The Role of Financial Distress in Moderating The Relationship Between Financial Leverage and Key Management Compensation in Consumer Cyclical Sector

(*Peran Financial Distress dalam Memoderasi Hubungan Antara Financial Leverage dan Kompensasi Manajemen Utama di Sektor Siklus Konsumen*)

Ginaris Prio Utomo*, Afandi Ukik Wahyu Bintang Maulana, Ahmad Rizki Sridadi
Fakultas Ekonomi dan Bisnis, Universitas Airlangga
Surabaya, Jawa Timur, Indonesia
Email: ginaris.prio.utomo-2023@feb.unair.ac.id

Abstrak

Penelitian ini menyelidiki pengaruh leverage keuangan terhadap kompensasi eksekutif puncak dan bagaimana kesulitan keuangan memediasi hubungan ini. Metode kuantitatif dengan analisis regresi berganda dan termoderasi diterapkan untuk menguji hipotesis menggunakan data 24 perusahaan siklus konsumen yang terdaftar di Bursa Efek Indonesia dari tahun 2018 hingga 2022. Hasilnya menunjukkan bahwa leverage keuangan secara signifikan dan positif memengaruhi kompensasi manajemen kunci, dan dengan demikian, tingkat utang yang lebih tinggi mengarah pada kompensasi yang lebih tinggi bagi manajer. Hasilnya juga menunjukkan bahwa kesulitan keuangan secara signifikan memoderasi hubungan ini, yang secara negatif mempengaruhi hubungan kompensasi eksekutif dan leverage. Moderasi ini menunjukkan bahwa dalam kesulitan keuangan, perusahaan mungkin mengurangi kompensasi manajemen sebagai respons terhadap peningkatan risiko yang terkait dengan leverage yang tinggi. Temuan ini memberikan wawasan berharga tentang struktur modal dan strategi kompensasi, terutama dalam konteks keuangan yang berbeda, dan memberikan rekomendasi praktis bagi para pemimpin perusahaan dalam merancang gaji eksekutif.

Kata Kunci: Leverage keuangan, Kesulitan keuangan, Kompensasi manajemen kunci, Struktur modal, Efek moderasi.

Abstract

This research investigates the effect of financial leverage on the compensation of top executives and how financial distress mediates this relationship. A quantitative method with multiple and moderated regression analyses was applied to test the hypothesis using the data of 24 consumer cyclical companies listed in the Indonesia Stock Exchange from 2018 to 2022. The results indicate that financial leverage significantly and positively influences the key management compensation, and thus, the higher levels of debt leads to higher compensation for managers. The results also show that financial distress significantly moderates this relation, which negatively affects the linkage of executive compensations and leverage. This moderation suggests that in financial distress, firms might cut down on management compensation as a response to the increased risks associated with high leverage. These findings contribute valuable insights into capital structure and compensation strategies, especially in different financial contexts, and provide practical recommendations for corporate leaders in designing executive pay.

Keywords: Financial leverage, Financial distress, Key management compensation, Capital structure, Moderation effect

Introduction

The COVID-19 pandemic has affected several corporate sectors in the world, and Indonesia is no exception. International companies, in particular have observed an unprecedented disruption in their business operations due to the pandemic (Gurkov, 2022). Data from Indonesia's Central Bureau of Statistics (BPS) shows that the national economy contracted 2.07% year-over-year (yoy) in 2020 compared to 2019. With these economic struggles, many companies' financing decisions have been made to sustain their operations since many have resorted to debt despite the economic slowdown. The impacts of this economic slowdown were notably felt in consumer cyclical companies, a sector that is very sensitive to economic changes such as the pandemic. A key component of corporate financial management is the use of financial leverage, which represents a firm's reliance on borrowed funds to support its operational and investment activities. Additionally, key management figures, such as CEOs and other executives, play an essential role in strategic decision-making, leading companies to assess compensation policies for these leaders. As noted by Gurkov (2022), increasing managerial compensation during the pandemic served as an effective incentive,

helping managers to creatively guide their companies toward larger objectives that were otherwise difficult to achieve in such challenging times.

According to the literature, it has been widely shown that CEO compensation is one of the most prominent areas of research since the significant boost in CEO pay packages from the 1970s onwards (Frydman & Saks, 2010). Some concerns have been raised about overcompensation as it is often not aligned with firm performance (Cheng & Firth, 2005). Some research works have established a positive relationship between CEO compensation and firm performance (Conyon, 1997; Coughlan & Schmidt, 1985; Frydman & Saks, 2010; Kato et al., 2007; Sheikh et al., 2018), while others show an insignificant relationship (Bebchuk et al., 2002; Jensen & Murphy, 1990). Other studies point out that CEOs can also target private benefits through, for example, empire-building (Garvey, 1997), keeping excess cash (Liu & Mauer, 2011), extracting rents (Bebchuk et al., 2002), and acquiring golden parachutes at the cost of shareholders (Hartzell et al., 2004). Even though political constraints have kept CEO compensation in check, compensation schemes are still far from being properly performance-related (Jensen & Murphy, 1990).).

Empirical evidence shows that financial leverage is associated with executive compensation. Lin et al. (2019) and Suherman (2019) documented a positive association between financial leverage and compensation. However, research in Indonesia by Kunaifi et al. (2021) found a negative relationship between financial leverage and top management compensation in family firms. These results suggest that further investigation be conducted regarding the influence of financial leverage on key management compensation. Another concern during this pandemic may be financial distress. Lin et al. (2019) found that financial distress moderates the relationship between financial leverage and executive compensation. Chang et al. (2022) further stated that financial distress, as an independent variable, has a positive influence on key management compensation. Therefore, financial distress can be used as a moderating factor between financial leverage and compensation.

This research centers on consumer cyclical companies listed on the Indonesia Stock Exchange (IDX) between 2018 and 2022. Such companies are especially vulnerable to economic volatility, with performance often reflecting broader economic trends. The economic disruptions, including challenges from COVID-19, affect the production of a wide range of goods and services, from automotive products and luxury goods to household items and consumer services. As argued above, this study intend to fill the gap of literatures by analyzing the effect of financial leverage on the compensation of top executives and how financial distress moderates this relationship. By focusing on consumer cyclical firms, which are more acutely impacted by macroeconomic trends, this study provides a robust framework for examining the strategic financial responses of companies facing economic challenges. The results of this study may hold some additional value to policies and governance, especially in developing countries, where firms may feel the most strain to service or repay their debts during shocks.

Theoretical background

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frameworks: the trade-off theory and agency theory. The trade-off theory, first proposed by Modigliani and Miller (1963), suggests that firms aim to strike an optimal balance between debt and equity in order to maximize their overall value. According to this theory, while debt financing provides tax advantages, firms must be cautious about taking on too much debt because of the potential costs associated with bankruptcy. However, research indicates that these direct bankruptcy costs might not fully explain why some firms avoid excessive leverage. As a result, scholars have started to explore the role of indirect bankruptcy costs in shaping capital structure decisions. Titman (1984) developed a model to illustrate how the liquidation of firms producing unique products could be especially costly, not just financially, but also in terms of relationships with employees, customers, and suppliers. In particular, employees with firm-specific skills face a loss in human capital value if a firm goes bankrupt, which in turn affects the firm's approach to borrowing. Building on this idea, Berk et al. (2010) further argue that the costs of financial distress, particularly those related to human capital, could be significant enough to deter firms from taking on substantial debt.

Another theoretical framework is agency theory which introduced by Jensen and Meckling (1976). This theory concerns about conflicts that may arise between the principal or the shareholder and the agent or the manager, where the managers place their utility above those of shareholders, such misalignment can lead to decisions that may not be beneficial to the firm. Regulatory structure within the firm has to be such as to align the incentive and the powers of controls to mitigate such conflicts. Both agency and trade-off theories give a more subtle understanding of how the firms' benefits and costs of debt are balanced, while they control for actions and motivations of their managers.

Financial Leverage
According to Syamsudin cited in Komang et al. (2020), financial leverage refers to the manner in which a firm employs fixed-cost assets or funds in the form of debt to enhance its potential returns on equity. The concept immediately brings forth how a firm can use borrowed funds to finance operations or projects or any other income-generating activity with the hope of generating more earnings compared to what could be achieved by using equity financing alone (Claassen et al., 2023). When a firm employs financial leverage, it assumes the obligation to pay interest on the amount borrowed. On the other hand, when the investments yield returns in excess of the cost of debt, the additional income belongs to the equity holders. Consequently, even though financial leverage can support profitability and lead to greater returns for shareholders, it also gives rise to financial risk especially in scenarios where business performance does not turn out as expected

or economic conditions get worse (Choi and Richardson, 2016). In this aspect, using financial leverage in a judicious manner becomes extremely important to manage both potential gains and associated risks effectively.

Key Management Compensation

According to Oktavia and Paramitha (2021), compensation includes all types of income, both monetary and non monetary, received directly or indirectly by officers as a reward for their services rendered to the organization. Among other things, it includes salary, bonus, benefit, and other types of compensation. For the purpose of this research, key management refers specifically to the board of commissioners and the board of directors; it underscores their respective roles in the governance structure of the company. This difference is because Indonesia has adopted a two-tier board system that clearly separates the supervisory role played by the Board of Commissioners from the management role played by the Board of Directors.

Considering that CEO compensation is a large factor in the general cost pool of a company, it may get influenced by several factors leading into financial decisions and performance of an organization (Kweh et al., 2022; Denis and Sibilkov, 2010). One important factor is financial leverage, defined as the proportion of indebtedness in the financing of the firm's operations and its investments. Highly geared-up financial leverage could, therefore, affect a firm's risk profile and cash flow, to an extent that it would inversely impact compensation levels awarded to its senior executive officers, including the CEO.

Financial Distress

According to Hidayat and Yuniati (2024), financial distress is defined as a condition in which the state of finances of a firm is under crisis, popularly described as an unhealthy financial status. The state of distress indicates that the firm is unable to settle its financial obligations, after which serious consequences may follow, including bankruptcy. In this respect, it is considered that the financial distress assessment is measured by the Altman Z-Score, which is an established measure of a firm's financial health. The Altman Z-Score is a quantitative analysis that classifies firms according to the likelihood of facing financial difficulties. Specifically, when the firm's Z-Score is less than 1.1, the firm is classified as being in a state of financial distress, meaning it has a high risk of bankruptcy or insolvency. On the contrary, a Z-Score of more than 2.6 indicates that the company is in a better state of finance and is not considered to be in financial distress (Tania et al., 2021). This assessment method is very important because it gives the investor and management all clear indications of the risks and a guideline for making informed decisions with regard to strategic actions and interventions in finances.

Profitability

According to Lailiyah and Suryono (2019), profitability refers to the measure of a firm's ability to generate profit by using the assets effectively. This measures how a firm can leverage the available resources under its disposal to create value, which directly impacts the financial health and sustainability of the firm. Empirical evidence has long established profitability as a major determinant of executive compensation, especially for CEOs. Jensen and Murphy (1990) documented a positive pay-performance sensitivity where the higher the rise in the value of the firm, the higher the increase in CEO's wealth. Similarly, Kato and Kubo (2006) found a positive association between the firms' accounting profitability and CEO cash and bonus payments for Japanese companies.

Other stdy by Zhou (2000) reported a similar relation for Canadian firms where executive's compensation was found to be positively correlated with the firm performance. In the UK, Ozkan (2011) discovered that cash payoff associated with executive performance, yet this correlation was quite weak when total pay was considered. Moreover, Chen et al. (2015), using the U.S., found that the enactment of the Sarbanes-Oxley Act enhanced pay performance sensitivity, therefore an elevated accounting standard along with a strengthened corporate governance generated better alignment in the compensation of executives along with corporation performance. These findings indicate that profitability is an important factor in the world to design executive compensation in order to align the interests of management and shareholders, particularly through incentive-based compensation structures.

Hypothesis development

Financial leverage and key management compensation

Studies by Lin et al. (2019) and Suherman (2019) give evidence of a positive relationship between financial leverage and key management compensation. These two studies suggested that as a company's leverage increases, so does the remuneration of its key management. This relationship may indicate that firms with higher leverage reward their management to compensate for the greater responsibility and risk associated with debt. Conversely, studies by Adu-Ameyaw et al. (2021) and Kunaifi et al. (2021) demonstrate a negative relationship between financial leverage and key management compensation. In these cases, firms with higher leverage might restrict executive pay as a means of risk mitigation or cost management, especially in financially constrained environments. Given these mixed findings in the literature, this study hypothesizes:

H1: Financial leverage influences key management compensation.

Financial distress in financial leverage and key management compensation

Lin et al. (2019) studied the effect of financial leverage on key management compensation by comparing financially distressed companies with financially healthy ones. The study found that the relationship between debt and key management compensation in financially distressed firms is negative, implying that companies facing financial difficulties may curtail executive pay, probably due to limited resources or plans to restore the company's financial health. Alternatively, Chang et al. (2022) find financial distress as an independent variable positively affecting executive compensation. This implies that under some circumstances financial distress may elicit an

increase in managerial compensation as firms seek to retain experienced captains to steer the ship through troubled waters. Given the said differences with regards to their perspectives, this study proposed the following hypothesis: *H2: Financial distress moderates the effect of financial leverage on key management compensation.*

Research methodolgy

Data and sample
This research has a quantitative research design, where the relationship among the variables is measured and the hypotheses are tested for generalization. Such quantitative techniques are very apt in financial or management studies where it is important to have objective and quantifiable data to support the management in its decision making process. The sample frame will comprise 141 consumer cyclical companies that are listed on the Indonesia Stock Exchange (IDX), between the years 2018 to 2022. This sector, which is vulnerable to changes in the economy, offers a good environment to examine the relationship between financial leverage and management pay. This use of purposive sampling is a non probability sampling design that involves selecting subjects according to certain values and criteria:

1. Complete financial reports (2018–2022) to ensures consistent reporting for longitudinal analysis.
2. Disclosure of key management compensation which allows direct analysis of compensation as a primary variable.
3. Reports in Indonesia Rupiah (IDR) to voids currency conversion issues for data consistency.
4. Not suspended by IDX, focuses on active, compliant companies with reliable reporting practices.

This study utilizes secondary data with a focus on annual reports and financial statements contained in the IDX website (www.idx.co.id) for the duration of 2018 to 2022. The use of secondary data is also economical and efficient as it eases the process of obtaining by providing ready made standard information that is already verified, which proves useful in conducting statistical studies over the consumer cyclical sector in Indonesia.

Model Analysis
The multiple linear regression analysis is employed by this study to explore the relationships between financial leverage, the control variable return on assets (ROA), and the dependent variable, owing to which key management compensation exists. This would quantitatively allow one to assess the extent of variation in financial leverage and ROA that generates a variation in the compensation received by key management personnel in the companies being studied. The use of Moderated Regression Analysis (MRA) is a strong methodological feature of the study allowing one to examine the moderating role of financial distress on the relationship between financial leverage and key management compensation. An extension of the ordinary least squares regression, MRA aims not just to assess the direct effects of independent variables on the dependent variable, but also to present evidence of possible interactions among those variables. Thus, such a framework is essential for understanding how the impact

of financial leverage on key management compensation could vary depending on the level of financial distress, thus leading to a more explained view of these relationships (Kweh et al., 2022). Below is the following equations related to hypothesis testing in this study:

$$MCOMP\ it = \alpha + \beta 1 LEVit + \beta 2 ROA\ it + \varepsilon\ it$$

Description:
$MCOMP_{it}$: Compensation of key management for company i during period t.
LEV_{it} : Financial leverage of company i during period t.
ROA_{it} : Profitability of company i during period t.
α : Constant term.
β : Regression coefficients.
ε_{it} : Error term (residual or prediction error).

$$MCOMP\ it = \alpha + \beta 1 LEVit + \beta 2 FDit + \beta 1 LEVit\ x\ \beta 2 FDit + \beta 3 ROA\ it + \varepsilon\ it$$

Description:
$MCOMP_{it}$: Compensation of key management for company i during period t
LEV_{it} : Financial leverage of company i during period t.
FD_{it} : Financial distress of company i during period t.
ROA_{it} : Profitability of company i during period t.
α : Constant.
β : Regression coefficient.
ε_{it} : Error (residual or prediction error).

The MRA equation helps to understand interaction effects, shedding light on the connections between financial leverage, financial distress, and important management compensation. The t-test is used to evaluate the partial regression coefficients, determining the influence of each independent variable on the dependent variable. A significant effect is indicated when the significance value is below 0.05, which leads to the rejection of the null hypothesis; conversely, if the significance value is above 0.05, the effect is deemed insignificant. Table 1 presents the variables examined in this study. The study highlights the R^2 test, which measures how much variation in the dependent variable is explained by the independent variables. An R^2 value close to 1 indicates a strong predictive relationship, while a value near 0 suggests a weak one. This analysis sheds light on how financial leverage and profitability, moderated by financial distress, influence key management compensation for companies on the Indonesia Stock Exchange. To ensure model validity, classical assumption tests are also conducted, including normality, multicollinearity, heteroscedasticity, and autocorrelation checks. Normality is confirmed if the 2-tailed p-value exceeds 0.05, while multicollinearity is absent if tolerance exceeds 0.10 or VIF is below 10

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Table 1. Variables measurement

Variable	Operational definition
Financial leverage	Debt to Asset Ratio $= \frac{Total\ Debt}{Total\ Assets}$ x 100%
Key management compensation	The total of short-term incentives, long-term incentives, and post-employment benefits provided to the board of commissioners and directors of the company.
Financial distress	Altman Z Score = 6.56 (Working Capital / Total Assets) + 3.26 (Retained Earnings / Total Assets) + 6.72 (EBIT / Total Assets) + 1.05 (Total Equity / Total Debt)
Profitability	Return on Asset $= \frac{Net\ Income}{Total\ Asset}$ x 100%

Source: Author's elaboration.

The heteroscedasticity test checks for constant variance in residuals across levels of independent variables. A random distribution of residuals around the zero line on the Y-axis indicates the absence of heteroscedasticity, supporting the reliability of the regression model. Finally, the autocorrelation test assesses whether observations at one time period correlate with those at previous periods. A Durbin-Watson (dw) statistic between -2 and 2 suggests no autocorrelation, confirming that the residuals are independent.

Findings

Based on the result of the normality test, the findings are presented in Table 2, which indicates that for Model 1 and Model 2, the data is normally distributed, considering a sig (2-tailed) value greater than 0.05. In addition, the results of the heteroscedasticity tests for Model 1 (without moderation) and Model 2 (with moderation) are presented below in Figures 1 and 2. The scatter plot points in these two figures are scattered both above and below the zero line—a confirmation that the models are not subject to heteroscedasticity. Further, as reflected in Tables 3 and 4, the results of the autocorrelation test for the two models indicate that the Durbin-Watson values fall between -2 and 2. This range satisfies the assumption of no autocorrelation, thus legitimizing the data for further analysis.

Interpretation of the multiple linear regression equation yields the following relationships: Here, it can be observed that the regression coefficient for the variable financial leverage (LEV) is 51.727, indicating that for a single unit increase in financial leverage, key management compensation is expected to rise by 51.727 times. Similarly, the variable profitability (ROA) has a regression coefficient of 625.374, indicating that for one unit increase in profitability, key management compensation will rise by 625.374 times.
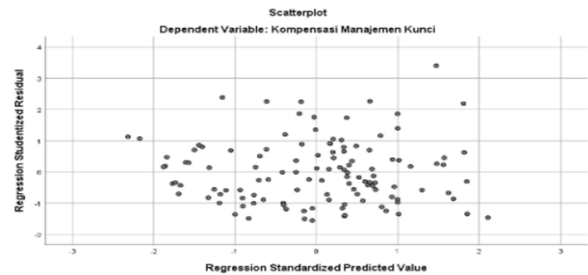
Tabel 2. Hasil Uji Normalitas

Model	Sig 2 tailed value
Model 1 (With Moderation)	0,057
Model 2 (Without Moderation)	0,648

Source: Author's elaboration.

Gambar 1. Hasil Uji Heterokedastisitas Model 1
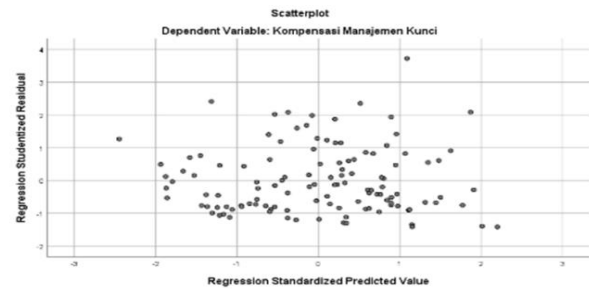
Source: Author's elaboration.

Gambar 2. Hasil Uji Heterokedastisitas Model 2

Source: Author's elaboration.

As presented in Table 5, partial t-test shows that there is a positive effect of financial leverage on key management compensation significantly: the β value is 0.319, the significance level is 0.000, and the t-statistic is 5.347. Therefore, based on the positive β value, it supports the acceptance of hypothesis H1, hence proving a strong influence of financial leverage on management compensation. As shown in Table 5, the coefficient of determination reports an adjusted R-squared value of 0.598. This value suggests that 59.8% of the variation in key management compensation is explained by financial leverage and profitability jointly, while the rest, 40.2%, is due to factors other than those considered in this study. If moderation is allowed in the analysis, as Table 6 demonstrates, the adjusted R-squared value increases to 0.636. This suggests that 63.6% of the variation in key management compensation can now be explained by financial leverage, financial distress, and profitability, leaving 36.4% to unexamined variables

Selanjutnya, dilakukan review dan kajian terhadap artikel secara mendalamdengan memfokuskan pada hasil penelitian dan jumlah kutipan sitasi artikel terbanyak. Pada akhir penelitian dilakukan perbandingan hasil temuan dari beberapa artikel dan membuat kesimpulan.

Tabel 3. Hasil Uji Autokorelasi Model 1

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.778ᵃ	.605	.598	2198.508	.627

Source: Author's elaboration.

Tabel 4. Hasil Uji Autokorelasi Model 2

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.805ᵃ	.649	.636	2091.284	.754

Source: Author's elaboration.

Tabel 5. Hasil Model Regresi Linier Berganda

Variables	Standardized Coefficients (Beta)	T-value	Sig.	VIF
Financial leverage	.319	5.347	.000	1.054
ROA	.785	13.161	.000	1.054

R Square - 0.605
Adjusted R Square - 0.598

Source: Author's elaboration.

Other regression coefficients provide further insight. The financial leverage variable demonstrates a regression coefficient value of 39.269, which means that for each unit increased in financial leverage, key management compensation grows by 39.269 times. On the contrary, the negative regression coefficient of -5.351 is manifested by financial distress-FD. This indicates that when there is an increase in financial distress by one unit, then management compensation will decrease by 5.351 times. Besides, the interaction term between financial leverage and financial distress-FDxLEV manifests a regression coefficient of -9.009. This implies that when FDxLEV increases by one unit, then the compensation for key management will decrease by 9.009 times. Furthermore, profitability, as proxied by ROA, has a positive effect, such that for every unit increase in profitability, key management compensation grows by 703.042 times.

Tabel 6. Hasil Moderated Regression Analysis

Variables	Standardized Coefficients (Beta)	T-value	Sig.	VIF
Financial leverage	.242	3.839	.000	1.032
Financial distress	-.125	-2.043	.043	1.221
Financial leverage x Financial distress	-.220	-3.281	.001	1.471
ROA	.883	13.093	.000	1.487

R Square – 0.649
Adjusted R Square – 0.636

Source: Author's elaboration.

The results of the moderated regression analysis shown by the t-test in Table 6 indicate that the interaction of financial leverage with financial distress (FDxLEV) is statistically significant with p = 0.000 much lower than the threshold of 0.05. This suggests that financial distress played the role of a moderator in the relationship between financial leverage and key management compensation, hence providing support to hypothesis H2. Finally, multicollinearity diagnostic as presented on Tables 5 and 6 indicates that multicollinearity is absent because tolerance values are greater than 0.10 and VIF values are below 10. This assures the reliability of the regression model used in this research.

Discussion

Hypothesis 1 proposes that financial leverage influences key management compensation. From multiple regression analysis, it was found that there is a positive association between financial leverage and key management compensation in consumer cyclical companies. Hence, the discovered evidence supports hypothesis 1. From here, it can be interpreted as: consumer cyclical companies with a higher degree of financial leverage tend to pay higher key management compensation. This result is in line with the trade off theory, where, even though high debt levels increase the costs of bankruptcy, high debt levels yield tax benefits by reducing taxable profits through interest expenses. Nazir et al. (2021) therefore argued that management should establish optimum debt ratio that will balance the costs and benefits of debt, so that when management of a company succeeds in obtaining debt efficiently, it is considered to be an achievement. These findings are consistent with the studies conducted by Bertay and Uras (2020), Bouteska et al. (2024), Lin et al. (2019), Liu et al. (2020), and Suherman (2019) which also observed that financial leverage has a strong and positive effects on managerial pay. Third, the study by Chemmanur et al. (2013) shows that leverage positively and significantly affects average employee pay, and that the associated labor costs due to higher leverage may easily outweigh the incremental tax benefits. Again, Kweh et al. (2022) found that both salary and bonus contribute to the positive relation of firm's performance with the compensation of CEOs.

Meanwhile, hypothesis 2 states that financial distress moderates the relationship between financial leverage and management compensation. Results of the study present that, as a predictor variable, financial distress has a substantial negative impact. This negative coefficient means that, when conditions of high financial distress and a high level of financial leverage are present, key management compensation tends to decrease. This reduction occurs because a financially distressed firm with a high level of debt tries to reduce compensation costs. This result is in line with Lin et al. (2019), who also found that

financial distress can moderate the relationship between financial leverage and key management compensation.

The key management compensation is significantly and positively related to the control variable, profitability. In particular, profitability measure which is ROA, substantially affects key management compensation; that is to say, companies with a higher value of ROA, signaling efficiency in using the assets, are prone to rewarding key management for their professional performance. Results such as this correlate with those obtained by Liu et al. (2020) and Bouteska et al. (2024), where the correlation between ROA and executive compensation was positive. Previous empirical studies also concluded that there exist a positive correlation between the performance of the firm and compensation paid to the CEO (Frydman & Saks, 2010; Kato et al., 2007; Sheikh et al., 2018).

Conclusion

The study examines the financial distress-based moderating effect of financial leverage on key management compensation in consumer cyclical companies. Two major contributions have stemmed from this research. First, financial leverage has a positive and significant effect on key management compensation in consumer cyclical firms. An increase in the level of financial leverage will also increase compensation awarded to key management, indicating that higher levels of debt bring with them attention to the increase in managerial compensation. This finding accords with the trade-off theory, which suggests that companies with greater leverage may compensate management more highly because of the benefits and risks associated with additional debt. Secondly, financial distress acts as a moderating effect on the relationship between financial leverage and management compensation. When a company is experiencing financial distress, it not only alters the use of leverage but also how the firm rewards key management. The moderating effect suggests that firms can realign their compensation practices as they gain better financial information about their operations while they pose a greater risk of financial distress with increasing leverage. The ability of financial distress to influence compensation enforces the complicated link between a company's financial structure and the compensation practices for its executives.

This study provides empirical evidence in support of the tradeoff theory, which states that firms weigh the private benefits and social costs of corporate debts with severe emphasis on the aspect of financial distress. Practically, the findings are relevant for managers and decision-makers. Knowledge on how leverage interacts with financial distress to influence management compensation will assist firms in making better decisions with respect to capital structure and executive compensation. What was discussed earlier did not provide an instantaneous account of achievements, such as improving managerial compensation models and organizing results in a straightforward manner. Although such issues are numerous, discussing just one under this study may also highlight the limitations of this work. The sample for this study is comprised solely of consumer cyclical companies in other sectors. Since other variables did not provide cash compensation decisions, critical variables like market conditions or firm specific characteristics have not been accommodated. Future research could use this study to survey a much larger range of industries and include lots of moderating factors, which could thus convey a much broader outlook on the relationship between financial leverage, financial distress, and executive compensation.

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