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Bachelor thesis

Bank executive incentive schemes prior to the Financial Crisis of 2008 and their optimisation for the future

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Matriculation no. : 11-740-594

Field of Study: Banking and Finance

Number of semesters: 8

Academic advisor:

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Submitted:

Executive Summary

Presentation of the Problem

Since the beginning of the international Financial Crisis in 2008, bank executives were described in the media as irresponsible, greedy and even incompetent. They were and still are accused of excessive risk-taking, which is considered by the public as one of many causes of the financial meltdown, which began seven years ago.

Thereby, public pressure was put on banks to restructure their compensation plans and to review the incentive schemes, which these compensation systems are based on. In fact, wrong incentives provided by financial institutions were considered as one cause of executives' misbehaviour.

The main purpose of the present dissertation is the identification of differences between compensation plans before and after the financial crisis. Additionally, the measures taken by banks to improve their compensation systems are analysed and solutions to potential problems are provided.

Approach

First of all, the reader will be given an overview of the current academic literature in relation to executive compensation. In other words, the question, if executive incentives provided by compensation systems can be considered as a direct cause of the crisis, is going to be treated.

Furthermore, the evolution of executive compensation plans within the Swiss financial sector during the period of 2007 until 2008 is analysed. This evolution is going to be illustrated with the compensation systems of the following four Swiss banks: UBS, Credit Suisse, Raiffeisen, Alternative Bank Schweiz. Thereby compensation plans for each year and for each of the banks mentioned above are going to be explained. Positive and negative aspects of these systems are going to be identified. Additionally, the analysis does not only focus on financial but also on non-financial or qualitative criteria used by compensation committees in order to determine variable compensation. The information analysed in this section is provided by official reports published by the four banks themselves.

Moreover, possible solutions to the problems identified in the previous section are described. In addition to that, measures recommended by academic literature and by the Swiss Financial Market Authority, which were already implemented after 2008 are also described.