

IMPROVING STAFF PERFORMANCE: Experimental evidence of the effectiveness of performance pay and motivational messages

Paying people to work harder can backfire, but combining it with a motivational speech works really well. That is the central finding of experimental research by **Ola Kvaløy**, **Petra Nieken** and **Anja Schöttner**, to be presented at the annual congress of the European Economic Association in Mannheim in August 2015.

The study ran an experiment in which people had to enter data into a spreadsheet. Everybody was given a fixed wage, but some people were also given extra pay based on their performance. Within each group, some people were also given a motivational speech before they started.

The researchers find that paying people more for their work actually causes output to fall, but combining it with a motivational speech causes it to rise by 20% while reducing the proportion of mistakes by 40%. The authors conclude:

‘Our results have important implications for firms. First, communication is crucial to prevent monetary rewards from backfiring. Second, small piece rates, making up only 10% of the total salary, can be effective when they come with a motivational speech.’

More...

The question of how to motivate employees is essential for companies. Should companies use monetary rewards such as paying an extra bonus or a piece rate? Or should they rely on the leadership skills of their managers to increase the motivation of the workforce? Is it effective to combine both instruments or do they cancel each other out?

Kvaløy, Nieken and Schöttner show in a field experiment that the combination of a piece rate and a very short motivational speech by a manager can increase the output level substantially. While introducing a piece rate system actually led to an output reduction, combining this piece rate with a short motivational speech led to an output increase of 20%.

The quality of work was also improved considerably. The ratio of mistakes to produced output was reduced by 40% if the piece rate was accompanied by the motivational speech. The researchers refer to this phenomenon as the ‘hidden benefit of rewards’.

Using monetary rewards such as performance pay to motivate employees is a standard approach in many companies. But performance pay can also crowd out intrinsic motivation to work on a task leading to a ‘hidden cost of reward’. But intrinsic motivation is not only affected by money. It can also be triggered by managers and company leaders. A very simple leadership technique to evoke intrinsic motivation is by giving a motivational speech.

While both instruments, money and leadership techniques are used in companies, little is known about their interaction. It is crucial for companies to understand the effects and the interplay of both instruments when deciding about the best strategy to motivate

their workforce. Should a company spend resources to develop the leadership skills of their managers or should they invest in a performance pay plan?

So the central questions are will performance pay undermine a leader's effort in motivating employees? Or does performance pay instead complement and enhance the effect of a manager's leadership efforts?

To study these questions, Kvaløy, Nieken and Schöttner conducted a field experiment in a controlled work environment. The task was to enter sports data into a database. The researchers varied the payment. All participants (students) received a fixed wage but some also received an additional small piece rate based on their performance. In addition, part of the participants under either payment scheme were exposed to some simple form of motivational speech before they started working.

With this design, the researchers can isolate the effect of introducing performance pay or giving a short motivational speech. But they can also study the interaction between both instruments.

The motivational speech improves performance only when accompanied by performance pay (piece rate). Moreover, the piece rate alone indeed leads to lower performance, but this detrimental effect disappears if it is accompanied by a motivational speech. The data support the 'hidden benefit of monetary rewards': complementarity between performance pay and the motivational speech.

These effects also carry over to the quality of work. Performance pay alone leads to more mistakes. Adding a motivational speech makes the difference. The effects are strong. In treatments with performance pay, the motivational speech increases output by about 20% and reduces the ratio of mistakes by more than 40%.

Those results have important implications for company practices:

- First, communication can be crucial to preventing monetary rewards from backfiring.
- Second, small piece rates, constituting only 10% of the total salary, are rather effective when they are accompanied by simple forms of a motivational speech.

ENDS

Hidden Benefits of Reward: A Field Experiment on Motivation and Monetary Incentives
Ola Kvaløy, Petra Nieken, and Anja Schöttner (published in the European Economic Review, 2015)

Contact:

Petra Nieken: +49 721 60842877