# Varied impacts of compensation on employee performance in the public sector

## A case of the Premier Medical Aid Society of Zimbabwe

**C Hofisi**
Department of Development Studies
University of Fort Hare

**S Mago**
Department of Development Studies
University of Fort Hare

## ABSTRACT

***Compensation administration in a highly inflationary environment has proved to be a major challenge to most organisations. While employees need reasonable amounts of disposable income on their side, organisations need super profits for their sustenance hence the paradoxical nature of compensation administration. This study is meant to ascertain the relationship between compensation and employees' performance. The study hypothesises that satisfactory compensation enhances employee performance. A case study approach was used to ascertain this relationship. Interviews with key informants in a sample drawn from a population of the parastatal's employees were administered. This article presents the following arguments. Compensation can only have a positive impact on employee performance if it is not only linked to employee performance but democratised to incorporate the input of employees, properly installed and maintained. The influence of compensation administration on employee performance can be applicable to those who derive their motivation from it. Therefore, to say that compensation drives employees to perform may be an overstatement and fictitious. Human needs are dynamic in nature let alone complex. For the sake of sustainability, a remuneration strategy should also clarify the relationship between salaries, wages and benefits to the key success factors of the organisations. Issues of equity and fairness of compensation should be adhered to for compensation to achieve desired results. For remuneration to drive the performance of employees it should clearly portray those behaviors that need to be rewarded.***

## INTRODUCTION

A satisfactory compensation administration system has proved to be a thorny issue in the past decade in Zimbabwe due to a hyperinflationary environment. This led to widespread strikes and in some instances company closures or work stoppages. It is, therefore, imperative especially against such a background to analyse the relationship between compensation administration and employee performance. The Premier Service Medical Aid Society has been performing well. The purpose for this research is to analyse whether their success is attributable to a satisfactory system of compensation administration.

It is interesting to note that while a comprehensive compensation administration system may be an insurmountable task to some organisations due to financial costs involved, employees will not be motivated to perform well if it is not effectively implemented. However, without rushing to prematurely draw some conclusions it is imperative to establish some nexus between compensation administration and its bearing on employee performance. Given the dismal failure of parastatal organisations to perform to expectations, in Zimbabwe, it has been argued that high salaries and attractive benefits are the pre-requisite for excellent employee performance, it is however necessary to test that hypothesis.

The research mainly investigates the relationship between compensation administration and employee performance. The research question posed is: Does a comprehensive system of compensation administration lead to high employee performance? While compensation administration is a complex and dynamic concept, emphasis will be on whether it is a pre –requisite for excellent employee performance that inevitably leads to high organisational productivity or *vice versa*.

## COMPENSATION AND EMPLOYEE PERFORMANCE: CONCEPTUAL AND THEORETICAL FRAMEWORKS

Compensation refers to a wide range of financial and non-financial rewards to employees for their services rendered to the organisation; these rewards include paid vacation, insurance, maternity leave, free facility and retirement benefits (Chhabra 2001:279). Implied in the definition is the fact that compensation comes in various forms that is financial and non-financial. Chhabra, (2001:329) argues that performance of employees constitutes their personalities, contributions and potentials. Fredrick Taylor's Scientific Management Theory advocates, what he termed *a piece rate pay*. He further contends that a system of pay must solely be based on individual output by an individual worker. Implied in this argument is that compensation is directly linked to employee performance. Hertzberg's two factor theory also links compensation together with employee performance. He identifies one's job salary as an extrinsic factor as one of the pre-requisites for good employee performance. Aswathappa (1997: 269) postulates that there are theories of remuneration which are reinforcement, expectancy theory and equity theory. The reinforcement and expectancy theory postulates that high employee performance followed by a monetary reward will make future employee performance more likely. A high performance not followed by a reward will make its recurrence unlikely in future. The equity theory posits a fair day work for a fair day pay as well as equity in pay structures.

The concept of salaries and or wages is one of the most commonly used in organisations including the Premier Medical Aid Society in Zimbabwe. It is however important to note that it has varied impacts on employee performance. Dessler (1984:494) argues that salaries are often tied to seniority rather than to performance, which can be demotivating to potentially high performing employees. The issue of inequality both internal and external plays a pivotal role in determining the influence of salaries and employee performance. There is need for equity if salaries have to be effective. Aswathapa (1997:267) posits that fixed remuneration is difficult to motivate workers since it removes fear of insecurity in the minds of employees while Lanz (1988:52) also argues that salaries that are perceived to be too low can act as a stronger demotivator since it is seen as an indication of an employee's worth to the company. Therefore, it is those satisfactory salaries that have a positive bearing on employee motivation. Wilson (1992:49) asserts that in issues of employee performance, pay plays a critical role in accentuating performance.

Incentives, as defined earlier on, constitute financial rewards paid to workers whose production exceeds some predetermined standard. These may be piece rate, paid to employees for each piece produced by employees. This system of pay applies to Taylor's scientific management. These types of incentives have a great deal of influence on employee performance since they seek to tie productivity or profitability to pay. It implies that the greater the effort that is applied the more the employee will be compensated. These have been criticised since they lead to many compromises on quality. Employers may also arbitrarily raise production standards whenever workers earn excess wages.

Stoner *et al*. (1995:396) comments on the other side of rewards/incentives. He argues that the idea of rewards can be questioned. Kohn (1993:11) also asserts that any approach that offers reward for better performance is destined to be ineffective due to the following reasons: they are a form punishment, since when you do not get them it is like being punished; rewards destroy relationships while real co-operation and sharing are necessary; rewards focus on outcomes and can ignore reasons. The work place can be turned into a game show. Aswathapa (1997:267) also contends that since incentives are variable rewards granted according to variations in the achievement of specific results, their primary advantage is the inducement and motivation of workers for higher efficiency and greater output.

Aswathapa criticises incentives in that they only work if they are appropriate to the type of work and workers, linked to efforts, well-defined and if they have an understood formula, properly installed and maintained. Workers should also have a reasonable control over efforts and rewards; they are also disincentives for non-performers. Moreover, this scheme may be difficult or impossible to implement due to technical considerations or psychological circumstances, which might be prejudicial to output.

Pearson (1999:45) asserts that clearly, other things being equal organisations that can motivate their employees are more likely to achieve their organisational goals while Peters and Waterman (1980:2430) contend that almost every executive agrees that people are the most important assets. Blunt and Jones (1992:280) also argue that economic pay off from work may frequently be the main focus of concern rather than rewards stemming from prestige or intrinsic rewards. Therefore, incentives are not only designed to attract people who are capable but also to motivate them towards superior performance and retaining them over an extended period of time.

Against such a complex background of the varied effects of compensation in employee performance one can note that while compensation indeed affects performance of employees designing the same has several implications. Pre–requisites such as chauffeur driven car, corporate aircraft, home security, company apartments, club membership and entertainment may also serve the purpose of attracting as well as retaining employees (Aswathappa 1997:282). It is important to note that employees in their positions may work hard to be retained in their positions thereby boosting their performance.

Remick (1981:371) argues that open pay improves employee motivation especially those employees concerned with equity while secrecy arouses suspicions and demotivates employees. However, it must also be emphasised that while secrecy prevents much quibbling, openness could lead to unnecessary strain and dissatisfaction among employees as well as some misunderstanding and petty complaints (Miner 1974:12). Thus, compensation administrators should have the shrewdness to discern or scan their work environment for them to determine whether the concept of secrecy should prevail or openness should be introduced otherwise their efforts will not come to fruition. Flippo (1980:249) argues that the ability of companies to pay also shapes the compensation paid to employees.

Against this complex background, one can note that there is no one best way of compensating employees or dealing with the compensation problem (Anderson 1990:28). Compensation is a complex problem facing companies especially in times of economic recession or economic instability. Remick (1981:371) contends that employees must be made to believe that greater efforts results in greater reward. Thus if employees see a direct relationship between reward and effort then greater effort will result. Therefore, one can note that this is a deliberate strategy that is meant to solicit good performance from the employees.

## Method

This was largely a qualitative research which is appropriate when the research focuses on phenomena and interpret it on the basis of meanings attached to it by people (Swanson & Holton 1997:3).

## Target Population

The organisation from which the sample was chosen is a medical aid society which is part of a group of companies. The study was directed at senior, middle, junior leadership and shop floor level employees. These were the categories from which key informants were randomly chosen for the administration of in-depth interviews.

## Measurement

The perceptions of the target population and their opinions about the extent to which compensation impacts on employee performance were determined and obtained through in-depth interviews which were held with key informants. The interview schedule covered issues such as performance expectations, compensation awarded; awards, how compensation awarded impacted on employee performance and whether compensation awarded was linked to employee performance. Open ended questionnaires were also administered to key informants from the Premier Medical Aid Society. This method is crucial since it provides an in-depth analysis of phenomena. It is also very convenient since short and few effective questions can be asked to respondents without wasting much time.

The semi-structured interviews were also used in conducting the research. These are important since interviews enjoy a high response rate. The researcher can ferry out information by explaining and clarifying questions. Thus, both primary and secondary sources of data were used.

## RESULTS

### Organisation's compensation policy

The study found that the PSMAS compensation policy is implemented by the human resources manager together with the administration manager acting on the advice of the CEO. An interview held with one of the middle managers revealed that the duo were competent in the execution of their duties. Their competence was evidenced by their ability to process salaries timeously, carrying out an effective job evaluation exercise which had been agreed upon by management and worker committees as well as implementing quarterly salary reviews (at 100% of the basic salary) so as to be in line with the rate of inflation (at 500% in March 2004). An interview with a respondent in the Department of Finance revealed that employees from PSMAS rarely leave the organisation for another medical aid society owing to the their compensation administration. This is largely attributable to disposable income left to the employees, well catered for by quarterly salary reviews although these were last implemented in July 2004. The late disbursement of the 2005 salary increment begun to demotivate the employees who started clamoring for another salary increment at the time of the interviews.

PSMAS has as its core value a precise mission statement, which is championed by a force, which is motivated by a comprehensive compensation plan. Its mission statement entails the following.

- being iented at all times;
- sourcing managing and availing funds in the most prudent and economical way;
- paying claims timeously and accurately;
- processing membership expeditiously;
- employing and retaining competent staff; and
- continuous improvement through innovation and creativity.

The Chief Executive Officer (CEO) argued that what is stated in their mission statement can only be implemented successfully if their human resources are well motivated and trained. This, he argued could only be done if a well-crafted compensation plan that is properly understood, installed and leaves disposable income to employees is put in place and manned by competent employees.

A respondent in the Human Resources Department defined compensation as "a total package offered to employees/reparation for services rendered. This is a combination of monetary (salaries and wages) and non-monetary rewards such as educational allowances, car loans, cell phones, insurance, housing and transport allowances".

It was further stated that the factors that influence compensation packages include:

- nature and grade of the job (that is) based on job content – based on how the job has been evaluated;
- performance of the individual (for motivation);
- industry practice;
- market based survey (that is what the market is paying for similar services in related organisations);
- performance of the organisations (this is done for the sake of sustainability);
- macro-economic factors like inflation, supply and demand factors (thus compensation should afford the employee the basics of life based on consumer price index and inflation);
- job evaluation based on the Perommes job evaluation system (conducted in 2004); and
- on job evaluation.

The following observations were made: the more difficult the job the more its worth; the more skill, education and responsibility required in a job the more its worth; the more scarce the labour supply and higher the demand the more a job is worth. Although these are general deductions, they are to extent the indicators of what the level of pay should be.

It is also important to note that the implementation of the Perommes job evaluation system resulted in the development of grades, which in turn determined the levels of pay applicable to each and every grade tabulated in table 2 below.

Their own staff conducted the PSMAS job evaluation exercise with the consultants only facilitating the exercise. The interviews with the employees revealed that the grades were not imposed on employees but the process was democratised such that all relevant stakeholders were consulted. PSMAS conducted quarterly salary reviews to address inflationary pressure. However, employee morale declined at some point as a result of late salary increments. The delays in awarding another salary increment could be attributed to the decline in the rate of inflation which was at 132% in February 2005 i.e. down from approximately 640% in January 2004. Salary increments at PSMAS are normally awarded based on the rate of inflation.

One employee pointed out that although there were delays in salary increments they were still better off compared to other employees in competing organisations. In addition

**Table 1**

| Staff category | Grade | Compensation package |
|---|---|---|
| Executive management | 1-6 | Salary, full digital satellite television, grocery, rates, electricity, unlimited telephone and fuel usage, cars, cell phone, insurance, allowances for housing, education, holiday, entertainment. |
| Middle management | 7-9 | Salary, cars, limited telephone and fuel usage, clothing allowance, holiday, education, housing, entertainment. |
| Staff | 10-16 | Salary, allowances for education, housing, entertainment, education. |

to the above-mentioned salient features of PSMAS compensation policy some observations can be made. One can note that compensation has always been part of PSMAS's focus and strategy. This is why their employees have not forsaken them despite the delays in awarding them a salary increment.

Implied in the arguments of management that for an organisation to achieve its goals needs to adequately compensate the human resources that overwhelmingly drive the goals of the organisations. This according to them motivates even the non-performers. PSMAS compensation policy could also be said to be based on equity and fairness, guided mainly by what the market is offering as well as macro-economic factors such as inflation, supply and demand factors, consumer price index and a host of other factors.

## Compensation and performance of employees

When asked to comment on the performance management system one of the senior managers revealed that evaluation is done at departmental level. Since PSMAS is for health service delivery their worker output is difficult to measure. This explains why performance is evaluated at departmental level rather at individual level. Even at departmental level there is formal evaluation *per se,* but each manager closely monitors his/her subordinates. Non-performers are warned several times if they do not take heed of the warnings then they will be dismissed.

The research also revealed that there is no performance increment. Although the employees are awarded bonuses at the end of the year these are again not linked to the performances of employees, since non-performers are dealt with instantly. The dismissal of non-performers will then be a wakeup call to others to work even harder thereby influencing the performance of employees to achieve the goals of efficiency and effectiveness in the discharge of their duties in terms of both quality and quantity.

The CEO observed that the general performances of employees of the society had really been commendable owing to the effective and efficient administration of a well-crafted compensation policy mentioned earlier on. This confirms findings by Daly (1975:3345) that compensation has measurable effects in workplace regarding attitudes and behaviour.

The Human Resources manager echoed the same sentiments when she argued that:

> *Specifically referring to our employees, compensation has a positive impact as it is based on a standard and systematic compensation plan taking into account all factors mentioned earlier on …as a result of this compensation plan our employees have enabled the society to meet and exceed the expectations of our members and valued stakeholders in terms of being in financing health care in the country.*

It is against this background that one can postulate that a standard and systematic compensation plan can propel an organisation from the doldrums of financial instability, poor employee performance, high employee turnover, absenteeism, workplace instability to the pinnacle of organisational success characterised by financial stability; attraction and retention of well qualified and competent staff; low turnover as well as excellence in service provision in terms of both quality and quantity.

The CEO further pointed out that having successfully managed to direct and co-ordinate the various talents the employees (motivated by a comprehensive compensation policy) PSMAS won the following awards tabled below.

Commenting on the awards bestowed on his organisation the CEO claimed that:

> *I cannot take the credit without mentioning the unwavering support of all PSMAS employees who have managed to turn around the society to be the best healthcare provider in the country…. The Honours or Awards should be regarded as corporate awards for the performance of the society, achieved mainly through our employees who are well motivated by our compensation plan.*

These awards alone point to the fact that PSMAS has been performing beyond expectations over the years, especially, since 1998 after the overhaul of the compensation plan which saw the attraction and retention of competent staff as revealed by the CEO. It is not surprising to note that the CEO attributed such success to their compensation plan although he mentioned other factors such as teamwork, good management styles and concern for the general welfare of staff. Notwithstanding these awards, PSMAS has often been criticised for failing to process claims timeously. This reinforces the fact that PSMAS is without major pitfalls.

The mentioning of other factors as highlighted above, implies that there is no one best way of driving employees to perform. Thus, although compensation (that is salary, wages, benefits and other incentives) plays a pivotal role in determining or enhancing employees' performance, other factors come into play well.

The CEO further contended that compensation is a major motivational factor that affects performance of employees versus the company's goals and objectives. Thus in the PSMAS case they have managed to achieve most of their goals and objectives through a fair compensation plan, coupled with other factors like team work, good management styles and concern for general welfare of staff.

The CEO outlined some of the goals achieved through a fair compensation plan administered to employees that in turn boosted their performance as follows: large membership base which continues to grow; excellent service in terms of both quality and quantity to members and customers; limited staff turnover; a conducive work environment; and a healthy industrial relations environment. Acquisition of strategic business units to provide to members a total

**Table 2**

| Award | Year |
|---|---|
| Manager of the year | 2003 |
| Runner up Manager of the Decade Award | 2003 |
| National Economic Consultative Forum Benefactor Award, Awarded by His Excellency, the President of Zimbabwe. | 2004 |
| Gold Medal for excellence in Business Practice which is an International Award in Geneva-Switzerland | 2004 |

quality package in terms of medical insurance; access to rehabilitation services; laboratory services; surgeries and hospitals; as well as dental services.

Commenting on the various effects of compensation he also asserted that:

> *Compensation has varied effects at management and shop floor level. However, currently all staff whether general or management looks at their compensation and how far their disposable incomes cater for their needs versus the macro-economic environment, therefore at any level what is considered is the disposable income.*

Having aptly outlined that, the CEO concluded by observing that:

> *"Given the above factors, I believe we have managed to attain this through our compensation plan".*

The dimension of disposable income should feature prominently in the discourse of compensation. Compensation that enhances employee's performance, is that which leaves huge amounts of disposable income to employees. This salient feature of compensation should therefore be taken into account when discussing or analysing the compensation debate.

Implied in this argument is the fact that it is not compensation *per se* that accentuates employee performance but that which leaves disposable income to employees. Another important component of compensation that was said to have a *huge impact* as well, was incentives. Apart from salaries given to employees, incentives motivate employees to work even harder. This is so because incentives reward that *extra effort* exerted by employees. Incentives are variable rewards awarded according to variations in the achievement of specific results. Their primary advantage is that they induce and motivate workers for higher efficiency and greater output.

## DISCUSSION

Basing one's arguments on the foregoing findings one can argue that compensation can be said to have varied effects on employee performance. It does not only have varied effects but it is also complex and dynamic in nature. While a company's remuneration policy outlines its remuneration philosophy as well as what it takes to achieve, the implementation of the same may not have desired results. This is so because policy as formulated may not be policy as implemented. Several confounding factors like resource limitations, craft incompetence and craft illiteracy may militate against successful implementation of a given policy.

Findings on PSMAS portrayed to a greater extent the fact that a comprehensible remuneration strategy can drive the performance of employees. Thus the PSMAS remuneration policy has a direct bearing on the contribution of employees towards organisational goal attainment. The success of the organisation was largely attributable to the good performance of employees, which was also attributable to their compensation plan.

It is important to note that compensation, in the case of PSMAS did not only have a positive impact on the attraction as well as retention of competent employees. The fact that different components of compensation have varied effects on employees cannot be overlooked as well. Aswathappa (1997:267) contends that unlike salaries and wages, incentives have a primary advantage in that they induce the motivation of workers for higher efficiency and greater output while fixed remuneration is difficult to drive employees to perform since it removes fear of insecurity in the minds of employees. However, incentives only have positive effects if they are appropriate and adequate to the type of work and workers; well defined and comprehensible with a formula which is properly installed and maintained; and when workers have reasonable control over their efforts. Moreover the concept of incentives is applicable to where measurement of output is feasible.

With the case of PSMAS in mind it was found that supplementary pay/fringe benefits are more useful in maintaining a competent workforce and in motivating higher levels of performance. Benefits such as cars, cell phones and insurance have greater impact on employees as well as exceed expectations of the organisations notwithstanding the fact that there are genuine complaints of delays in processing of claims. The latter implies that PSMAS is not without criticism.

Moreover, compensation affects those who require it to perform optimally. Thus the influence of compensation administration on employee performance can be applicable to those who derive their motivation from it. While some employees have an inherent desire to perform brilliantly, some may have reached the self-actualisation stage where they will no longer be driven by remuneration to perform. Hertzberg's *two factor theory* also explains the role of other factors while Maslow's *hierarchy of needs* suggests that when employees' lower level needs are satisfied they spontaneously and instantaneously move up the ladder for satisfaction of other needs.

## CONCLUSIONS AND RECOMMENDATIONS

The research findings suggest that there is no one best way of enhancing employee performance. To say that compensation drives employees to perform better may be an overstatement and fictitious. Human needs are dynamic in nature let alone complex. Each individual does not live in a vacuum nor does he/she live in a world of their own where environmental factors do not manipulate them. This inevitably suggests that human needs are multifaceted and only a multifaceted approach to the satisfaction of those needs is required for them to realise their potential. Therefore there is need for a contingency approach to compensation.

Against such a complex background of varied effects of compensation on employee performance several arguments can be put forward:

A remuneration policy should entail other components of variable pay that is pay, which is linked to the performance of employees. This inevitably results in the direct correlation between pay and performance. Thus employees must be made to believe that greater efforts result in greater rewards. Individual employee achievement of key result areas must have a direct relationship with compensation. In industries where output is measureable then the concept of incentives should be introduced. This will obviously drive employees to achieve set targets and even surpass them.

For the sake of sustainability a remuneration strategy should clearly elucidate the relationship between salaries, wages and benefits to the key success factors of the organisations. Thus, it should be made clear to employees that individual packages are determined by the ability of the company and the individual's performance. The ability to pay is determined by macro-economic factors such as inflation; supply and demand; and the profitability of the organisation which is also determined by the performance of employees. This inevitably provokes an employee to champion the sustainability of the organisation.

Issues of equity and fairness of compensation should be adhered to for compensation to achieve desired results. Thus there must be both internal and external equity. Competent individuals must be appointed to manage this fair and equitable reward plan. A company's remuneration should democratise the pay process as well as demystify remuneration administration. Thus employees' should also influence what they earn. This is a pre-requisite for industrial stability, which is the key to boosting employee performance.

For remuneration to drive the performance of employees it should clearly portray those behaviours that need to be rewarded. Thus its role should not be ambiguous but it must be stated in no uncertain terms. The need for adherence to regulatory/statutory requirements can never be overemphasised. Employees are bound to be frustrated and demotivated if they get to know that what they earn is below the regulatory/statutory requirements. This may also result in unnecessary legal disputes, which in turn result in inordinate delays that may militate against successful employee performance.

There is a need for market related compensation. Apart from enhancing the employees' competitive advantage such compensation is bound not only to attract competent employees but even to retain those within the organisation as well. The need for greener pastures inevitably demotivates employees. A remuneration strategy should also take into account the prevailing macro-economic environment. The need for disposable income on the part of the employees should never be underestimated. It is those employees with a sustainable livelihood who are bound to enhance the performance. Thus factors such as inflation, consumer price index and poverty datum line as well as supply and demand factors should influence a company's remuneration strategy.

Above all a compensation plan should be properly installed and maintained, it should be a product of both management and employees. Employees must understand a given compensation plan. Moreover, the pay process should be democratised. While employee input should not be overlooked, management should stick to a sustainable remuneration plan. This harmony is conducive for results oriented employee performance.

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