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Ascertaining the effects of employee bonus plans

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Abstract

The effect of employee bonus plans may be difficult to ascertain empirically if the size of bonus is not large enough in magnitude compared to base salary. This study makes use of data from Taiwan where employee bonus payments are not only mandated by law but are quite often several times a typical employee's annual base salary. The use of this unique data allows one to empirically observe interesting relationships difficult to ascertain from traditional datasets. Evidence is found that the performance of bonus-paying firms is related to the size of bonuses paid, both before and after analysis, and across industries. In general, evidence seems to indicate that bonus-paying firms tend to achieve higher productivity, better cost control and asset utilization, and share price returns. However, there may be evidence that marginal returns to employee bonuses are decreasing, reflecting the use of bonuses as substitutes for cash pay in order to attract employees in short supply. These results can serve as useful benchmarks for future studies.

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