89
Measuring & Analysing Instruments-Mfrs	4	2,695	4,288	0.63	0.98
Transportation Services	6	2,520	4,027	0.63	1.57
Depository Institutions	6	5,023	8,130	0.62	1.00
Electric Gas & Sanitary Services	7	3,332	5,457	0.61	0.94
Security & Commodity Brokers	12	2,165	3,905	0.55	0.95
Holding & Other Investment Offices	21	2,188	4,002	0.55	1.01
Other	41	3,315	6,258	0.53	0.35
Communications	6	2,814	5,411	0.52	1.05
Oil & Gas Extraction	4	2,049	3,966	0.52	1.01
Insurance Carriers	3	3,323	6,833	0.49	1.00
Insurance Agents Brokers & Service	4	1,096	2,315	0.47	0.67
Business Services	16	1,919	4,160	0.46	1.00
Amusement & Recreation Services	5	3,187	7,116	0.45	1.03
Automotive Dealers & Service Stations	4	1,306	2,978	0.44	0.95
Chemicals & Allied Products Mfrs	12	2,977	7,358	0.40	1.02
Health Services	7	2,048	5,977	0.34	1.03

## Exhibit 2: Engineering, accounting and management services

CEO pay for fiscal 2017 (in thousands of Australian dollars). Market capitalization in millions of Australian dollars.

Ticker	Name	CEO Pay	Peer Pay	Market Capitalisation	Peer Market Capitalisation
DOW	DOWNER EDI LTD	3,770	3,429	3,812	3,605
MND	MONADELPHOUS GROUP LTD	1,005	2,448	1,314	1,186
SPO	SPOTLESS GROUP LTD	4,758	2,448	1,263	1,186
MMS	MCMILLAN SHAKESPEARE LTD	907	2,448	1,115	1,186
CDD	CARDNO LTD	1,166	1,824	585	600
RCR	RCR TOMLINSON LTD	1,646	1,220	477	478

## Exhibit 3: Metals and Mining

CEO pay for fiscal 2017 (in thousands of Australian dollars). Market capitalization in millions of Australian dollars.

Ticker	Name	CEO Pay	Peer Pay	Market Capitalisation	Peer Market Capitalisation
BHP	BHP BILLITON GROUP (AUS)	5,937	11,743	74,768	25,954
FMG	FORTESCUE METAL GROUP	7,470	11,743	16,254	25,954
NCM	NEWCREST MINING LTD	8,660	11,743	15,465	25,954
EVN	EVOLUTION MINING LTD	2,832	2,042	4,056	3,379
NST	NTHN STAR RES LTD	1,961	3,228	2,853	2,588
RRL	REGIS RESOURCES NL	1,876	3,782	1,894	2,166
IGO	INDEPENDENCE GROUP NL	1,501	3,628	1,848	1,919
NHC	NEW HOPE CORP LTD	1,613	5,298	1,330	740
SAR	SARACEN MINERAL HOLDINGS	2,690	596	948	1,201
SFR	SANDFIRE RESOURCES	1,949	560	892	932
RSG	RESOLUTE MINING LTD	2,004	560	877	932
ORE	OROCOBRE LTD	1,232	703	731	746
GOR	GOLD ROAD RESOURCES LTD	1,111	879	584	556
WSA	WESTERN AREAS LTD	1,950	879	575	556
ASL	AUSDRILL LTD	804	879	573	556
WGX	WESTGOLD RESOURCES LTD	1,295	879	563	556
PLS	PILBARA MINERALS LTD	3,312	879	557	556
MLX	METALS X LTD	1,304	1,001	408	380
DCN	DACIAN GOLD LTD	1,642	1,001	399	380

#### Exhibit 4: Healthcare

CEO pay for fiscal 2017 (in thousands of Australian dollars). Market capitalization in millions of Australian dollars.

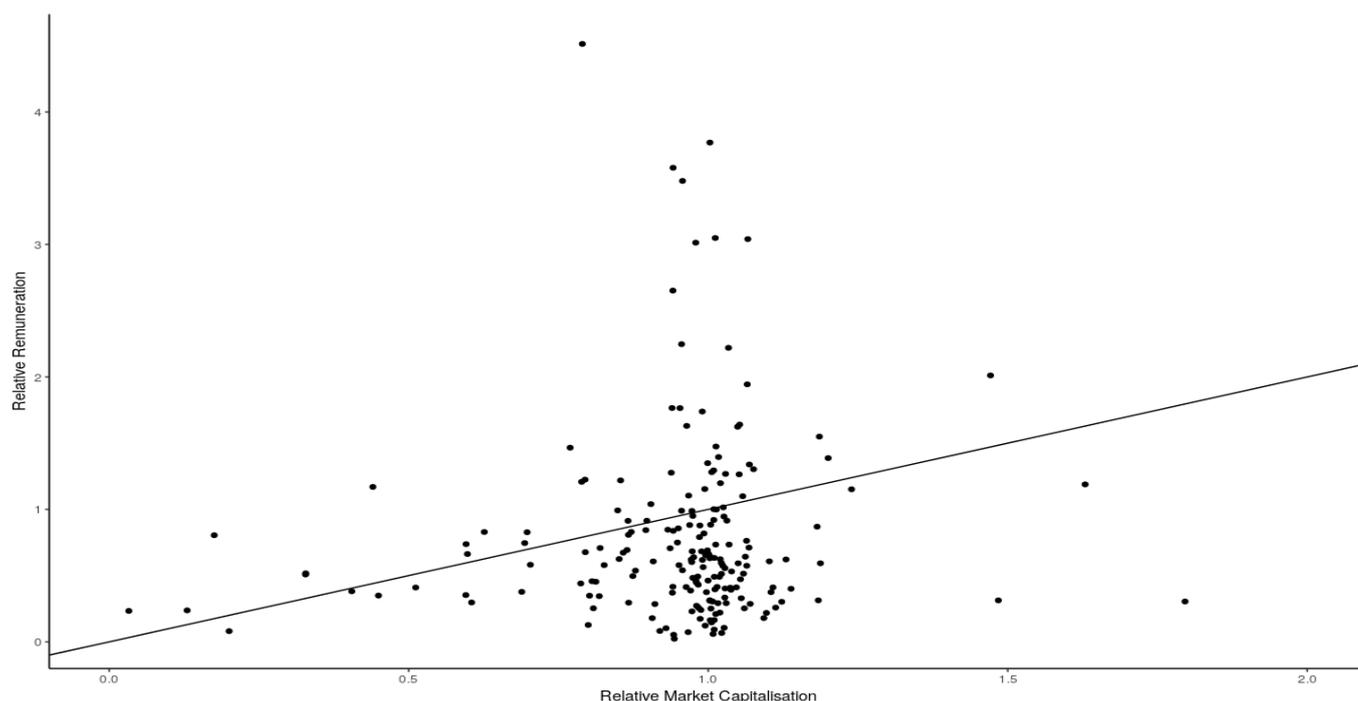
Ticker	Name	CEO Pay	Peer Pay	Market Capitalisation	Peer Market Capitalisation
SHL	SONIC HEALTHCARE LTD	5,841	14,633	10,153	9,043
HSO	HEALTHSCOPE LTD	2,709	10,065	3,837	3,953
PRY	PRIMARY HEALTH CARE LTD	2,556	3,828	1,898	2,090
REG	REGIS HEALTHCARE LTD	1,001	5,592	1,180	1,302
EHE	ESTIA HEALTH LTD	757	4,242	795	773
JHC	JAPARA HEALTHCARE LTD	932	1,344	558	645
VRT	VIRTUS HEALTH LTD	540	2,133	432	535

#### Exhibit 5: Communications, Television and Radio

CEO pay for fiscal 2017 (in thousands of Australian dollars). Market capitalization in millions of Australian dollars.

Ticker	Name	CEO Pay	Peer Pay	Market Capitalisation	Peer Market Capitalisation
TLS	TELSTRA CORP LTD	5,660	10,999	51,141	48,298
TPM	TPG TELECOM LTD	3,363	5,408	5,188	4,591
SVW	SEVEN GROUP HLDS LTD	1,932	6,776	3,449 t	3,786
NEC	NINE ENTERTAINMENT CO HLDGS	3,199	3,224	1,202	1,417
SXL	SOUTHERN CROSS MEDIA GROUP	2,221	3,122	957	896
SLC	SUPERLOOP LTD	510	2,939	535	542

**Figure 1: Relative Remuneration vs. Relative Size<sup>9</sup>**



<sup>1</sup> We deem Rio Tinto to be a non-Australian firm, as it is headquartered in the United Kingdom. We also exclude a number of other firms with insufficient data available for our examination, or firms that operate as investment funds without a defined chief executive officer or managing director. These firms are replaced in the sample, yielding a sample of 200 firms with both the highest market capitalisation and data available. This sample is reflective of the S&P/ASX 200.

<sup>2</sup> Industries are determined by two-digit Standard Industry Classification (SIC) codes.

<sup>3</sup> We use the logarithm of market capitalization so that a firm that is half the size is considered as close a match as a firm that is twice the size.

<sup>4</sup> Comparing compensation across jurisdictions is not without challenges, but we use the numbers that are most comparable and believe that these numbers are sufficiently comparable for this exercise to be worthwhile. An alternative measure of pay would be based on “realized” compensation, we focus on expected pay for comparability and because for measuring quantum of pay, expected pay has merits. Note that reported pay often mixes elements of expected and realized pay.

<sup>5</sup> Our data have the following sources. Firm financial and stock price data from Compustat and the Center for Research into Security Prices (CRSP). Compensation data from Morningstar/SIRCA (Australia), Execucomp (US) and Boardex (rest of world). We use the total value of compensation reported in the summary compensation tables of the firm. This pay includes the fair values at grant date of equity-based compensation. An alternate measure for US peers would be the use of total direct compensation. Reproducing our analysis using this form of compensation for US peers yields qualitatively similar insights, with all industries except Metals and Mining providing lower-than-benchmark levels of pay.

<sup>6</sup> Reflects the ratio of Australian firm CEO remuneration to the average CEO remuneration of the size-matched peer firms.

<sup>7</sup> The option grants received by Martin Sheppard were granted in November 2016 in connection with appointment in 2015, and thus were likely to be considered by shareholders in voting at the 2016 AGM.

<sup>8</sup> BHP’s remuneration in this sample is based on their UK single figure remuneration. An alternative measure of pay using Australian standards puts BHP’s remuneration at US\$7,092, or A\$9,246, below the peer benchmark of A\$11,743.

<sup>9</sup> Figure 1 excludes two firms with relative market capitalisation greater than 2.0 times the peer group.