



# Money and Employee Motivation

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## **20 | 20 SKILLS ASSESSMENT**

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**Abstract.** – Research consistently substantiates the effectiveness of financial incentives on job performance, although companies need to consider the issue of job quantity versus quality and also be aware of the limitations of financial incentives. Employees can have vastly different motives for acquiring wealth – including using money to fulfill psychological needs. Thus, it is not surprising that money alone is less an effective motivator for employees than when it is used in conjunction with non-financial reinforcements. We review the nuances of financial incentives and make basic recommendations that can form the basis of best practice compensation and incentive policies.

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The 20 | 20 Skills™ assessment is the only screening, selection and training assessment guaranteed to satisfy professional testing and legal standards and which was designed specifically for the hospitality-service industry. During the assessment test takers must indicate the degree to which they disagree or agree with a number of statements that pertain to their personality or approach to professional situations. One of those statements is:

**“Acceptance is more important to me than money”**

How well does that statement describe you, your coworkers or executive team? More importantly, what does one’s attitude towards money as a motivator actually reveal? This article explores this latter question in the context of classic and recent research findings pertaining to the workplace and beyond. Our aim is to outline the nuances of financial incentives for enhancing job performance.

## **Understanding Materialism**

*Materialism* is defined simply as when a person values money, wealth and possessions over other things in life<sup>14</sup>. Studies have consistently shown that a materialistic focus in life is associated with a lower psychological well-being<sup>2,6,7,8,12</sup>. Even though individuals who are very poor financially demonstrate increased happiness when their income rises, intensity of desire for wealth remains negatively correlated with psychological well-being<sup>2</sup>. There are a few possible reasons for these trends<sup>2</sup>. Specifically, materialistic pursuits do not provide what people are really looking for in their quest for happiness; the tendency for those without much in the way of non-material resources to focus on material goods or the endless and forever evolving supply of goods and services produced in materialistic or capitalistic societies precludes satiation. They further

suggested that people who are unhappy or lacking in social connections may seek solace in material goods, using external means to fulfill internal desires and aspirations<sup>2</sup>.

Some researchers<sup>16</sup> have argued that the motives that drive one to focus on money are more relevant than the intensity of the focus itself, and they subsequently differentiate between *instrumental materialism* and *terminal materialism*. Instrumental materialism describes using material goods as a means for attaining personal goals and fulfillment; whereas terminal materialism involves using material possessions to achieve social status and elicit envy from others. They also divide motives for materialistic pursuit into three different categories: positive, negative and freedom of action. Positive motives involve using money for basic necessities and as a measure of achievement. Negative motives refer to using money to gain power or superiority over others. Negative motives also include efforts to allay one's self-doubt. Motives concerning freedom of action simply imply spending money in any way that one desires.

When the significant negative correlation between subjective well-being and money importance was analyzed, while controlling for the influence of motivation, the correlation lost its statistical significance. In addition, when calculated independently, the relationship between negative motives and money importance was both negative and statistically significant. As a result, the authors<sup>16</sup> attributed the correlation between psychological well-being and money importance to negative motives alone. This suggests that not all motives for wanting money lead to decreased happiness. Their findings suggest that it is not the importance of money that contributes to well-being; rather, *attempting to use money to alleviate self-doubt and increase self-esteem leads to problems*. They add that such motives become problematic when money is used for things it cannot provide, e.g., self-esteem, happiness and genuine friendship.

Overall, the research described above suggests that having money is not related to personal happiness *per se*. However, whether people who have money or not, the amount of importance they place on it can actually be maladaptive. Indeed, individuals who consider money important tend to be less happy than those who place less importance on money<sup>2,16</sup>.

## **Financial Incentives in the Workplace**

No one works for free, nor should they. While pursuing money based on negative motives can lead to a poorer psychological well-being, this is not the same as pursuing money to provide security and comfort for oneself and family. Obviously, employees want to earn fair wages and salaries, and employers want their workers to feel that is what they are getting. To that end, it is logical that employees and employers alike view money as the fundamental incentive for satisfactory job performance.

The use of monetary or other financial incentives in the classic “work performance paradigm” is based primarily on reinforcement theory. Reinforcement theory<sup>15</sup> focuses on the relationship between a target behavior (e.g., work performance) and its consequences

(e.g., pay), and it is premised on the principles and techniques of organizational behavior modification<sup>9,17</sup>. Organizational behavior modification is a framework within which employee behaviors are identified, measured and analyzed in terms of their functional consequences (i.e., existing reinforcements) and where an intervention is developed using principles of reinforcement<sup>10,17</sup>.

In a much publicized study, Gupta and her colleagues<sup>5</sup> analyzed thirty-nine studies conducted over four decades and found that cold-hard cash motivates workers whether their jobs are exciting or mundane, in labs and real-world settings alike. But the research team acknowledges that money is not the only thing that concerns employees – noting that beyond a certain point higher salaries will make employees happier, but it will not “buy” better performance. Still, Gupta warns that employers who dole out small merit raises – less than 7% of base pay – may do more harm than good. According to her, small raises can actually be dysfunctional in terms of motivation because employees become irritated that their hard work yielded so little. Because of this, she advises employers who must give small raises to be careful about linking them to results and to be scrupulous about being fair.

Still, the research by Gupta’s team is just one study from a wealth of findings that can appear inconsistent. These apparent inconsistencies reflect, in part, important nuances about the relationship between monetary incentives and job performance. For example, the broad literature on job performance encompasses financial incentives that address both *individual* and *group* performance and productivity. Furthermore, monetary incentives can extend beyond the mere raises discussed by Gupta’s team to include individual and small-group rewards, merit pay, pay-for-performance, variable pay plans, or group bonus plans as well as profit-sharing and gain-sharing incentive plans.

Perry and his colleagues<sup>13</sup> analyzed this diverse literature in an outstanding review and culled two general propositions relevant to best practices in the service industry:

- **Financial incentives moderately to significantly improve task performance, but their effectiveness is dependent upon organizational conditions.** Differences in institutional arrangements contribute to the feasibility and effectiveness of various monetary incentives, as do differences in employees’ preferences for specific incentives. Therefore, companies are wise to study these issues before implementing changes to existing incentive plans. This is especially pertinent for service organizations, where financial reinforcements tend to produce a stronger effect on task performance than non-financial rewards used alone. Even stronger results are seen with a composite approach. For example, one meta-analysis of 72 field studies found that monetary incentives improved task performance by 23%, social recognition improved task performance by 17% and feedback elicited a 10% improvement<sup>18</sup>. Simultaneously combining all three types of reinforcements improved performance by 45%.
- **Group incentive systems are consistently effective in private sector settings.** Team-based or small-group incentives are defined as rewards whereby a portion

of individual pay is contingent on measurable group performance<sup>1</sup>. In general, its effectiveness is dependent on the characteristics of the reward system, the organization, the team and the individual team members<sup>1</sup>. Here again, studying this issue via employee surveys or interviews can be useful. But generally speaking, research suggests that equally divided small-group incentives sustain high levels of productivity and satisfaction for group members, and that small-group incentives are at least as effective as individual incentives with groups of two to twelve people<sup>4</sup>.

Qualitative, quantitative and survey research studies of alternative pay systems such as profit-sharing or gain-sharing plans are even more consistent in their findings. These incentive programs include various pay-for-performance approaches that link financial rewards for employees to improvements in the performance of the work unit<sup>20</sup>. Research reveals that these types of incentive systems are associated in practice – and in employer and employee minds – with both higher productivity and improvements in organizational performance.

## Cashing in on the Latest Research

We have shared several useful insights into the relationship between money and employee motivation. For readers wanting more in-depth discussions of this information, we recommend the resources listed below. These sources also provide guidance on how to translate some of these principles into practice:

- Heneman, R. L. (1992). *Merit pay: linking pay increases to performance Ratings*. New York: Addison-Wesley.
- Milkovich, G. T., & Wigdor, A. K. (Eds). (1991). *Pay for performance: evaluating performance appraisal and merit pay*. Washington, DC: National Academy Press.
- Perry, J. L., Mesch, D., & Paarlberg, L. (2006). Motivating employees in a new governance era: The performance paradigm revisited. *Public Administration Review*, 66, 505-514. (Accessed on October 26, 2006 at <http://www.aspanet.org/scriptcontent/custom/staticcontent/t2pdownloads/PerryArticle.pdf>)

Of course, the available research makes it clear that a monetary incentive is simply one piece of a larger mosaic of issues. Savvy organizations delve into those other issues. Employee surveys and interviews can help organizations identify what type of monetary incentives are the most motivating to a given employee base, and, naturally, those incentives must be feasible for the organization to implement. Subsequently, companies must balance financial considerations with other non-financial reinforcements to maximize job quantity and quality. The best rule of thumb stems from Stajkovic and

Luthans' influential meta-analysis,<sup>18</sup> which concluded that *feedback combined with money and social recognition produced the strongest effect on job performance*.

We further recommend that performance feedback should be structured to maximize its benefit both to the employee and the company. For example, many employees respond well to coaching or mentoring. And there are many tools, such as the 20 | 20 Skills™ assessment, that can streamline goal-setting for individual employees or even entire departments. Goal-setting is an important aspect to enhancing job performance, although it is not always an obvious one to managers. For instance, one review<sup>19</sup> discovered that, while monetary incentives influence performance, the relationship is not mediated by goal-setting. That is, *goal-setting and monetary incentives independently influence job performance* (for more information, see Perry et al.<sup>13</sup>).

HVS has also completed proprietary research on the effectiveness of pay-for-performance metrics in the hotel, gaming and restaurant industries, and its results generally reinforce the findings of researchers like Gupta and Perry. That is, “money ranks below other factors relative to job satisfaction, but high on the motivational matrix when all other factors have been met.” Furthermore, as executive search professionals, we understand what motivates individuals to change positions and employers. Job stature, scope of responsibilities, employer reputation and other key criteria need to be met before compensation negotiations begin. Once negotiations begin, it is all about the money and how the pay package compares to industry peers.

For example, once major league baseball players become free agents, “what motivates them to stay or sign with another team?” Issues such as team dynamics, ability to win, job security, preferred location and position must be satisfied. Once satisfied, it becomes an issue of money. And the easiest way to compare offers is to look at what other similar players in similar positions are paid. It is no different in the corporate world. The tangible results of a well-conceived pay program are numerous, but the HVS study found that executives with clear pay-for-performance metrics outperformed their peers by nearly 80% at the Net Operating Income line.

HVS Executive Search and 20 | 20 Skills™ assessment offer consultation on employee compensation and coaching issues. But for those companies seeking simple guidance here and now, the following heuristic nicely summarizes how most employees in the private sector view the relationship between money and employee motivation...

**“Show me the money, show me respect and show me attention...  
or show me the door.”**

## About the Authors

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