

A Comparison of Intrinsic and Extrinsic Compensation

Instruments in the Banking Sector of Pakistan

A Case of National Bank of Pakistan (NBP), District Attock

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Abstract

A company's financial assets have always occupied central importance and banks are the part of the financial institutions that look after that aspect. However, world's recent plunge into financial crisis has raised this importance to critical level. Particularly, this has put direct effect upon financial sector. The fact that organizations cannot control their external environment in the current period of recession has put direct emphasis on management of internal environment of such organizations. Compensation management deals with the ability to effectively compensate the employees to work, and create a competitive advantage through highly motivated human resources. Although, human resources are accepted to be organization's most important assets yet organization's decision often depicts contradiction with this belief. Human resource should not be neglected because they can bring competitive advantage to organization. Therefore, they should be managed with equal importance with other functions of the business (Barney and Wright 1998). Employee participation, extensive employee training and performance, contingent incentive compensation, are widely believed to improve the performance of organizations (Pfeffer, 1994). Similarly, If employees are compensated effectively they increase productivity of the organization (Ichniowski, Shaw & Prensushi 1997). The paper focused upon exploring different instruments and the factors of motivation which they affect the banking sector of Pakistan. In order to achieve these objectives, interviews were conducted at each level of employees of NBP. The paper has concluded that Compensation Management has a profound direct positive relationship with employee motivation level and intrinsic factors played important role in the motivation process. The paper recommends that banking sector shall apply progressive human resource strategy and provide healthy compensation plans regarding benefits and intrinsic factors.

Field of Research: Human Resource Management

INTRODUCTION

A company's financial assets have always occupied central importance whenever it has come to management decisions. However world's recent plunge into financial crisis has raised this importance to critical level. This has particularly put direct effect upon financial sector such as banks. The fact that organizations cannot control their external environment in current period of recession has put direct emphasis on management of internal environment of such organizations. Compensation management deals with the ability to effectively compensate the employees to work, and create a competitive advantage through highly motivated human resources (HR).

Compensation is the cornerstone of an effective talent management strategy. The ability to enable consistent, reliable and standardized compensation processes that is linked to performance drivers of individual and organizational strategies can affect many facets of the business. Some of these facets include:

- Improved employee morale and retention
- Increased employee engagement and productivity
- Strengthened governance and compliance with company and regulatory issues.

Motivation is the set of reasons that determines one to engage in a particular behavior. The term is generally used for human motivation but, theoretically, it can be used to describe the causes for animal behavior as well. This article refers to human motivation. According to various theories, motivation may be rooted in the basic need to minimize physical pain and maximize pleasure, or it may include specific needs such as eating and resting, or a desired object, hobby, goal, state of being, ideal.

"Employee satisfaction" helps the company to maintain a standard & increase productivity by motivating the employees. As "human resource" is the most important resource for any organization, so to study on employee satisfaction helps to know the working conditions & what are the things that affect them to work properly or otherwise.

These factors become really crucial when we talk about financial institutions that have nothing more than services and that also of financial basis to attract their customers. In this condition it becomes really important for them to deal in an effective and committed way to their customers. Because they have no real brand names to back them up, and also customers feel very protective while dealing with financial products, services or institutions.

Pakistan is a developing country, and being a developing country recent financial crunch has the worst impact over it. Where developed countries like America and that of European Union managed to sustain their financial institutions through the strength of their governments. But it is evident that countries like Pakistan lack such government strength. So businesses and especially financial institutions in a country like Pakistan has no hope to control the effect of any such calamities through bailing out by factors like government from their external environment. So then what they must do? It is the question that has to arise. We have already discussed the problem of financial institutions for lacking any strong brand and

having sensitive customers. In this scenario financial institutions may only count on the strength of their internal environment. "Strength of their own backs", as we may quote it.

The strength of any financial service provider lies in its human resources. It is logical that if you have a strength that can be your competitive advantage and is directly related towards your operations it will help in evading your threats in external environment. A satisfied and motivated workforce will have convincing influence upon customers and can attract them even in most gruesome conditions as we can find nowadays.

Observing financial sector of Pakistan, it becomes clear that banking sector dominates it. Banking sector for Pakistan has been somewhat static and slow moving for decades, until government let go of all banks except National Bank of Pakistan in private hands. This started a new revolution in banking sector, with changes erupting in almost every aspect of private banks. This brought about a serious competitive environment in banking sector. But with all the positive impacts it also brought some big question marks and doubts. Doubts regarding employees and customer satisfaction. Question marks about who is the best. But with financial crunch these doubts have changed to which bank can survive, and who can still have trust of its customers.

In banking sector if one name can not be ignored then it is National Bank of Pakistan, The bank that has not only the largest branch network nation wide but also in foreign country, largest reserves, highest authority, and strong corporate brand position with government backing. Before going further into our topic let's have some information about National Bank.

National Bank has a vision of "To be recognized as a leader and a brand synonymous with trust, highest standards of service quality, international best practices and social responsibility." Its Mission statement is "NBP will aspire to the values that make NBP truly the Nation's Bank by Institutionalizing a merit and performance culture, Creating a distinctive brand identity by providing the highest standards of services, Adopting the best international management practices, Maximizing stake holder's value, and Discharging our responsibility as a good corporate citizen of Pakistan and countries where we operate."

National Bank of Pakistan was established under the NBP ordinance in 1949 and was 100% govt.-owned. NBP acted as an agent of the Central Bank wherever the State Bank did not have its own Branch. It also undertook Government Treasury operations. Its first branches were in jute growing areas in East Pakistan. Offices in Karachi and Lahore followed. In 1950 NBP established a branch in Jeddah, Saudi Arabia. In 1955 By this time NBP had branches in London and Calcutta. In 1957 NBP established a branch in Baghdad, Iraq. In 1962 NBP established a branch in Dar-es-Salaam, Tanganyika. In 1964 The Iraqi government nationalized NBP's Baghdad branch. In 1965 the Indian government seized the Calcutta branch on the outbreak of hostilities between India and Pakistan. In 1967 The Tanzanian government nationalized the Dar-Es-Salaam branch. In 1971 NBP acquired Bank of China's two branches, one in Karachi and one at Chittagong. At separation of East Pakistan NBP lost its branches there. NBP merged with Eastern Mercantile Bank and with Eastern Bank

Corporation. In 1974 the government of Pakistan nationalized NBP. As part of the concomitant consolidation of the banking sector, NBP acquired Bank of Bahawalpur (est. 1947). In 1977 NBP opened an offshore branch in Cairo. In 1994 NBP amalgamated Mehran Bank (est. 1991). In 1997 NBP's branch in Ashgabat, Turkmenistan commenced operations. In 2000 NBP opened a representative office in Almaty, Kazakhstan. In 2001 State Bank of Pakistan and Bank of England agree to allow only 2 Pakistani banks to operate in the UK. NBP and United Bank agreed to merge their operations to form Pakistan International Bank, of which NBP would own 45% and United Bank 55%. Also that year, NBP closed its branch in New York. In 2002 Pakistan International Bank renamed itself United National Bank Limited (UNB). The ownership structure of the UNB remained as before. The only change to the shareholding structure is that UBL had recently been privatized in Pakistan and was now owned 49% by the Government of Pakistan and 51% by a joint foreign consortium of Abu Dhabi. In 2003 NBP received permission to open a branch in Afghanistan. In 2005 NBP closed its offshore branch in Cairo. Today NBP has 1450 domestic branches nationwide spread over 23 regional segmentations. It has assets up to 350 billion rupees.

Literature Review

Lyndsay Swinton in her article "How to Increase Your Work and Life Satisfaction: Put Abraham Maslow Theory into Practice" described a relationship between Maslow's hierarchy of needs with Herzberg's theory. Maslow's theory states a person's needs hierarchy with basic needs at base followed by security needs, social needs, esteem needs and self-actualization needs. She is of the opinion that up to the esteem needs level employee motivation or satisfaction can be maintained by factors which Herzberg called hygiene factors. This includes salary, benefits, job security, company policy etc while to deal with people at self-actualization level factors known as motivators would be needed. This includes employee achievement, employee recognition, and employee growth. By keeping in mind this relationship among two basic theories of management organization may find it easy to manage their HR and other operations. Ahmed Belaid Kridan and Jack Steven Goulding in their research paper "A case study on knowledge management implementation in the banking sector" are of the view that knowledge management system could play an integral part in increasing any organization's performance and can help it to compete in such highly competitive environment as today's. They say that knowledge management system if applied can bring improvements in decision making, increase in customer value, improving relationships with consumers and bringing new value in to sight by including the concept of innovation. G.S. Sureshchandar, Chandrasekharan Rajendaran, R.N. Anantharaman and T.J. Kamalanabhan in their research paper "Management's perception of total quality service in the banking sector of a developing economy- A critical analysis" studied banking sector of India and analyzed how different banks apply concept of total quality service in their functions. They found that these applications are inconsistent and incongruent

with in all banks. Which makes it highly sophisticated sector. According to them banks of India can be divided into three groups based upon their perception about total quality services in operations.

(Barney, 1998; Wright, 1998) describes that although human resources are accepted to be organization's most important assets yet organization's decision often depicts contradiction with this belief. They further say that HR should not be neglected because they can bring competitive advantage to organization. Therefore they should be managed with equal importance with other functions of the business. (Huselid, 1995) has emphasized on the fact that usage of high performance work practices i.e. comprehensive employee recruitment, Incentive compensation and performance management, extensive employee training and involvement programs surely increase competence of employees, it increase their motivation and reduce turnover. This results in retention of quality employees and also is a useful way to eradicate poor performers from the organization.

Nowadays organizations are been persuaded by competitive environment to apply a progressive HR strategy. As stated with the relevance of (Pfeffer, 1994) "The past decade has presented with many testimonials to the value of progressive HRM practices and system of such practices. In particular, employee participation, empowerment and job redesign, extensive employee training and performance contingent incentive compensation, are widely believed to improve the performance of organizations." (Delaney, 1996; Huselid, 1996). Human Resource management and productivity of organization has a direct relationship with each other. If employees are managed appropriately i.e. job analysis, recruitment, training, motivational tools like compensation etc they are destined to give high performance in their operations so will improve the over all productivity of the organization. (Ichniowski, 1997; Shaw, 1997; Prensushi, 1997) while

Thomas E. Catanzaro (2001) in his article Compensation & Motivation described the effects of compensation over employee motivation. He stated that compensation has a profound effect over employee motivation. He also discussed several factors of compensation which include both intrinsic and extrinsic factors and their possible effects over motivation in detail. He also emphasized that monetary values are not the only motivators but non monetary factors have more importance towards motivating employees. In Hong Kong, base salary, merit pay, year-end bonus, annual leave, mortgage loan, and profit sharing were the most important factors to retain and motivate employees. In China, base salary, merit pay, year-end bonus, housing provision, cash allowance, overtime allowance, and individual bonus were the most important factors to retain and motivate employees. (Chiu, 2002; Luk, 2002; Tang, 2002) Reward and recognition programs can positively affect motivation, performance and interest within an organization. While a little more problematic, team-based incentives, if designed appropriately, can also encourage and support a range of positive outcomes. (Milne, 2007) Promotion and wages positively influence employees' work motivation. A comparison of the relative strengths of the effects reveals that fair promotion was a more powerful motivator than wage level and

wage increase. The reason why fairness in promotion was more effective than wage to motivate employees was discussed in light of the unique career system existing in Japanese companies and the agency problems between companies and their supervisors. (Takahashi, 2006) Explores past and present attitudes of employees concerning work-related motivational factors. Understanding the factors that employees consider motivating lends insight to the rewards to which they more positively respond. It compares the results of four motivation surveys conducted in 1946, 1980, 1986 and 1992. The comparisons revealed that employees' motivational preferences vary over time. In addition, the results of the 1992 survey indicate that the factors that motivate today's workers are more extrinsic than they used to be. Although employees differ on how they rank these factors, they overwhelmingly selected "good wages" as the top motivator. A good wage is an extrinsic reward with intrinsic potency. On the surface "good wages" seem to be purely extrinsic. Yet, at a deeper level, monetary rewards communicate what the company values and affect employees' emotional and familial wellbeing. (Wiley, 1997)

Methodology and Research Design

Nowadays Business environment have entered in such an intense competitive state that management have to emphasize with utmost concentration on each and every function of organization. Nowadays every aspect can be utilized as competitive advantage and if a company neglects it then competitor would surely adopt it. Human Resource is also a vital function of business, and in most cases we find HR at the base of a company's operations, because it is employees who carry out all the functions of the company.

Therefore HR is an important resource as well as primary choice for competitive advantage.

Now if we take the example of banking sector we will find that its service oriented field where all that depend is how HR resources deliver their services to customers. Nowadays banks have become extremely decentralized in nature and due to privatization of banks the level of competition has entered in a new dynamic phase. Which directly have its effects over employees of banks? Continuous increasing market demands have literally over loaded employees of banking sector and stretched their working hours in an absurd way. All of this has resulted in employee complaints about work pressure, stress, strain, lack of fulfilling family expectations etc which really have a bad impact over employee motivation of banking sector and ultimately their performance. Which is completely opposite to what is demanded by higher management? To coup with this situation companies have to utilize their compensation strategies and reward policies with good effect. The problem or question is also whether banks are applying the appropriate compensation strategies with respect to their HR issues? Are their strategies achieving their desired results?

These questions leads to identification of problems like demotivation, dissatisfaction of employees and customer, high turn over etc and therefore needs to be studied with care.

Research Objectives

The paper will find out different aspects of a compensation system having the following objectives.

- Checking the employee perception about different compensation instruments
- Assessment of instruments used for extrinsic compensation including both monetary and non monetary types.
- Checking the effectiveness of different intrinsic instruments regarding job satisfaction and motivation to work.

We conducted literature reviews and studied scholarly articles and research papers about Human Resource, Compensation management, Employee Motivation, and Employee Performance so that we could get basic idea about all the modern themes and variables of compensation management and could analyze compensation strategy of NBP in best possible way.

Interviews were adopted as primary data collection tool. The reason behind this was the facts that our research topic was qualitative in nature.

Sample and data collection

We chose to conduct an unstructured interview with open ended questions from employees of district Attock; total 20 officers were interviewed, including 4 branch managers of the branches located in the district namely Attock city, Kamra, Makhad and Ghorghushti branches, 16 officers of Attock branch were also interviewed. Reason was that compensation strategy is same throughout the organization, so data collected from one region may be replicated and projected for the rest of the regions as well.

Research Design

An exploratory research design is developed for assessing the impact of different instruments of compensation on different work related issues that will be highlighted by the employees during interviews in response to open ended questions.

Concepts	Indicators	Variables
Compensation	Extrinsic	Monetary
		Non Monetary
	Intrinsic	Job itself
		Career Development
		Empowerment
		Delegation

Findings and Discussion

From research conducted we identified several instruments that has been used in compensation strategy by National Bank of Pakistan and that were in turn applied with slight modification by all other parties in the banking sector of Pakistan. Instruments were from both Intrinsic and extrinsic factors of compensation.

Among Extrinsic factors employees indicated instruments i.e. basic salary (different for each scale), increment of 15% in basic pay annually, full basic pay bonus on Eidains, medical expenditures refunds, Far area bonus, Year end bonus, house loans, car loans etc.

Among Intrinsic factors employees indicated instruments like friendly work environment, training and development programs separately for each grade, employee of the year award in each region, regular promotion, constant employee performance appraisal, sense of association towards employees from regional authorities.

It was found that employees had general acceptance that their salary and benefits package is relatively better in the banking sector of Pakistan. And a high level of satisfaction was felt and observed in employees regarding their extrinsic factors.

However what was really indicated as motivating tools in this regard were instruments from intrinsic factors. Permanent nature of the job has minimized the fear of losing job, so employees can deliver there best with a sense of satisfaction. Employees who were interviewed strongly advocated that no other bank in Pakistan except National Bank of Pakistan keeps its employees this much close. Nor do they really do much for employee loyalty, and development. For instance regular promotions of employees cannot be observed in Habib Bank as quoted by several employees. Also creation and observation of this sense of belongingness to a prestigious organization to and by employees of National Bank cannot be seen else where. Reason for this claim was related mostly towards privatization of other banks. From interviews it became a reality that National Bank's employees are one of the most loyal Human Resources an organization may find regardless of the fact that they have to work more hours and hectically than other banks. There were complaints about low staff distribution in many branches of small cities and long working hours disturbing employees' social life but even these were overcame by the positive effects created by National Bank's compensation strategy upon its employees over the years.

Conclusion

The paper had concluded that Compensation management has a direct relationship with employee motivation and performance. Extrinsic benefit plans plays a delight role in perception of an employee towards its organization and its work. And these factors play the role of satisfiers.

Instruments of intrinsic factors have a profound impact upon an employee's loyalty and an organization's turn over. Intrinsic factors play the role of motivators for the employees and associate them with their job and organization. They feel important and consider their performance as organization performance and image of organization as their own image.

Recommendations

From our conclusion it can be wisely recommended that banking sector must focus a lot upon the well being of its Human Resources. So that they can achieve a competitive advantage through them and stand apart as well stand strong in such hard times as in current global financial crisis when financial sector is experiencing a tight squeeze in external environment.

Intrinsic instruments are strongly advised to be more aligned for the entire banking sector. The paper recommends extrinsic factors as the basis but intrinsic as the beauty as only the inner satisfaction can produce optimum quality.

This is an introductory and basic type of work on the topic therefore it recommends more research on the topic including exploration of different aspects of motivation and job satisfaction and the factors that are necessary to determine there levels. Studies to find out the relationship of different factors with different instruments will have interesting findings.

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