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The Crystal Report on Executive Compensation



**Billionaires Are Good Buys for Shareholders
Equilar Releases New Study
Citigroup Grants Some Stock Options**

by Graef Crystal

November 9, 2009

(Note to readers: As the headlines imply, this article comes in three parts.)

Billionaire CEOs

Billionaire CEOs possess, for the most part, two traits that any shareholder would find immensely appealing: They work for a lot less, and they perform better than non-billionaires.

Those conclusions came from studying 14 billionaires (counting the current value of their shareholdings, as well as the outstanding value of their options and free shares as of the end of their company's fiscal 2008). They were among a group of 356 companies I studied, all of which had market caps of \$5 billion or more as of last spring.

Total Pay Below Market

I first calculated each billionaire's total pay in 2008, which consisted of the sum of: 1)base salary; 2)annual bonus; 3)the grant date fair value of options and free shares granted in 2008; 4)the "target" value of other long-term incentives contingently awarded in 2008; 5)pension accruals; 6)deferred compensation; and 7)miscellaneous compensation.

The best buy among the 14 was Steve Jobs of Apple. He took just \$1 for the entire year.

The second-best buy was Warren Buffett of Berkshire Hathaway. His total pay was only \$175,000.

On the other end of the spectrum, we have Larry Ellison of Oracle, with total pay of \$61 million. (He recently agreed to cut his base salary to \$1 a year) and Rupert Murdoch of News Corp., with total pay of \$30 million.

The pay of each of these CEO was compared to the pay of 342 other CEOs, all running companies with market caps of \$5 billion or more, as of around this past May.

In analyzing the pay of these 356 CEOs, I found I could explain 19 percent of the variation in their pay packages by taking account of the size of their companies (as measured by 2008 sales) and the risk in their pay packages (as measured by the ratio of option present value to total pay, options being generally considered the most risky form of pay).

After taking account of these two factors, all but three of the 14 billionaires were found to be earning below their “market” rates. The median billionaire turned out to be sitting 75 percent below the market.

Herewith a table showing for each of the 14 billionaires, his total pay and the percentage by which that total pay was higher (or lower) than the “market” rate obtained from my multiple regression analysis.

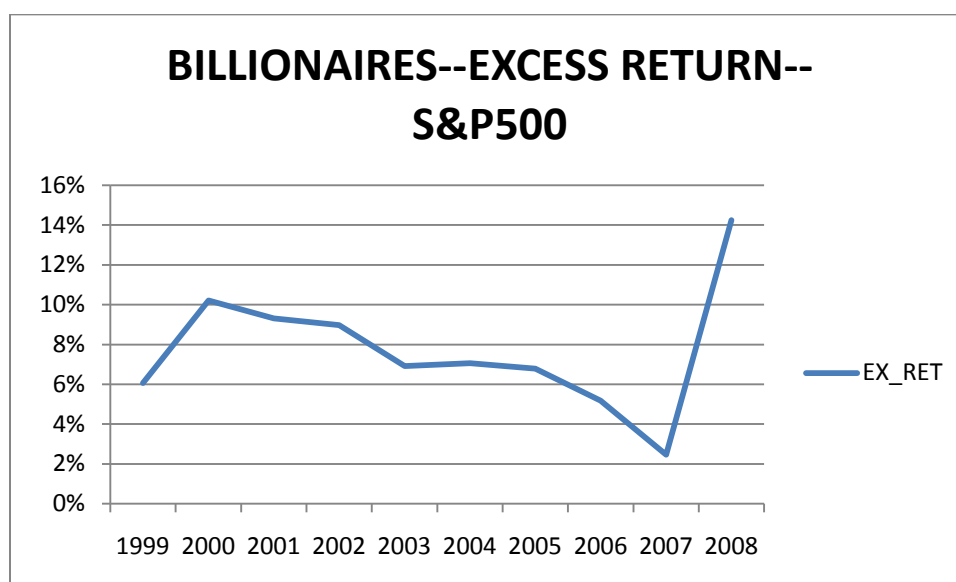
COMPANY	CEO	TOTAL PAY (millions)	ABOVE/ (BELOW) MARKET
ORACLE CORP.	ELLISON, LAWRENCE	\$60.9	233%
NEWS CORP	MURDOCH, RUPERT	\$29.9	122%
HESS CORP	HESS, JOHN	\$27.9	70%
MARRIOTT INTL	MARRIOTT, WILLARD	\$7.5	-48%
CARNIVAL CORP	ARISON, MICKY	\$4.9	-56%
SCHWAB CHARLES	SCHWAB, CHARLES	\$3.4	-60%
ARCELORMITTAL	MITTAL, LAKSHMI	\$6.0	-74%
SIMON PROP. GROUP	SIMON, DAVID	\$1.8	-76%
LAS VEGAS SANDS	ADELSON, SHELDON	\$1.3	-84%
AMAZON.COM	BEZOS, JEFFREY	\$1.3	-89%
MICROSOFT	BALLMER, STEVEN	\$1.4	-92%
GOOGLE	SCHMIDT, ERIC	\$0.5	-96%
BERKSHIRE HATH.	BUFFETT, WARREN	\$0.2	-99%
APPLE	JOBS, STEVEN	\$0.0	-100%

Higher-Than-Expected Performance

Turning to performance, I examined 10 different time windows of total return performance, stretching from a single year all the way to 10 years. The widest window began on Oct. 30, 1999. The start of each additional time window was advanced one year beyond the immediately-earlier time window, i.e., Oct. 30, 2000, Oct. 30, 2001, etc. All time windows ended on Oct. 30, 2009.

From each company's total return in a time window, I deducted the comparable return on the Standard & Poors 500 Index to create a so-called "excess return" series.

The results can be seen in the following chart, which is based on the medians of the 14-company group.



As can be seen, there was no time window where the median company failed to surpass the S&P 500. For all 10 time windows, the median excess return was 7.0 percentage points.

Of course, it should not be surprising that our billionaires would do so well, performance-wise. If they had not done so, some of them might not today be billionaires.

Still, I am heartened that, as a group, these very rich folks are demonstrating a strong degree of self-discipline.

They are to be applauded.

Equilar's New Stock Ownership Study

As this article was being written, I received a 38-page report from Equilar on a parallel subject, namely, the prevalence of stock ownership guidelines for senior executives.

Ownership guidelines are alive and well, despite the recent market crash. Fully 82 percent of the *Fortune* 250 companies have imposed them on their CEOs and other senior executives.

Looking back over my long career, a significant change in perspective has occurred. When I first started in the executive compensation field in the 1960s, no company that I knew of had ownership guidelines. Their attitude: You do whatever you want with your shares. Indeed, some companies wondered aloud that if they required their senior executives to hold shares and then the market tanked, they might have an ethical, and maybe even a legal, responsibility to make the executives whole.

These days, all the talk is about the risk in pay packages and how to lower it. Ownership guidelines can play a key role in this regard, and for two reasons:

- Holding shares binds shareholder interests and executive interests more closely together. In the old days when you didn't hold any shares and had lots of stock options, you only gained on the upside. If the stock sagged, you could sit comfortably on your large ship, sip a cooling drink and watch the shareholders' lifeboats sink beneath the waves. (You did, of course, suffer an economic penalty, in that your options became worthless.) But if you own shares, you're going down with them. That, in turn, will, in theory, make you less willing to bet the farm.
- The more shares you own, the less diversified you become. With less diversification comes a lesser appetite for taking risk.

Still, there is no panacea here. It is worth remembering that two CEOs who were painted as villains in the recent Wall Street crash – Dick Fuld of Lehman Brothers Holdings and Jimmy Cayne of Bear Stearns Companies – held enormous numbers of shares – to the point where each of them personally lost about \$1 billion. Somehow all those shares failed to insulate their shareholders.

If you'd like to request a copy of Equilar's new report, please click on the following link: http://www.equilar.com/Executive_Compensation_2009_ESOG_Report.php.

Citigroup Grants Stock Options

Just as dreaded, loaded-with-risk stock options were about to be interred for financial firms comes Citigroup, which is going to issue several million option shares to the 75,000 employees below the Top 100 – the very employees that Ken Feinberg's bony talons cannot reach.

The plan is to offer one stock option share for each unvested free share granted at an earlier time.

The purpose is to provide some motivational juice and to offer a bit of hope for the future.

Not everyone is happy about this move – leave aside Ken Feinberg. Paul Hodgson, a senior compensation analyst at The Corporate Library was quoted in *The New York Times* on Nov. 7 as saying: “With stock options, you can make a lot of money if the stock goes up, but you are not losing anything if it fails.”

I cannot agree with that reasoning. Citigroup had available to it many ways to spend the money. It could have raised salaries a bit. Or it could have souped up bonuses a bit. While it is true that an underwater stock option offers no value, there is still a loss to the employee compared to what he might have had in other forms of compensation.

For my part, I have always been a stock option fan, although I would like to see the terms of most option grants modified to provide true long-term incentives and to take away the ability of the optionee to call the timing of the exercise.

That options may have peeked their heads out of Ken Feinberg’s deep freezer is, for me, good news.

The compensation data used in this article were obtained from Equilar Inc., a leading provider of executive compensation information. Please click here to go to Equilar:

<http://www.equilar.com>

2009 marks Graef Crystal’s 50th anniversary in the executive compensation field. He has been a director of compensation for General Dynamics and Pfizer, worked as a consultant for Booz, Allen & Hamilton, served as worldwide practice director at Towers Perrin for 18 years, was a professor at the University of California at Berkeley’s Haas School of Business for 10 years and a syndicated columnist for Bloomberg News for almost nine years. He has written six books and more than 1,600 articles on executive pay.