

Influence of Pay for Performance on Employee Engagement & Turnover Intention

Shweta Mittal

The purpose of this study is to investigate the relationship between pay for performance, turnover intention and employee engagement with the social exchange theory. Structured questionnaire was used to get the data from 271 employees. The findings exhibit that pay for performance is positively related to turnover intention and employee engagement.

Shweta Mittal is from Bennett University, Greater Noida & is a Post-Doctoral Fellow, ICSSR at Indian Institute of Technology Delhi. E-mail: f12shwetam@iima.ac.in

Introduction

The pay for performance (PFP) performs the significant role by optimizing the cost of compensation and rewarding the high performers (Bhattacharyya, 2013). Pay for performance is not a universal policy, it varies with the organization and place (Bhattacharyya, 2013). Gerhart et al., (2009) stated that pay for performance is based on appraisal ratings provided by the supervisor's, distinguishing the high performers. Organizations are witnessing a paradigm shift from the traditional HR practices like lifetime employment and seniority-based pay after liberalization towards more specific motivating HR policies like pay for performance, with the specific aim of monitoring and recognizing the performance of employees.

The five-dimensional model of Hofstede (2001) characterized India with the cultural values of high-power distance and collectivism. High power distance reflects hierarchical, paternalistic and status whereas medium collectivist orientation is influenced by extended family, caste, religious and linguistic. The emotional aloofness combined with high con-

trol of subordinates characterized by the British style of Indian management was inherited when the latter left India in 1947 (Singh, 2009). Indians are to a greater extent still more parochial in thinking, feeling, and behaving. They are more accustomed to thinking in terms of narrow identities like our own selves, castes, communities, regional and linguistic groups (Desai, 2008). The differences mentioned above suggest that the behaviors and influence mechanisms needed to manage Indian workforce can be substantially different from that developed in the West.

Although Indians are indeed collectivists, there are strands of thoughts, feelings, and actions in their minds that reflect the underlying value of individualism. India is divided into two parts inward looking and outward looking. The inward looking has characteristics of collectivism and high-power distance whereas outward-looking is marked by individualism and low power distance. Researchers have provided proof that economic growth and appropriate infrastructure makes individuals independent, in-turn increases the individualistic behavior and intentions (Hofstede, 1991; Triandis, 1995). The studies have found that with economic development, urbanization, technology adoption, competitive environment, market capitalism has brought individualism in the collective society (Gupta & Panda, 2003). Economic development and cultural changes are correlated; the economic development marks major social and cultural changes. Hofstede's (2001) research suggests that economically developed societies adopt

the fundamentals of western capitalism. Thus, the younger, educated employees of today nourish western values of achievement, advancement and ability utilization.

Professionals working in Indian organizations today are better educated and tend to have more evolved thought process. Such employees generally crave for greater autonomy and responsibility to work on their own. Sinha (2008) emphasizes the importance of a participative style of leadership along with a nurturant-task style. As the organizations become more global and there is a greater exchange of knowledge and manpower between the West and the East, we believe that PFP will become salient in driving employee performance. The pay for performance has become relevant to employees who are conscious of their status, promotion, and competence. Today's employees find their worth in the amount they earn, thus pay for performance takes a central position for these employees.

Pay for Performance

HR policy through PFP aims at higher level of performance, remunerated with higher level of pay. Rewards are given to the employees in one or other forms of compensation. The biggest challenge is to decide the form of compensation which impacts employees' attitude and behavior as well as acquire and retain the human capital (Lazear & Rosen, 1981). The organizations aiming for the compressed financial status amongst its employees will be creating an egalitar-

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ian environment (Bloom, 1999). This environment does not promote the high performers, as lack of reward and recognition deter their performance. Thus, organization started investigating how the compensation in different forms, can impact the attitude and behavior of employees for the effective and growth-oriented organization (Gerhart & Rynes, 2003; Pfeffer, 1998; Rigby, 2001). Thus, this led to the growth and extensive use of pay for performance plans (Schuster & Zingheim, 1992). The study by Carla O'Dell and Jerry McAdams, Gibson (1995) stated that pay for performance executed by organization had the net return of 134%. Pay for performance will make the organization less hierarchical and highly competitive, focused, adaptable, and collaborative (Baker, 1993). Thus, the pay for performance acknowledges the performance of the employees and makes them more glued towards their goals. Gerhart & Milkovich (1990) found the compensation like PFP, as a strategic decision because it "typically accounts for 20 to 50 percent of total operating expenses.....and how implications for attraction, retention, and performance motivation across business units and functional areas and thus perhaps for organizational performance." Research has shown that PFP improves the productivity (Rynes et al., 2005) and thus influence work motivation. Lazear

(2000) showed that the productivity increased by 44% with the commencement of pay for performance; Gielen et al. (2010) also gave the similar results where productivity increased by 9%. The meta-analysis done with 45 studies, where incentives were utilized to improve productivity, Condly et al. (2003) showed that productivity improved by the incentive programs by 22 percent. On the contrary, PFIP with the course of time has also resulted in negative consequences; Pfeffer (1998) argued that extrinsic motivation can reduce the creativity and innovation involved in work. The economic and accounting literature has also shown the negative impact of PFIP on intrinsic motivation (Kuntz & Pfaff, 2002; Prendergast, 2008). The book, *Drive* (Pink, 2009) has strongly highlighted that PFIP has negative impact on intrinsic motivation, and reduces the performance of employees. Fang and Gerhart (2012) have shown that PFIP may result in the increase of intrinsic motivation by boosting employees' perceived autonomy and competencies and these results are not in cognizance with the above-mentioned research. Similarly, Ogbonnaya et al. (2017) found that PFIP is positively associated to job commitment, job satisfaction and trust in management. Thus, after looking at the mixed results, it becomes even more imperative that we understand how extrinsic motivation impacts employees' attitude and behavior.

Social Exchange Theory

Social exchange theory (SET) is one of the most important conceptual frameworks to understand workplace behavior.

ior. Social exchange theory posits that interdependent relationships with numerous interactions result in the reciprocity and mostly, quid pro quo reciprocity (Blau, 1964; Kuvaas et al., 2020). The reciprocity rule in exchange theory (Gouldner, 1960) states that positive treatment provided by the party gets obligated to pay back favorably. On the contrary, the opposite also holds true, that negative treatment would also be responded. It also states that, when employer begins a positive action, the employee pays back with positive reciprocation (Cropanzano et al., 2017). Employee-organization relationship is impacted by the pay for performance. Pay contingent performance is an economic exchange between the employer and the employee in a tangible form (Rousseau & Ho, 2000; Shore et al., 2006). The successive positive reciprocal exchange relationship can change the economic relation into high quality social exchange relationship (Cropanzano et al., 2017). The beneficial act of the organization creates obligation for the employee, the employees must pay back by getting involved in the activities beneficial to the organization (Blau, 1964). In accordance with the social exchange theory, pay for performance can be a signal to employees for their worth and competence and is reciprocated by the employees with positive attitudes and behaviors. The relationship between pay

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for performance and work engagement is not much researched and thus is unclear, the present study investigates the relationship between pay for performance and employee engagement i.e., positive work related affective-motivational state of mind (Schaufeli & Salanova, 2011). Work engagement over the years has been predictors of positive employee attitudes and behaviors (Hakanen & Schaufeli, 2012; Innstrand et al., 2012; Shimazu et al., 2015). Thus, it is imperative to understand that paying employees based on their performance affects work engagement.

Remuneration constitutes the most important part of the job. Organizations motivate employees by paying for their performance, creating the pay differences among high and low performers (Lazear & Rosen, 1981; Lazear, 1995; 1999). High performers stay in the organization to earn their incentives (Lawler, 1971) and with the course of time accumulate it over the years. This study helps us to understand how PFP impacts turnover intention. In this research, we will understand the relation between pay for performance with employee engagement and turnover intention.

Employee Engagement

The employee engagement concept in current scenario has attracted widespread attraction from researchers. Employee engagement is an important, highly, and widely referred terminology (Robinson et al., 2004).

Engagement has gained popularity among the scholars and organizations as

individuals increase their performance by investing physical, intellectual, and emotive energy in their job roles, though the effort is discretionary in nature (Cameron et al., 2003; Kahn, 1990). Kahn (1990: 694) has defined employee engagement as “the harnessing of organization members’ selves to their work roles; in engagement, people employ and express themselves physically, cognitively, and emotionally during role performances”. Individual disengagement states that “the uncoupling of selves from work roles; in disengagement, people withdraw and defend themselves physically, cognitively, or emotionally during role performances”. Thus, Kahn (1990; 1992) has described engagement as the state when employee is psychologically present while occupying and doing their work role. Rothbard (2001: 656) states that though engagement is a psychological presence, it comprises two important components: attention and absorption. Attention talks about being involved intellectually in the role while absorption refers to being dedicated and focused on one’s role. Some studies have argued that employee engagement and burnout are in the continuum where burnout is on the other end and they are distinct from each other (e.g., Maslach et al., 2001; Gonzalez-Roma et al., 2006).

Engagement has also been defined as “as a positive, fulfilling, work-related state of mind that is characterized by vigor, dedication, and absorption” (Schaufeli et al., 2002: 74). Vigor is an individual’s state of high efficiency, vitality, and mental flexibility at work, capable of putting energy and persistence at one’s work even dur-

ing problems. Dedication is referred to as having a sense of importance, willingness, eagerness, motivation, and pride at one’s workplace. Finally, absorption is referred to as being immersed at work, whereby the individual loses track of time and doesn’t disassociate himself/herself from the work. Schaufeli et al. (2002:74) further mentions that engagement is not any typical state and is not connected to money but it is a, “a more persistent and pervasive affective-cognitive state that is not focused on any particular object, event, individual, or behavior”.

Employees will be more engaged when they perceive that their performance will lead to higher rewards and recognition. Recognition and rewards in organizations may strengthen employees’ motivation to be completely engaged (Maslach et al., 2001). Similarly, Maslach et al. (2001) reported that in the absence of rewards and recognition, there will be a burnout, and therefore, appropriate recognition and reward (possibly in the form of PFP) is required to foster employee engagement. Pay for performance and employee engagement can be explained with the social exchange theory (Saks, 2006), explaining the reason of engagement-disengagement. In accordance with the social exchange theory, when employees’ pay reflects their achievement, they feel obliged and respond by being engaged in their job role. Compensation or remuneration motivates an employee to achieve higher growth by being focused on their job role and development. A study by Saks and Rotman (2006) showed that when organization provides rewards and recognition to their employ-

ees, they feel obliged and pay back with higher levels of engagement. Kahn (1990) reflects that employees' engagement is dependent on the perception of rewards received. Therefore, employees' perception of reward determines the performance and hence engagement in their work. Thus we believe that PFP is positively related to employee engagement.

Hypothesis 1: Pay for performance is positively related to employee engagement.

Turnover Intention

Research on turnover is plentiful (Griffeth et al., 2000; Hom et al., 1992; Mobley, 1977). Employees' impact on organizations based on their contributions (Lepak & Snell, 1999; Sturman et al., 2003). Retention of employees has become a major problem for the organizations (Wang et al., 2007) and has been a concern for human resource professionals as they invest time and effort in developing human competencies for the organizational performance. Researchers have widely explored the determinants of turnover in the management literature as it is costly (Hinkin & Tracey, 2000), and it impacts the bottom-line of any organization (Flint et al., 2012). The turnover intention is directly linked to turnover.

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and training. Moreover, the researchers have found evidence that employee turnover negatively impacts organizational performance (Trevor et al., 1997). Thus, there is a need to understand under what circumstances this relationship can be altered (Rynes et al., 2005; Shaw et al., 2009).

The workplace and pay go hand in hand. Society for Human Resource Management's (2014) survey of employees found job security, benefits, and compensation as the most important job attributes. All the three job attributes are related to compensation. The pay for performance acts as an extrinsic motivation for the employees, in its absence can result in negative consequences. Organizations when do not pay employees in accordance with their performance, the discontent rises and employees resort to negative behaviors (e.g., lower effort, higher turnover) (Gerhart & Rynes, 2003). The pay for performance can be a key variable in attracting and retaining the efficient workers (Gerhart et al., 2009). The pay for performance with the course of time increases the cumulative pay which can lower the turnover intention. Shaw and Gupta (2007) found that PFP was negatively related to turnover intention of high performers as it strongly communicates that efforts are rewarded.

Rooted in social exchange theory (Blau, 1964) and norm of reciprocity (Gouldner, 1960), high performing employees with the course of time have cumulative impacts on their pay, feel respected and valued and respond by lower

turnover intentions. Pay for performance could be an internal signal for the high performing employees to be a part of the organization for longer period. Therefore, we hypothesize:

Hypothesis 2: Pay for performance is negatively related to turnover intention

Sample & Data Collection

Information was collected from a high-tech company based in India and data was collected from both the managerial and technical staff present during the survey period through questionnaire. In the 271 sample size, 92% percent respondents were males and 7.5 % were females. 16.4 per cent were graduates, 65.5 per cent were postgraduates and 18.1 per cent were Ph.Ds.

Measure of Employee Engagement

This measure consisted of nine-item version of the Utrecht Work Engagement Scale (Schaufeli et al., 2006). Sample items included: “at my job, I feel strong and vigorous” (vigor), “when I am working, I lose track of time” (absorption) and: “my job inspires me” (dedication). Two items from absorption and one item from vigor were dropped due to low reliability. The responses to the items were measured on a 7-point Likert scale ranging from 1 (strongly disagree) to 7 (strongly agree). The Cronbach’s alpha for the scale was .87. We have used the total score instead of three separate dimensions i.e., vigor, absorption and dedication. It is a valid approach to use gen-

eral score of work engagement based on UWES. Schaufeli et al. (2006 :71) stated that “practically speaking, rather than computing three different scores of vigor, absorption and dedication, researcher might consider using the nine-item score as an indicator of work engagement”. Balducci et al. (2010) and Littman-Ovadia (2013) suggested the composite score of work engagement. Seppala et al. (2009) advocated “(...from a practical view, the high correlations between the three factors indicate the substantial overlap between them, and thus restrict their use as a separate dimension”. From the above-mentioned reasoning, the use of composite measure of work engagement is valid in the context of the study.

Turnover Intention

Irving et al. (1997) measure was adapted to assess turnover intention. The scale had 3 items. A sample item of the scale was “I intend to stay in this job for the near future”. The responses to the items were measured on a 7-point Likert scale ranging from 1 (strongly disagree) to 7 (strongly agree). The Cronbach’s alpha for the scale was .82.

Compensation

Various aspects of employee compensation (pay-for-performance, group-performance-based-pay, seniority-based pay, and job security) were measured using 20 items, identified from the literature (e.g., Bustamam, Teng & Abdullah, 2014; Fang & Gerhart, 2012; Fischer, 2008; Gomez-Mejia & Balkin, 1992; Kim & Gong, 2009). The responses to the

items were measured on a 7-point Likert scale ranging from 1 (strongly disagree) to 7 (strongly agree). The Cronbach's alpha for the pay-for-performance was .89.

Control Variables & Data Analysis

In the present study, employee demographic variables such as age, gender, education level, work experience, as well as employee perceptions of job security, group-based pay and seniority-based pay were controlled during the data analysis.

The structural equation modeling (SEM) and ordinary least squares (OLS) regression techniques were used to test the hypotheses. The measurement model and hypotheses testing were assessed using AMOS 22 and SPSS 22 respectively. The constructs' discriminant validity was tested using the average variance extracted (AVE) method suggested by Fornell and Larcker (1981). The demographic variables (age, gender, education, and work experience), and employee perceptions of job security, group-based pay, and seniority-based pay were controlled. The confirmatory factor analysis (CFA) using AMOS 22 was performed to test the convergent and discriminant validities. The composite reliability (CR) and the AVE (Average Variance Extraction) figures were computed and reported for all the study constructs (Fornell & Larcker, 1981).

Results

Confirmatory factor Analysis (CFA) was performed for this study. Thompson

(2004) stated that the measurement model confirms the dimensions of the construct. The CFA was performed with the three dimensions of the model; PFP, employee engagement and turnover intention. The composite reliability value showed the internal consistency of the construct. Fornell and Lacker (1981) suggested the value should be higher than 0.60. AVE is the shared variance by the construct and its measures. The standard value of AVE should be greater than 0.5 (Fornell & Larcker, 1981). The AVE for PFP, work engagement and turnover intention is 0.53, 0.53 and 0.66 respectively and the composite reliability for PFP, work engagement and turnover intention are 0.90, 0.87 and 0.83, respectively. Further, the composite reliability is greater than AVE and AVE has values greater than .50 for all the constructs which implies that the items represent their construct (Fornell & Lacker, 1981). The AVE was above .50 and the square of correlation between the constructs was less than the AVE. This confirms the discriminant validity (Fornell & Lacker, 1981) (Table 1).

The model fitness was determined by the goodness of fit index (GFI), adjusted goodness of fit index (AGFI), root mean square error of approximation (RMSEA), comparative fit index (CFI) and Parsimony adjusted comparative fit index (PCFI). Baugartner and Momburg (1996) proposed GFI and AGFI value should be higher than 0.90. Browne and Cudeck (1993) indicated RMSEA should be less than 0.05 for the model to be fit. The permissible limit of CFI is > 0.90 and PCFI > 0.50 . The

Table 1 Descriptive Statistics & Inter-construct Correlations

	Mean	SD	A	CR	Age	Gender	Educ	WorkEx	PFP	JS	SBP	GBP	WE	TI
Age	35.24	8.92	—	—	—	—	—	—	—	—	—	—	—	—
Gender	.92	.26	—	—	.02	—	—	—	—	—	—	—	—	—
Educ	1.02	.59	—	—	-.14*	-.06	—	—	—	—	—	—	—	—
WorkEx	12.44	8.75	—	—	.95**	.04	-.12 ⁺	—	—	—	—	—	—	—
PFP	4.25	1.33	.90	.90	.35**	-.09	-.18**	.31**	(.53)	—	—	—	—	—
JS	3.89	1.32	.72	.75	-.08	.00	-.10	-.09	-.06	(.59)	—	—	—	—
SBP	3.32	1.54	.75	.74	.08	.14*	-.13 ⁺	.06	.31**	.25**	(.60)	—	—	—
GBP	2.44	1.07	.66	.67	.08	-.13 ⁺	-.07	.06	.27**	.03	.10	(.51)	—	—
WE	5.63	1.21	.87	.87	.38**	-.08	-.18*	.36**	.50**	-.08	.16*	.25**	(.53)	—
TI	3.79	1.64	.83	.85	.04	-.09	.00	.05	-.54**	-.01	-.05	.04	.20**	(.66)

1.** $p < .01$; * $p < .05$; + $p < .10$; N = 2102. EDUC – Education Qualification; WEX – Work Experience (in years); PFP – Pay-for-individual-performance; JSEC – Job Security; SBP – Seniority-based Pay; GBP – Group-based Pay; WE – Work Engagement; TI – Turnover Intention.3. Values along the diagonal represent Average Variance Extracted (AVE) for the latent constructs.

measurement model comprising PFP, work engagement, and turnover intention showed good fit with the data (χ^2 [111] = 172.823, $p = .00$; $\chi^2/df = 1.55$; CFI = .97; GFI = .92; AGFI = .90; PCFI = .80; RMSEA = .04)).

Hypotheses

Table 2 summarizes the results of regression of PFP on work engagement and turnover intention. PFP was significantly related to work engagement ($B = .31$, $p < .01$) and turnover intention ($B = -.46$, $p < .01$).

Discussion

Based on the social exchange theory, our study contributes to compensation research by finding the relationship between pay for performance, employee engagement, and turnover intentions. As hypothesized the pay for performance is positively related to employee engagement and turnover intention. We found that pay for performance and employee engagement are positively linked and have an underpinning in the social exchange theory, supported by the work of Saks (2006), that employees will be engaged in their work when they perceive rewards are paid for their performance. It is further supported by the social exchange theory that employees feel obligated and reciprocate with higher levels of engagement when organization rewards them for their performance. Thus, pay for performance and engagement are related to each other, where a person is more engaged when his actions are rewarded. The second finding supports

Table 2 Unstandardized Regression Coefficients of Hypotheses Testing for Turnover Intention and Employee Engagement.

	Turnover Intention (TI) and Employee Engagement (EG)	
	TI	EG
Constant	6.63**	3.46**
Age	-.04	-.03
Gender	.34	-.23
Education	-.07	-.15
Work Experience	-.03	.00
Job Security	.15*	-.06.
SBP	-.01	-.04
GBP	.06	.16**
PFP	-.46**	.31**
R ²	.39	.33
F	F (8, 245) = 19.31**	F (8, 245) = 14.99**

Note: SBP – seniority-based pay; GBP – group-based pay; PFP – pay-for-performance N=254
(Eliminating data points having incomplete information on control variables)** p< .01. * p< .05. +
p < .10

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the relationship between the pay for performance and turnover intention. It is in line with the research done by Shaw and Gupta (2007). Pay for performance retains the competent employees, whose cumulative amount of pay increases with the course of time and decreases the turnover intention. The relationship is explained by the social exchange theory, when employees earn consecutively for their efforts, they feel valued, reciprocate by staying in the organization for a longer period of time.

Limitations& Suggestions

The study has some limitations that can be addressed in future research. The

cross-sectional data was collected for the constructs PFP, work engagement and turnover intention, and so any inferences regarding causality are limited. To understand the impact of PFP on employee attitude and behavior, longitudinal research is advised. Most of the data was self-reported; it gives a problem of potential bias. Another limitation of the data was that it was collected at a single point in time. Thus, in future, the studies can explore the impact of PFP on individual's behavior and attitude like organizational citizenship behavior and organizational commitment.

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