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Time for Change: Rethinking Top Managers' Bonus Systems for A Sustainable and Prosperous Future

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Abstract

This opinion paper explores the negative consequences of short-termism in western corporations and the influence of short-term oriented political systems on the business world. It highlights the need for a paradigm shift towards long-term orientation and sustainable growth, focusing on four key areas: redesigning bonus systems, encouraging a culture of long-term thinking, fostering transparency and accountability, and engaging shareholders in long-term discussions. Through practical examples, the paper demonstrates how businesses can effectively implement these strategies to promote long-term value creation, ensuring their long-term success and contributing to a more sustainable and resilient global economy.

Keywords: Short-term Orientation; Bonuses; Performance Evaluation System; HR; Long-term Orientation

Introduction

In today's fast-paced business environment, there is an urgent need to shift focus from short-term gains to long-term strategies. The study I recently published revealed a stark disconnect between top managers' understanding of long-term orientation's benefits and their inclination to prioritize short-term rewards. As someone deeply concerned about the future of businesses and their impact on society, I believe it's high time we revise the bonus systems for top managers in western corporations. This change would encourage a long-term perspective and ensure more sustainable and responsible business practices.

The Short-termism Problem

Short-termism in western corporations is not only harmful to the long-term sustainability of businesses but also detrimental to society and the environment [1]. Managers who prioritize their personal gains, such as annual bonuses, often make decisions that may yield immediate results but compromise long-term value creation. This approach creates a vicious cycle where businesses struggle to adapt to changing market conditions, leading to suboptimal performance and, ultimately, failure. The problem of short-termism is further exacerbated by the political systems in western democracies, which are inherently short-term oriented due to their electoral cycles [2]. Elections are often held every four years, which encourages politicians to focus on achieving results within their term in office to secure re-election. This short-term focus leads to a preference for quick wins and policies that produce visible results within a few years, at the expense of long-term strategies and investments.

Long-term goals that require investment today but will only yield results in the future are not popular among politicians, as they entail budgetary expenditures that may appear negative during their tenure. The positive outcomes of such investments may only materialize when the opposition, or at least not the initiating politician, is in power. Consequently, subsidies and government programs are naturally short-term oriented, favoring projects with immediate benefits over those that contribute to long-term progress. This short-term mindset permeates the business world as well, as companies often align their strategies with government policies and subsidies. The pressure to deliver short-term results also comes from shareholders and investors who demand rapid returns on their investments. This environment leads to businesses adopting short-term strategies, with top managers incentivized to prioritize their personal gains over the long-term success of their organizations as a study of Gerlich [3] shows.

It is crucial for both businesses and governments to recognize the systemic nature of short-termism and work towards fostering a culture of long-term thinking. Political systems must evolve to incentivize long-term policies and investments that address societal and environmental challenges, such as climate change, income inequality, and infrastructure development. This shift will require reevaluating electoral cycles and political incentives to encourage politicians to focus on the long-term well-being of their constituencies.

In the business world, a change in incentives and bonus structures for top managers is needed to promote long-term strategies and sustainable growth [4]. This change must be accompanied by a shift in shareholder expectations and investment practices that prioritize long-term value creation over short-term gains. By adopting a long-term perspective, both governments and businesses can work together to build a more sustainable and equitable future for all.

Addressing the shortcomings of the current bonus system for top managers in western corporations is essential to ensure that managers' incentives align with the long-term interests of shareholders, employees, and society at large. Short-term thinking, which is often promoted by the current bonus systems, can lead to a lack of innovation, insufficient investments in research and development, and a disregard for the potential impact on the environment and society.

To counteract these detrimental effects, corporations must shift their focus towards long-term performance, cultivating a more sustainable and forward-looking approach to business management. One way to achieve this is by redesigning bonus systems to reward long-term achievements and incorporating non-financial measures such as environmental, social, and governance (ESG) criteria.

A strong corporate culture that values patience, commitment, and responsible decision-making is also key to achieving long-term success. By investing in training and development programs that emphasize long-term planning and sustainable growth, organizations can empower employees and managers to adopt a long-term perspective. This cultural shift can lead to better strategic decision-making, improved risk management, and a more robust and resilient organization.

Building trust and commitment among stakeholders is essential for a successful transition to long-term thinking. Managers who communicate their long-term strategies clearly and consistently to all stakeholders, including employees and shareholders, foster a sense of trust and commitment. This transparency ensures that everyone is working towards the same long-term objectives, fostering an environment of collaboration and accountability.

Lastly, actively engaging shareholders in discussions about long-term strategies and their benefits is crucial. By involving shareholders in these conversations, businesses can create a shared understanding and commitment to long-term value creation. This engagement can contribute to a more sustainable and resilient global economy at large.

The Necessity for Change

I strongly believe that the current bonus system is fundamentally flawed, as it incentivizes short-term thinking and undermines the overall sustainability of businesses. This system needs an overhaul to align managers' incentives with the long-term interests of shareholders, employees, and society at large.

To achieve this alignment, organizations should:

i. Redesign bonus systems to reward long-term performance: Companies must move away from annual bonus schemes and instead adopt performance metrics that reflect long-term goals, such as multi-year performance targets, environmental, social, and governance (ESG) criteria, and other non-financial measures.

ii. Encourage a culture of long-term thinking: A cultural shift is needed where businesses value patience, commitment to long-term objectives, and responsible decision-making. Organizations should invest in training and development programs that emphasize the importance of long-term planning and sustainable growth.

iii. Foster transparency and accountability: Managers must communicate long-term strategies clearly to all stakeholders, including employees and shareholders. This transparency helps build trust and ensures that everyone is working towards the same long-term objectives.

iv. Engage shareholders in long-term discussions: It is crucial to involve shareholders in conversations about long-term strategies and their benefits. By actively engaging shareholders in these discussions, businesses can create a shared understanding and commitment to long-term value creation.

Our current short-term focus in western societies and corporations significantly hinders our ability to tackle pressing global problems like climate change. By embracing a long-term orientation, businesses can contribute to sustainable development and help build a better future for all. The four steps outlined earlier provide a roadmap for corporations to address the short-term orientation problem within their performance management systems, motivating the adoption of urgently needed long-term strategies.

Breaking away from short-termism is critical in addressing complex issues that require long-term planning and commitment. Climate change, for instance, demands concerted efforts from businesses, governments, and individuals to transition to a low-carbon economy, invest in clean technologies, and develop innovative solutions. Short-term goals, while important in maintaining operational efficiency, cannot fully capture the essence of these long-term challenges.

Implementing long-term strategies requires overcoming the obstacle of breaking them down into manageable short-term goals that can be monitored effectively. This process may involve revisiting existing performance measurement tools and developing new ones that capture the long-term value creation while providing actionable insights for the short term. Organizations can leverage emerging technologies, such as data analytics and artificial in-

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telligence, to identify patterns, trends, and correlations that may not be immediately apparent, thus enabling more informed decision-making.

Furthermore, the transition to long-term orientation should be a collective effort that transcends organizational boundaries. Policymakers, investors, and consumers also have a role to play in fostering a long-term mindset. For instance, governments can introduce regulations and incentives that encourage businesses to prioritize long-term sustainability, while investors can shift their focus from short-term gains to long-term value creation. Consumers, on the other hand, can drive change by supporting companies that demonstrate a commitment to sustainability and long-term growth.

Conclusion

The current bonus systems for top managers in western corporations are a significant hindrance to the adoption of long-term orientation strategies. It is my firm belief that revising these systems to incentivize and reward long-term thinking will drive a cultural shift towards sustainable business practices. The responsibility lies with organizations, shareholders, and regulators to work together and create a future where businesses thrive responsibly and contribute positively to society and the environment.

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