The effect of intrinsic and extrinsic rewards on the perceptions of middle level managers

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A. Introduction and aims

Recognition of the role that reward systems can play in gaining middle level management commitment to corporate goals has a long pedigree (Hopwood, 1974; Porter et al., 1975). Yet there are very few studies that provide evidence of how managers perceive these reward systems (Vancil, 1979; Kominis & Emmanuel, 2007). And even fewer that have explored whether these perceptions are similar or different across companies or countries (Chow et al., 1999).

This project addresses how reward systems are designed at different companies, located in different EU countries, as seen through the eyes of practising managers. In particular it looks at:

• whether middle level managers display a similar rewards preference
• whether the motivational impact of reward systems on performance is similar
• whether the antecedents of the reward system embedded in the management control system are perceived differently by middle managers, in different companies, in different EU locations.

The study reveals a marginal preference for intrinsic rewards, such as accomplishment and recognition, over extrinsic rewards like job promotion and salary increase. However, the direct impact of reward systems on motivation varies significantly across the research sites although higher motivation is generally associated with higher performance. The variety can be explained by the convergence of target attainments, performance measure accuracy, resulting in extrinsic rewards actually being given. The implications of the study for reward system designers, middle level managers and top management are tentative but offer initial avenues for future research.

B. The research summary

Data collection and survey analysis

An analytic questionnaire survey was administered to a cross-section of middle managers from three financial institutions in Greece (GR), Slovenia (SLV) and the United Kingdom (UK). The UK firm is a leading, publicly held, clearing bank. One of the UK’s oldest commercial banks, it has aimed at and achieved a high rate of growth with a remarkably low cost-to-income ratio over the years, which places it among the top five in the UK. The Slovenian bank is a state-owned financial and banking institution, which has maintained a leading position in the Slovenian banking market for the last thirty years, and is increasingly becoming a key regional player in south-east Europe. The Greek bank, initially established in the late 1920s by the state to support the development of the country’s agricultural sector, is today a rapidly expanding, diversified financial institution with a primary focus on banking, but is also active in insurance, leasing, asset management, mutual funds and credit cards.

The questionnaire was translated into the language of the target population and pilot tested at each financial institution, and subsequently administered through each company’s human resource division to the participant managers. In all three companies, the sample was specifically selected to consist of managers from the middle level of the organisation’s hierarchy, all evaluated and rewarded by the same, company-specific management control system (MCS), with a minimum of two years working experience in their current managerial position. In addition to the administration of the questionnaire survey, the study’s research design made provision for the collection of data that could be used for the authentication of the findings of the quantitative analysis. These typically included a review of the reward systems in place in each organisation, as well as closed presentation sessions with top HR executives from the Bank, and/or more open focus-group meetings with participants and non-participants in the research, where the study’s findings were presented and feedback was collected to ascertain the accuracy of the researchers’ interpretations.

The analysis of the data collected through the questionnaire survey was conducted through structural equation modelling (SEM) based on the maximum likelihood (ML) method (Byrne, 2001). A full explanation of this approach is given in Kominis and Emmanuel (2007).
C. Summary of findings

There is considerable agreement on the desirability of different rewards between the three companies:

- middle level managers perceive cash bonus, personal development and promotion to be part of their employment contract
- middle level managers do not necessarily value these rewards as the most important
- feelings of accomplishment and recognition appear to be highly desirable rewards
- all middle managers perceive motivation as related with performance
- the significant influences on motivation vary with the design of the specific company’s reward system.

1. The attainability of targets, the accuracy of performance indicators, the extrinsic and the intrinsic rewards have a direct and significant influence on motivation in Greece
2. The attainability of targets has a direct and significant effect on motivation in Slovenia
3. In the UK, extrinsic and intrinsic rewards have a lower-order direct impact on motivation, but the convergence of accurate performance indicators, attainability of targets, and transparency of performance-related rewards, appear to condition the impact of extrinsic rewards on managerial motivation.

D. Implications of the findings

1. Designers of reward systems
   - Employees and middle level managers, appear to perceive a menu of rewards to be available. Surprisingly, this did not seem to vary by company (or possibly culture) in these EU countries.
   - Middle level managers do not value cash bonus or personal development, but regard these as normal recompense for their current and future efforts.
   - A reward system which promotes identification of accomplishment and recognition appears to be required across the three companies.
   - Middle level managers, regardless of where their company is located in the EU, perceive motivation to influence performance in a positive manner.

2. Middle level managers
   - A mixture of extrinsic and intrinsic rewards are perceived as desirable but some more highly valued intrinsic rewards are not incorporated in the system.
   - The mixture/menu appears to be equally influential across all three companies (possibly cultures) regardless of reward system design.
   - The perceptions of reward system design appear to depend on the antecedents of the MCS. The perceptions of accuracy of performance indicators, attainability of targets and transparency with extrinsic rewards does vary.
   - The demographic profile of middle level managers may follow a pattern of valuing certain rewards more highly or lowly, over time.

3. Top management
   - The cost effectiveness of the reward system needs to be evaluated.
   - The relative influence middle level managers associate with desirable intrinsic rewards questions whether these can be incorporated in the formal system.
   - The accuracy of performance indicators, attainability of targets and transparency of rewards convergence may be possibly outweighed by identification of recognition and accomplishment.
   - Over time, and as middle manager personal, circumstances change. The reward system will need to evolve and accommodate the change in personal circumstances and reward preferences.
The effect of intrinsic and extrinsic rewards on the perceptions of middle level managers

E. Detailed analysis of the findings

Managerial perceptions of reward preferences

The analysis indicates that common patterns among managerial perceptions of desirable rewards exist across the three companies studied. In all three cases, intrinsic rewards, those that relate to inner feelings of achievement, self-fulfillment, self-actualisation, self-determination and competence that a manager may experience in the context of his/her job, appear to be valued marginally higher than the extrinsic rewards. This suggests that intrinsic rewards, which basically relate to the design and structure of the manager’s job environment, and the inherent variety of, interest in and control over the tasks and activities the manager has to carry out daily, may have at least as significant an impact on the motivation of middle managers as extrinsic rewards.

Tables 1 and 2 (see page 4) present a comparative analysis of managers’ reward preferences.

Further analysis indicates that:

• feelings of accomplishment and recognition rank among the three most valuable rewards in all three companies (see means of perceived reward values in table 2)
• cash bonus, promotion and salary increase rank among the three most frequently identified rewards in all three companies (see N of times rewards were identified in table 2)
• the monetary rewards typically included in companies’ reward systems (cash bonuses, stock options, and company benefit schemes) are perceived to be of a relatively smaller value to the intrinsic rewards in all three cases (compare means of perceived reward values in table 2).

These findings are of particular significance when one considers that managers in all three sites were allowed the freedom to identify and evaluate the set of rewards they themselves perceived available in their company. They suggest that companies which structure their reward systems solely around expensive monetary incentive schemes may not be maximising the motivational value of their compensation costs.

Looking for patterns within the sets of extrinsic and intrinsic rewards identified, one observes that:

• promotion is ranked consistently among the top two most desirable extrinsic rewards in all companies examined, whereas salary increase appears to be particularly desirable in the two partly state-owned companies (most desirable reward in GR, and third most desirable in SLV respectively)
• opportunities for personal development and more responsibility/authority are the intrinsic rewards most frequently identified by the UK, the Greek and the Slovenian sample of middle managers who took part in the study. The UK and Greek managers also view recognition as frequently preferred intrinsic rewards.

<table>
<thead>
<tr>
<th></th>
<th>Value of extrinsic rewards (EV)</th>
<th>Value of intrinsic rewards (IV)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>N</td>
<td>Mean</td>
</tr>
<tr>
<td>UK sample</td>
<td>225</td>
<td>5.57</td>
</tr>
<tr>
<td>Slovenian sample</td>
<td>68</td>
<td>5.52</td>
</tr>
<tr>
<td>Greek sample</td>
<td>241</td>
<td>6.18</td>
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</table>

Table 1: Preference for extrinsic vs. intrinsic rewards
The effect of intrinsic and extrinsic rewards on the perceptions of middle level managers

<table>
<thead>
<tr>
<th>Reward type</th>
<th>N</th>
<th>Mean</th>
<th>Standard deviation</th>
<th>Reward type</th>
<th>N</th>
<th>Mean</th>
<th>Standard deviation</th>
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</thead>
<tbody>
<tr>
<td>Work enjoyment</td>
<td>37</td>
<td>6.41</td>
<td>.76</td>
<td>Accomplishment</td>
<td>3</td>
<td>7.00</td>
<td>.00</td>
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<tr>
<td>Recognition</td>
<td>63</td>
<td>6.21</td>
<td>.81</td>
<td>Recognition</td>
<td>15</td>
<td>6.20</td>
<td>.77</td>
</tr>
<tr>
<td>Accomplishment</td>
<td>59</td>
<td>6.19</td>
<td>.88</td>
<td>Salary increase</td>
<td>28</td>
<td>6.11</td>
<td>.79</td>
</tr>
<tr>
<td>Profit sharing</td>
<td>63</td>
<td>6.11</td>
<td>.84</td>
<td>Work enjoyment</td>
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<td>6.00</td>
<td>.00</td>
</tr>
<tr>
<td>Promotion</td>
<td>170</td>
<td>5.92</td>
<td>1.04</td>
<td>Promotion</td>
<td>37</td>
<td>5.92</td>
<td>1.19</td>
</tr>
<tr>
<td>Responsibility/autonomy</td>
<td>145</td>
<td>5.90</td>
<td>.82</td>
<td>Responsibility/autonomy</td>
<td>28</td>
<td>5.82</td>
<td>1.02</td>
</tr>
<tr>
<td>Personal development</td>
<td>170</td>
<td>5.89</td>
<td>.92</td>
<td>Personal development</td>
<td>55</td>
<td>5.78</td>
<td>.88</td>
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<tr>
<td>Salary increase</td>
<td>93</td>
<td>5.89</td>
<td>1.12</td>
<td>Cash bonus</td>
<td>67</td>
<td>5.64</td>
<td>1.14</td>
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<td>Executive stock options</td>
<td>140</td>
<td>5.84</td>
<td>1.05</td>
<td>Companionship</td>
<td>7</td>
<td>5.29</td>
<td>1.38</td>
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<tr>
<td>Job security</td>
<td>75</td>
<td>5.76</td>
<td>1.36</td>
<td>Job security</td>
<td>12</td>
<td>5.25</td>
<td>1.29</td>
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<td>Stock options</td>
<td>51</td>
<td>5.69</td>
<td>1.26</td>
<td>Company benefits</td>
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<td>4.87</td>
<td>1.15</td>
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<tr>
<td>Cash bonus</td>
<td>206</td>
<td>5.67</td>
<td>1.13</td>
<td>Stock options</td>
<td>5</td>
<td>4.80</td>
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<tr>
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<td>5.64</td>
<td>1.28</td>
<td>Company benefits</td>
<td>117</td>
<td>4.56</td>
<td>1.25</td>
</tr>
</tbody>
</table>

Table 2: Results of structural analysis - UK vs. GR vs. SLV
The impact of rewards on managerial motivation and performance

Figure 1 provides diagrammatic representations of the significant relationships in each model examined. The examination of the model, which places expectancy-valence theory within a MCS framework, provides evidence of a significant (p<.01), direct relationship between the managers’ motivation and their performance. This finding is in line with the theoretical propositions and the empirical evidence available in the extant literature about the effect of motivation on performance (Lawler, 1994; Buchanan & Huczynski, 1997). It suggests that a closer examination of the factors that affect managerial motivation may be a useful way of increasing organisational effectiveness, particularly at managerial levels where the critical distance and the consequent information asymmetry make the implementation of other more direct monitoring and control devices too expensive or even infeasible.

The comparative analysis across the three cases studied provides evidence of a direct association between extrinsic and intrinsic reward value and motivation. In two of the three cases examined (UK and GR), managerial motivation is found to be significantly (p<.05) affected by both the managers’ perception of the value of the extrinsic rewards they receive, as well as by their perception of the value of the intrinsic rewards they enjoy in the context of their job. What is more, the impact of intrinsic rewards on motivation is found to be at least as significant as that of extrinsic rewards in both cases. These findings imply that companies may have significant motivational benefits to gain from systematically measuring their managers’ rewards preference and including in their compensation packages rewards that are highly desirable. Redesigning their managers’ task environments to enhance intrinsic motivational value is one plausible action suggested by the analysis.

Factors affecting the value and motivational impact of rewards

For extrinsic reward systems to be effective, middle level managers need to perceive the process as being transparent - the clarity of the link between expended effort and the reward being given, needs to be demonstrated. The link between reward transparency and the value of extrinsic rewards is confirmed in all three sites. This implies that the perceived value of extrinsic rewards, and consequently their motivational impact, are both inextricably linked with the way rewards are administered within the reward system. In order to acquire positive motivational properties, the rewards distributed by organisations through their incentive schemes may need to be performance-dependent and the link between performance and rewards to be perceived as transparent (Porter et al., 1975).

In all three countries, managers view the accuracy of performance indicators (Kominis and Emmanuel, 2007) as influencing the attainability of targets, and in the UK and Greek companies, performance indicator accuracy has a direct effect on reward transparency. Given the positive relationship identified in all sites between reward transparency and the value of extrinsic rewards, this suggests that the distribution of extrinsic rewards on the basis of incomplete and inaccurate performance measures, or with no transparent link to the manager’s measured performance, are likely to diminish the perceived attractiveness of these rewards and, by extension, their motivational impact.

In the Greek and Slovene companies, target attainability is found to have a direct and significant (p<.01) relationship with motivation. However in Greece there is also an accuracy of performance indicator association with managerial motivation at the p<.01 significance level, a finding not replicated in the UK sample. These differences are potentially explained by the specific features of the reward system design in each company.
Figure 1: Results of structural analysis - UK vs. GR vs. SLV
F. Final thoughts

The motivation of middle level management is a fascinating and largely uncharted area of study. Yet gaining this cadre’s commitment to corporate goals may depend on the reward system design.

This study suggests that companies in the same highly regulated financial sector have middle level managers with similar perceptions of desirable rewards. However, their views of the antecedents of the effective extrinsic reward system differ. There seems a challenge here for all these companies within the EU to embed intrinsic rewards in their efforts to motivate managers.

More questions than solutions have probably been prompted by this study but the relationships between rewards-motivation-performance are too important to be ignored.

Methodology and method

This study adopts a model generating, theory building approach to examine the above research questions (Jöreskog, 1993). An initial conceptual model of the process of motivation at the middle management level is developed by extending the traditional expectancy-valence (E-V) model with elements from the management control literature. This model is subsequently modified according to data collected from practising middle level managers from a variety of settings, so as to finally arrive at an empirically refined, and arguably more realistic, model of the effect of reward systems on managerial motivation and performance.

References


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