Impact of Pay-for-Performance on Work Motivation of Sales Personnel: A Case of Information Media Firms

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Abstract

The usage of pay-for-performance for the management of human resources is constantly growing. However, estimations about the efficiency of applying this are contradictory. The current paper describes the reasons for the contradictory results, suggests an expectations theory based model as an appropriate framework for analysing the pay-for-performance as motivator and presents results of an empirical research about the effects of pay-for-performance on motivation.

A reason for the contradictions lies in the fact that the pay-for-performance problems are based on different areas of research and its effectiveness depends primarily on management practices. Pay-for-performance is basically a stimulus, the purpose of which is to direct people's behaviour and influence their work motivation. Therefore, a prerequisite for creating and implementing effective pay-for-performance systems is using psychology and the principles about the mechanisms of human behaviour. The authors are of the opinion that one of such possibilities is a model based on expectations theory. The empirical research seeks to analyse the motivating effect of pay-for-performance on sales personnel and to study the role of pay-for-performance rates on motivation.

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*Key words:* Salary system, pay-for-performance, work motivation

1. Introduction

Growing pressure on higher efficiency has forced organizations seek any kind of means to achieve the targets and improve performance. One of such instruments in the field of human resource management is the increasingly growing application of pay-for-performance in compensation systems. Different studies provide different information on the range of usage of pay-for-performance. A general tendency is the increasing number of organizations where total compensation contain a part depending on
performance. According to the consultation firm Hewitt Associates, 50% of the firms used pay-for-performance in 1990, and in 2000 already 80% (Wiscombe 2001). An analogous tendency is also witnessed in Estonia. According to the salary survey conducted by the consultation firm Fontes in 2005, compensation policies of 91% of the firms in the survey include some kind of pay-for-performance.

Opinions about the effectiveness of pay-for-performance are different. The survey conducted by the Hewitt Associates in 2000 suggested that even these enterprises which have used the pay-for-performance system do not completely believe in its effectiveness: 21% of the firms said they do not believe its effect on improving work performance; 57% believed the effect was limited. A study conducted by the same firm in 1995 indicated that the pay-for-performance system had failed in 48% of the organizations (Wiscombe 2001).

Results of other surveys confirm the success of using pay-for-performance. An analysis of pay-for-performance programmes conducted in the USA in the second half of 1990s suggests that performance improves in approximately two out of three programs (Heneman, Ledford, Gresham 2000).

There are various reasons for the contradictory opinions and results. One may be definitely different methods of evaluation, differences in business sector, ambiguity of concepts used by researches. On the other hand, it can be assumed that application of pay-for-performance and its results can only be conflicting because the creating, implementation of the respective system and assessment of the results must often link conflicting interests of different stakeholders. The essence of contradictions lies in the fact that the field of pay-for-performance incorporates academic knowledge of different areas and their implementation in practice. The subject of pay-for-performance is related to psychology, economics and management. Many authors mention primarily mistakes in the implementation process and neglect of regulation mechanisms of human behaviour in building up pay-for-performance systems as the main reasons for contradictory results and arguable effect (Pfeffer 1995, 1998; Luthans, Stajkovic 2001; Rynes, Gerhart, Minette 2004).

Pay-for-performance is by nature an instrument for influencing people’s motivation. This presumes that the pay-for-performance schemes shall be oriented to people as performers of work and based on the psychological knowledge of the regulation mechanisms of human behaviour. On the organizational level, implementing pay-for-performance must yield better economical results. Therefore, the problems of compensation are influenced by arguments and concepts of economics.

From the aspect of economics, the usage of pay-for-performance is based on the theory of agent (Jensen, Mecling 1976). The agent theory is based on the opinion that the interests of employer/owner and employee are contradictory and that it is possible to join the employers’ and employees’ interests primarily with financial incentives or based on salaries and pay-for-performance. The agent theory is used by most of the studies that discuss the impact of pay-for-performance on firm’s performance as a whole.

A link between the desired economic performance and activity of people as performers of the work is management. In the context of effectiveness of pay-for-performance, the role of management is primarily to establish a system that satisfies both parties and to implement it reasonably. In practice this is associated with finding ways and measures for the assessment of work contribution.

The authors agree that the arguable effectiveness of the pay-for-performance systems is caused by the practice characterised by one-sided approach from economics.
aspects and in particular, weaknesses of management practices. The basic principles of knowledge in psychology are neglected or their impact is underestimated (Pfeffer 1998; Beer, Cannon 2004). For creating a well-working pay-for-performance system it should be based on human being as an agent and on the knowledge about the mechanisms that regulate human behaviour (Luthan, Stajkovic 1999; Pfeffer 1995; Rynes, Gerhart, Minette 2004).

This article will analyse the conditions for using pay-for-performance based on the mechanisms that regulate human behaviour. The authors suggest an approach according to which the pay-for-performance as a motivator should be discussed in the frames of the expectations theory (Vroom 1964; Porter, Lawler 1968). An empirical study of the motivating power of pay-for-performance was conducted among sales personnel of information media enterprises. The study sought to identify the effect of pay-for-performance rate as a reinforcement on people’s motivation and on the current system of pay-for-performance. The authors raised 2 work hypotheses:

Hypothesis 1: based on that sales work of information media enterprises is by nature a classical individual sales work, the pay-for-performance is for workers an essential source of motivation.

Hypothesis 2: Based on that pay-for-performance in terms of the expectations theory is a reinforcement of the chosen behavioural model, the pay-for-performance rate affects the employees’ opinions about the motivating power of pay-for-performance and the system of incentive pays.

2. Analysis of the Problem

Pay-for-performance is used for increasing the level of effort and direct people to act in a desired way, or to influence people’s behaviour. The patterns of changing human behaviour are described by learning and motivation theories. Therefore it is reasonable to analyse pay-for-performance as a motivator through the models describing development of learning and motivation.

The behaviouristic theory states that learning occurs through positive reinforcement: people want to repeat activity that was positively reinforced. In the context of behaviouristic theory, pay-for-performance can be discussed as an external stimulus, on the one hand, and as a positive reinforcement, on the other hand (Sahakian 1984). A possibility of earning pay-for-performance should direct people to make efforts for that. Receiving pay-for-performance is for a person a positive reinforcement signalling that he/she has acted properly and it is useful to exert effort.

A person’s particular behaviour does not, however, develop only as a reaction to a stimulus and each positive reinforcement. According to cognitive learning theory, a person learns through interaction of thinking and cognition: an important role in shaping human behaviour is played by the person’s subjective opinions about potential outcomes (Bandura 1986). Thus, the effectiveness of pay-for-performance as a director of efforts depends on its value for this person and therefore we cannot assume that pay-for-performance is an equally strong motivator for all employees.

Investigation confirms the validity of both viewpoints. Pay-for-performance is a stimulus and earning this a positive reinforcement that increases people’s efforts and through these productivity of work. Meta-analyses of the projects to increase labour productivity and of their results have indicated that using of an individual pay-for-performance increases labour productivity much more than introduction of different
elements of job enrichment (Locke, Feren, Mc Caleb, Shaw, Denny 1980; Guzzo, Jette, Katzell 1985).

The importance of pay-for-performance as a motivator and its effect that directs the efforts are not unambiguous. Researches have confirmed the differentiated effect of pay-for-performance depending on personal characteristics (Stewart 1996), person’s productivity of work (Trevor, Gerhart, Boudreau 1997), personal abilities and previous achievements (Trank, Rynes, Bretz 2002).

The development of a person’s work motivation based on his subjective values and reinforcement as a whole is discussed by the expectations theory (Vroom 1964; Porter, Lawler 1968). According to the expectations theory, a person’s motivation to work and make efforts depend on his expectations of the reward and past lessons of receiving the expected reward. The expectations theory does not determine the content of the expectations or kind of reward, but describes the linkage between the expectations and the outcome as the basis for creating or destroying motivation. The authors are of the opinion that the expectations theory is a suitable generalised model, which helps to understand the role of pay-for-performance as a potential motivator, on the one hand, and can support creation of effective pay-for-performance systems in practice, on the other hand. In terms of the expectations theory, pay-for-performance induces people to exert effort when they are interested in bigger earnings, believe that stronger efforts bring bigger reward and pay-for-performance fulfils their expectations. Pay-for-performance as a motivator in the context of expectations theory is explained in Figure 1.

Pay-for-performance as such is a reward for efforts made by employees. From the aspect of learning the reward to be received may be both negative reinforcement – the size of pay-for-performance is not up to expectations, and positive reinforcement – pay-for-performance is up to expectations. Depending on the nature of the reinforcement, the ensuing behaviour and motivation of people is different. As the repertoire of possible expectations and behaviours is wide and influenced in addition to reinforcement by many other factors, it is difficult to determine unambiguously the ensuing behaviour. Based on the theory of equity (Adams 1965) it may be assumed that pay-for-performance that does not fulfil expectations probably reduces people’s wish to exert effort, increases the likelihood of leaving etc. A pay-for-performance that fulfils expectations is a sign that working hard was worth the effort and with great likelihood motivation to work hard remains or grows. From the above we can draw a conclusion that the pay-for-performance rate may be a factor that determines the effectiveness of the pay-for-performance system. Many authors have stated its low level in absolute terms (Heneman 2004; Locke 2004, Miceli, Il Jae Jung, Near, Greenberger 1991) or too low proportion in total pay (Rynes, Gerhart, Minette 2004) as one reason for failures of pay-for-performance applications.

Based on this model it is possible to determine the critical factors that must be taken into account while creating an effective pay-for-performance system.

First, for employees who receive pay-for-performance financial incentives should be relatively more important than other motivators; secondly, these employees must believe in the possibility of earning more with better work and thirdly, the pay-for-performance rate must fulfil their expectations. Based on these factors we can define the requirements for jobs where the respective conditions are more likely to be fulfilled.

James Baron and David Kreps (Baron, Kreps 1999) suggest that pay-for-performance is more likely to work as an essential force that influences behaviour in jobs that are simple, individual in character and therefore enable people to feel direct connection between their effort and result and where results are unequivocally
measurable. When the listed conditions are fulfilled it may be assumed that pay-for-performance works as an instrument directing people’s work-related behaviour.

Figure 1. Mechanism of the Motivating Power of Pay-for-Performance in the Expectations Theory Context

3. Empirical Study

A survey to analyse the motivating power of pay-for-performance was conducted among the sales personnel of Estonian information media enterprises. 5 organizations participated in the survey, which possess 86% of the Estonian information media market and employ approximately 80% of the sales personnel in the respective field.

The job of the sales personnel is to sell various information media products to enterprises and organisations. The work is mainly classical „piece-work” and conforms to the requirements that are traditionally regarded as a precondition for pay-for-performance to be effective: it is relatively simple (training lasts approximately two weeks) and does not assume any formal professional preparation; it is unequivocally measurable, individual in character. Results of each individual worker have a direct effect on firm’s performance (firms’s income depends on the number and value of
contracts concluded) and therefore, employer is directly interested in directing people to exerting greater effort. Mobility of the sales personnel is big in all enterprises covered by the survey, amounting to 50-60%.

A questionnaire was used as a research method. The questionnaire consisted of four different parts. Questions in part one were about the size of basic salaries and pay-for-performance, the criteria and frequency of pay-for-performance payments. The first part of the questionnaire enabled to get general information about the current salary system and real basic salaries and pay-for-performance. The second group consisted of questions asked with the purpose to find out employees’ opinions about the adequacy of using pay-for-performance in the context of particular jobs: they studied employees’ opinions about the measurability of their work results and possibilities of influencing these by them, transparency of the principles of pay-for-performance and involvement of employees in working out the system. The third group consisted of questions asked with the purpose of identifying employees’ opinions about the current system and its motivating power. A 5-point scale was used in the second and third part of the questionnaire.

The questionnaire also contained a fourth part, which enabled respondents to define problems involved with the pay-for-performance system. There were a total of 18 questions in the questionnaire. The questionnaires were sent to respondents via the Internet and on paper. These could be completed both on paper and over the Internet. A total of 141 questionnaires were sent out to all sales workers of enterprises involved in the survey. 96 completed questionnaires were returned; hence the response rate was 68%.

An overall objective of the survey was to find out the employees’ opinions about the current pay-for-performance system and analyse its motivating effect in a field of activity that by nature is suitable for introducing pay-for-performance. A concrete research task was to identify the effect of pay-for-performance rate as a reinforcement on people’s motivation and on the current pay-for-performance system.

4. Results

Description of the Target Group in the Survey

77% of the respondents were women and 23% men. 47% of the respondents were aged 21–30 years, 22% aged 41–50 and 17% 31–40 years old. 69% of the respondents had been employed by the firm less than two years and 12% were on probation.

The questionnaire provided the following ranges of basic salary and monthly pay-for-performance rates: less than 2999 kroons, 3000–4999 kroons, 5000–6999 kroons, 7000–8999 kroons, 9000–10999 kroons and over 11,000 kroons. The respondents had to tick off their monthly basic salary rate and estimate their monthly average pay-for-performance during the past six months. On the basis of the pay-for-performance rate, the respondents were divided into the following groups: 21% of the respondents earn less than 2999 kroons of pay-for-performance, 27% 3000–4999 kroons, 25% 5000–6999 kroons, 8% 7000–8999 kroons, 13% 9000–10999 kroons and 5% over 11,000 kroons. The distribution of the respondents on the basis of basic salaries was as follows: 31% of the respondents earned less than 3000 kroons of basic salaries, 43% received 3000–4999 kroons, 15% 5000–6999 kroons, 5% 7000–8999 kroons, 2% 9000–10999 kroons and 3% over 11,000 kroons. The distribution of sales personnel covered by the survey depending on the basic salary and pay-for-performance rates is depicted on Figure 2.
As we can see, the basic salary and pay-for-performance rates vary in a quite large scale. Examining the distribution of the respondents between possible pay groups, we can still make some generalisations. The basic salary rates are mostly in the lower part of the scale: 74% of the respondents earn a basic salary of less than 4999 kroons. And only 10% of the respondents receive a basic salary of more than 7000 kroons. The pay-for-performance rates divide relatively more evenly: 48% of the respondents earn up to 4999 kroons and 26% of the respondents over 7000 kroons as pay-for-performance. As the sample frame is relatively small, then in further analysis we reduced the pay-for-performance groups and in the analysis of the effect of pay-for-performance rate we used four groups of pay-for-performance: up to 2999 kroons, 3000–4999 kroons, 5000–6999 kroons and over 7000 kroons. The distribution of the respondents between these wage groups was relatively even: 21% earned less than 2999 kroons as pay-for-performance, 27% 3000–4999 kroons, 25% 5000–6999 kroons and 26% of the respondents over 7000 kroons as pay-for-performance.

**Overall Opinions about the Current Pay-for-Performance System as a Motivator**

The participants in the survey were asked to evaluate the impact of different factors on their motivation. The factors regarded as typical motivators were listed: content of the job, pay-for-performance, relationships with colleagues, career opportunities, training, appreciation of immediate manager, relationships with immediate manager and colleagues, working conditions, social events in the firm. The strongest motivator for the respondents was pay-for-performance: 91% estimated pay-for-performance to be extremely or rather motivating. The second strongest motivator for the respondents was relationships with colleagues (88% regarded these as highly or rather motivating) and appreciation of immediate manager (75% of the respondents estimated appreciation to be highly or rather motivating). Career opportunities had the smallest motivating power: 38% estimated these to be very or rather motivating. Compared with the other factors also the work itself was estimated to be relatively less motivating: 56% of the respondents regarded this motivating or rather motivating.

Pay-for-performance is in the opinion of respondents an effective instrument that makes them work harder. 60% of the respondents said that pay-for-performance definitely makes them exert effort and 35% that it rather makes them exert effort.
On the basis of the opinions expressed by respondents we can state that work assignments are suitable for applying pay-for-performance to: 67% of the respondents regarded work results as clearly measurable and 21% as rather measurable. The respondents estimated the principles of calculating pay-for-performance to be clear for them: 66% said that they understood the principles of calculating pay-for-performance and 21% that they rather understood them.

The respondents were asked to evaluate overall satisfaction with the current salary system. 20% of the sales personnel in the survey were completely satisfied and 54% were rather satisfied.

Given on the opinions expressed by the respondents, the current pay-for-performance system is up to the expectations of the sales personnel of information media enterprises covered by the survey, it is in compliance with the nature of the work and the prospect to earn through pay-for-performance more is a significant motive for working harder.

Participants in the survey were asked to list problems that they have confronted in connection with pay-for-performance. 35% of the respondents mentioned irregular incomes, 31% stress, 15% competition between colleagues, 9% misunderstandings with colleagues and 10% misunderstandings with immediate manager.

The respondents were also asked to identify the circumstances that they think hinder them to achieve better work results. The list of factors that restrict higher efficiency was prescribed and contained a total of 13 different factors. 36% of the respondents mentioned too high targets as the main obstacle, 32% laziness, 25% insufficient work experience and 20% problems with communication.

One question was about the preferred salary system in case the employee could choose one. 44% of the respondents want such a compensation system where pay-for-performance and basic salary proportions were equal, 42% preferred as high proportion of basic salary in total pay as possible, 13% preferred higher proportion of pay-for-performance and 4% wanted fixed monthly salaries that do not depend on performance.

Despite the positive expectations for pay-for-performance and relatively high satisfaction with the current wage system, 46% of the respondents would prefer rather a higher proportion of basic salaries. Such expectations probably arise from the problems involved with pay-for-performance – above all uneven income level and stress.

**Analysis of the Impact of Pay-for-Performance Rate**

The rate of pay-for-performance is for a person a reinforcement to his efforts and may influence his opinions about the motivating power of pay-for-performance, his will to exert effort, overall satisfaction with pay-for-performance and his expectations of the compensation system.

In order to find out whether the pay-for-performance rate affects opinions about different aspects of using pay-for-performance, an ANOVA analysis was conducted. The factor trait was groups of pay-for-performance (4 groups). To determine the impact of pay-for-performance rate we selected 6 questions from the questionnaire, which were associated with opinions about the motivating power of pay-for-performance and satisfaction with the wage system. The results are provided in Table 1.
### Table 1. Impact of the Pay-for-performance Rate on Its Motivating Power: ANOVA Analysis

<table>
<thead>
<tr>
<th>Factors*</th>
<th>A</th>
<th>B</th>
<th>C</th>
<th>D</th>
<th>F_emp</th>
<th>F_crit</th>
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<td>N</td>
<td>M</td>
<td>V</td>
<td>N</td>
<td>M</td>
<td>V</td>
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<tr>
<td>Results are measurable</td>
<td>19</td>
<td>1.47</td>
<td>0.59</td>
<td>26</td>
<td>1.65</td>
<td>0.72</td>
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<tr>
<td>Principles of PFP are</td>
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<tr>
<td>clear</td>
<td>20</td>
<td>1.55</td>
<td>0.89</td>
<td>25</td>
<td>1.76</td>
<td>1.27</td>
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<tr>
<td>Motivating impact of</td>
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<tr>
<td>PFP is strong</td>
<td>20</td>
<td>1.55</td>
<td>0.58</td>
<td>26</td>
<td>1.54</td>
<td>0.74</td>
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<tr>
<td>I am satisfied with PFP</td>
<td>20</td>
<td>3.2</td>
<td>1.22</td>
<td>26</td>
<td>2.85</td>
<td>0.94</td>
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<tr>
<td>motivating</td>
<td>20</td>
<td>2.6</td>
<td>0.57</td>
<td>24</td>
<td>2.58</td>
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<td>salary system**</td>
<td>20</td>
<td>2.6</td>
<td>1.09</td>
<td>25</td>
<td>2.36</td>
<td>0.82</td>
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</table>

A, B, C, D: Pay-for-performance rates: A: up to 2999 kroons; B: 3000-4999 kroons; C: 5000–6999 kroons; D: over 7000 kroons

N: sample size; M: mean value; V: variance

*: a 5-point scale was used for evaluation: 1: completely agree, 5: do not agree

**: scale of options: 1-as high proportion of pay-for-performance as possible; 4: only basic wage
As a result of the ANOVA analysis we can state that based on this survey data the pay-for-performance rate does not influence people’s opinions about the motivating power of pay-for-performance. Opinions of people belonging to different pay-for-performance groups about pay-for-performance are not statistically different in the respective group of respondents

5. Discussion

Work motivation is complicated by nature, changing over time and its existence or absence depends on many factors. Based on the above surveys, we can divide the factors that influence work motivation into four groups: personal traits and attitudes; nature of work; organisational environment, primarily culture of organisation, organisation of work and everyday management practices; and social environment as a whole. To understand motivation and to influence it we must take into consideration all the listed factors: the will of a particular person in a particular organisation performing particular assignments to exert effort is a result of these different effects at a certain moment of time. Motivation including work motivation “belongs” to an individual and therefore the selection and implementation of the motivating instruments must be based on the individual and the starting point should be the mechanisms regulating human behaviour. One issue that in recent decades has split the academic researchers and practicians into different „camps”, is the issue about the role of money in influencing employees’ motivation.

Sara Rynes, Barry Gerhart and Kathleen Minette conducted a meta-analysis of the surveys presenting the impact of money as a motivator and reached a conclusion that the motivating effect of salaries has been verified in many more studies than we could guess on the basis of common opinions of consultants and managers (Rynes, Gerhart, Minette 2004). Salary is an essential motivator for people, which makes them work harder and influences their decisions as to take the job or leave the job. However, this does not mean that money is the only motivator and of equal importance for all people. The above referred research contained a survey of the investigations of the motivating role of pay-for-performance and the conclusions were the same: salaries depending on performance influence people to work harder and a pay-for-performance system improves enterprises’ performance. However, here the impact also has some limitations: pay-for-performance has the desired effect in case it is appropriate for the job and is a value for people performing that job. Various studies have identified that a possibility to earn pay-for-performance works for particular people as a job selection criterion and therefore a motivating pay-for-performance system creates preconditions for hiring people who are motivated to exerting effort and achievement (Harrison, Virick, Williams 1996; Turban, Keon 1993).

A suitable theoretical construction that would enable to analyse preconditions of the motivating effect of pay-for-performance and determine which conditions are necessary for this to be effective, is the expectations theory. The object of the empirical research for studying the motivating effect of pay-for-performance was selected by the authors based on the expectations theory model. It is a sales organisation. Sales organisations traditionally use the pay-for-performance system and it may be assumed that this kind of organisation is chosen for employment by people who are interested in earning pay-for-performance. The nature of work in these organisations enables to link employees’ efforts to performance and pay-for-performance may be a direct reinforcement for the efforts. Results of the research confirm hypothesis 1 raised by the
authors: pay-for-performance is an important source of work motivation in classical individual sales work. For sales personnel of the organisations studied by us pay-for-performance is a significant motivator and makes them work harder; satisfaction with the pay system is high. The research results did not confirm hypothesis 2: the pay-for-performance rate did not influence employees’ opinions about its motivating power and about the pay-for-performance system. Although the pay-for-performance rates differ in a large scale, no demotivating effect of low pay-for-performance rates as a possible negative reinforcement was observed. People receiving different pay-for-performance had not different opinions about pay-for-performance as a motivator and satisfaction with the pay-for-performance system. The pay-for-performance rates did not influence expectations of the salary structure either. On the basis of this survey it is not possible to draw conclusions about the reasons for the strong motivating power of pay-for-performance. This may be due to the fact that basic salaries are relatively low and the respondents’ answers were guided by the understanding that in order to earn expected total compensation they simply have to work harder to receive higher pay-for-performance. The positive opinion about pay-for-performance as a motivator raises a problem of the reasons of high labour turnover: in organizations covered by the survey it was between 50 and 60%. High workforce mobility is often regarded as a signal of an ineffective pay system. In the context of these firms and based on the research conducted by us, the critical factor of workforce mobility should be neither the pay-for-performance system nor the pay-for-performance rates. The reasons may be rather the nature of work and demographic characteristics of the employees. Based on the survey results, the content of the work has relatively less motivating power and career opportunities are few. At the same time, 47% of the respondents are aged 21-30 years. A relatively simple job that offers no career opportunities may be a critical reason for young people to change job.

For interpreting the research conducted by us one must accept some limitations. One limit is a relatively small sample size (96). The small sample size has a major effect on the results in the evaluation of the effect of pay-for-performance: comparable salary groups consisted of 19–26 respondents. Another limitation is the method used by us. A questionnaire is a relatively limited instrument for studying motivation. To get more reliable data on the motivation processes the questionnaires should be definitely supplemented with qualitative research.

References


