Are ESOPs still a fable?

By *Hadi Hayek* and *Sonja Petrovic-Lazarevic.*

In our post Marxist world, few things put the fire under the worker better than self interest, a fact well known to corporate productivity Tsars and their bean counters. Spear heading this has been the promise of the mutual benefit and subsequent improved organisational performance offered by Employee Share Ownership Programs (ESOPs). For many Australian public companies ESOPs are now as much a part of the furniture as the board room table but a recent report into the link between ESOPs and financial performance may have some boards reconsidering their use.

As defined by Fiore, ESOPs are employee contribution schemes, primarily in company stock, providing benefits to both the company and participating employees. ESOPs are unique reward systems. Such systems endeavour to motivate employees, increase participation and enhance productivity to improve organisational competitive advantage. In other words, they tie employee income and wealth to company performance.

Their popularity has grown steadily in Australia since favourable legislative changes in 1974, but according to an Australian Government publication Shared Endeavours, the employee ownership scheme is still at an early developmental stage in this country. The plan is that by tying employee income and wealth to company performance you can decrease employee-management conflicts and encourage general productivity. Well that's the plan. But the question begs, do Australian firms with higher employee share ownership plan participation rates exhibit improved financial performance as measured by common accounting ratios?

Our study analysed 507 annual reports of companies listed on the Australian Stock Exchange in the 2001-2002 financial year. Of the 71 organisations disclosing employee share holdings, 60 contained complete and useable data. By focusing solely on financial measures as a means of evaluating organisational performance, the findings disputed the accepted notion that the cosy alignment of employee and management objectives result in better organisational performance. The study indicates that in many cases, lower ESOP participation actually means higher profitability, share price and investor ratios. Furthermore it found no clear causal relationship between ESOPs and individual employee behaviour.

> Companies with lower ESOP participation rates have better organisational performance across many financial areas.

It was found that companies with lower ESOP participation rates have better organisational performance across many financial areas and exhibit higher profitability and superior share related performance. This obviously contradicts existing literature and with the trend towards increased employee ownership the findings are of particular importance. It is also apparent that at lower levels ESOPs are linked to highly efficient and financially successful firms, thus implying that employee ownership can play a role in but not entirely influence organisational performance. The full paper can be read at **www.gbata.com.**

Hadi Hayek Hons, Mgt, Mkt, Monash University is currently working as a Marketing Co-Ordinator and Estimator for Smorgon Steel Distribution in Melbourne Australia. His research interests are in: employee share ownership, motivation and participation; reward systems and organisational performance. **hhayek@smorgonsteel.com.au**

Sonja Petrovic-Lazarevic PhD, MA, BA, University of Belgrade is an Associate Professor in the Department of Management Monash University. Her research interests are in: strategic management; corporate governance; organisational culture; supply chain management; business ethics, fuzzy logic and neural network modelling. **Sonja.Petrovic-Lazarevic@buseco.monash.edu.au**