

**EFFECT OF COMPENSATION STRATEGY ON THE
PERFORMANCE OF THE OFFICE OF THE AUDITOR-GENERAL
IN KENYA**

**BY
CHRISTINE NZANGI MUTHENGI**

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DECLARATION

Declaration by the Student

I the undersigned clearly do state that this study is my original work and has not been submitted to any University or any other learning Institution for award.

Name : CHRISTINE NZANGI MUTHENGI - D61/79070/2015

Sign :

Date :

Declaration by the Lecturer

I confirm the work in this project was done by the candidate under my supervision as the University appointed supervisor.

Name : DR. MERCY MUNJURI

Sign :

Date :

DEDICATION

I fully dedicate this research to my late father: Charles Muthengi Muisyo and my mummy Mary Kalunda Muthengi.

ACKNOWLEDGEMENT

My heart touching recognition and appreciation to my husband Philip Ngovi, my children: Josephat Mwendwa, Catherine Ndinda, Grace Kalunda and Mercy Nina for your moral support and encouraging words, every time you talk to me all that seemed a mountain becomes a mole, you inspired me in all aspects and I will never cease saying that you remain my Standing Pillars.

Dr. Munjuri my project supervisor, you are a wonderful lady. You were strict, not ready to accept shoddy work but very helpful and supportive. When things were hard on me, you gave encouraging words to keep me going and through that, I made it this far. You were focused and always gave a way forward on the project which was always inspiring, a very big thank you and God bless you abundantly.

My Mum and late Dad: Mr. and Mrs. Muthengi, if it were not for your encouraging words to pursue education as the gateway to success, I could not have made it this far. My brothers and sisters, your memories give me the courage and energy to move day after the other in pursuit of a brighter future.

I pronounce blessings unto you all. I love you All.

TABLE OF CONTENT

DECLARATION	ii
DEDICATION	iii
ACKNOWLEDGEMENT	iv
LIST OF FIGURES	viii
DEFINATION OF TERMS	x
ABSTRACT	xi
CHAPTER ONE: INTRODUTION	1
1.1 Background of the Study	1
1.1.1 Compensation Strategy	3
1.1.2 Firm Performance.....	4
1.1.3 Office of Auditor-General	5
1.2 Research Problem	6
1.3 Research Objective	8
1.4 Value of the study.....	9
CHAPTER TWO: LITERATURE REVIEW	10
2.1 Introduction	10
2.2 Theoretical underpinning of the study	10
2.2.1 Equity Theory.....	10
2.2.2 Expectancy Theory.....	11

2.3 Types of Compensation	12
2.3.1 Direct Financial Compensation	13
2.3.2 Indirect Financial Compensation	13
2.3.3 Non-Financial Compensation.....	14
2.4 Measures of Firm Performance.....	15
2.5 Corporate Strategy	18
2.6 Compensation Strategy and Firm Performance	20
CHAPTER THREE: RESEARCH METHODOLOGY	22
3.0 Introduction	22
3.1 Research Design.....	22
3.2 Data Collection	23
3.3 Data Analysis	23
CHAPTER FOUR: DATA ANALYSIS AND PRESENTATION.....	25
4.1 Organizational Information	25
4.2 Direct Financial Compensation and Firm Performance	25
4.3 How Office of the Auditor-General has ensured the amount paid as Salaries are standardized with the current Economic Trends.....	26
4.4 Measures taken to improve on Direct Financial Compensation.....	27
4.5 Indirect Financial Compensation and Firm Performance.....	27
4.6 Non-Financial Compensation and Firm Performance	29
4.7 Balance Scorecard and Firm Performance	30

CHAPTER FIVE: SUMMARY CONCLUSION AND RECOMMENDATIONS	33
5.1 Summary of Findings	33
5.2 Conclusion	34
5.3 Recommendations.....	35
5.4 Limitations of the study	36
5.5 Suggestions for further studies.....	37
REFERENCES	38
APPENDICES.....	42
Appendix I – Letter of Introduction.....	42
Appendix II: Interview Guide.....	43

LIST OF FIGURES

Figure 4.1: Measures taken by the Office of the Auditor General in Kenya to improve on the direct financial compensation	27
Figure 4.2: Indirect financial compensation that the Office of the Auditor-General gives to employees	29

ABBREVIATIONS / ACRONYMS

AG	-	Auditor- General
CA &G	-	Controller and Auditor General
CEO	-	Chief Executive Officer
COR	-	Code of Regulations
HR	-	Human Resource
KENAO	-	Kenya National Audit Office
OAG	-	The Office of Auditor-General

DEFINATION OF TERMS

Compensation – as a reward given to an employee or a person for performing certain task by a firm or in exchange for his or her willingness to perform

Performance – the action or process of performing a task or function

Strategy – a plan of action designed to achieve a long-term or overall aim.

ABSTRACT

This study sought to determine the effect of compensation strategy on the performance of the Office of the Auditor General. The research was anchored on two theories which are Equity theory and Expectancy theory. The researcher used case study research design in conducting the study. The target respondents were two heads of departments who were interviewed. The researcher used an interview guide to collect data from the respondents and analyzed the collected data using content analysis method. The researcher found that, Office of the Auditor-General as a large organization which has been in existence since independence with a population of 1250 employees, some on permanent terms, others on contract terms and others on probation. It was found that direct financial compensation facilitated the employees to offer their desired services for the daily running of the organization. Direct financial compensation acts as a source of motivation to staff and rejuvenates their performance and so it is important since it helps in improving the organizational performance. Indirect financial compensation like medical cover has an impact on employee's health and so it was found that good health is directly proportional for good performance and growth of the Office of the Auditor-General. It was found that, non-financial compensation such as good working environment has contributed to job satisfaction at the Office of the Auditor-General. Fair and appropriate policies has brought about equity and as a result, there is improved performance at the Office of the Auditor-General. The researcher found that, customer perspective has contributed to the Office of the Auditor-General monitoring its performance through feedback received from their customers. Learning and growth perspective was found to be a measure that helped the office to identify the weak areas of performance and improved on them through training of employees. Internal business process is an important measuring tool of performance which the Office of the Auditor-General should not ignore. Communication channels are very important because they create good relationship between employee to employee and manager to employee as these mutual relationships are key in the performance of any organization that wants to improve on its performance and the Office of the Auditor-General is not an exception. The Office of the Auditor-General should continuously embrace and thrive to improve on the quality and enhance professionalism among the staff members. The office should also focus on the services offered to customers by ensuring their expectations are met and they be satisfy. The staff member should also focus on addressing any emerging issues promptly and efficiently.

CHAPTER ONE: INTRODUCTION

1.1 Background of the Study

According to DeNisi and Graffin (2001) compensation strategy is a very important tool whenever employees and organization performance are present because it helps to build the efficiency, effectiveness and competitiveness of the firm that wants to remain competitive in the market. If an organization starts out with the wrong compensation strategy which does not fit the needs of the organization's human resource or business strategy, then this can bring down the organization. Milkovich (1999) stated that, a good and well planned compensation strategy leads to high production by the firm due to good performance by the employees. According to Armstrong (2010) understanding the effects of specific needs of each individual helps to improve on performance because the world is changing and for any firm to remain competitive, it has to understand the needs of the employees.

The efficiency in every firm depends on the nature of work to be done by a person, well-being of the person, standards set in terms of job specification, duties and responsibilities, tools of trade provided and working environment provided by the firm. Employees are rewarded according to the value they create to the organization. For firm to thrive and make a name in this competitive world, it has to align compensation strategy with firm objectives and employee values (Medina, 2002). According to Beer et al. (1985) compensation is considered a driving force of the objectives in any firm and management needs to have knowledge on. Purcell et al. (2003) argued that when employees are well compensated, they are committed to work, be satisfied by their job which leads to a positive

attitude towards their work and loyalty to the firm. It is through firm compensation strategy which helps the firm to attract high flyers, reducing labor turnover and employee feel appreciated.

This study is anchored on two theories Equity theory and Expectancy theory. According to Adams (2007) it's good to appreciate and treat people well because when people feel appreciated, they are highly motivated but when they feel unappreciated they feel dissatisfied. The sense of fairness by the employee is determined by what is in the heart of Equity Theory. Employees compare their effort and reward that is input and output ratio to measure fairness. Vroom (1994) Expectancy theory argued that an employee performs a task with an expectation of receiving payment and when the payment is received and the employee is happy, then the employee will improve on his performance next time because he expects the same treatment he received earlier. As stated by the two theories, firm's performance depends entirely on the attitude employee have towards the firm and the input they give to the firm.

The Office of the Auditor-General is an independent office that works as watchdog of public funds of Kenyan citizens to make sure public funds are not mismanaged, well accounted for and for Kenyans gets value for their money (Kenya Constitution 2010). The work of the office is to safeguard public resources from misuse and ensure that they are efficiently and effectively used (Ouko 2012). It is a very important organ to the Kenyan economy in that it makes sure that all the money allocated to various institutions are utilized for the purposes they were allocated, it also advices the Government on viable projects to spend money on and the ones to ignore thus saving the country from incurring necessary

expenses. The office of the auditor-General was being accused of delaying the audit report and submitting it later than the stipulated time by the Constitution which provides that the Auditor-General is required to audit and report within six months after the end of each financial year. The office was being accused of giving a report which did not give a true picture. The office was being accused of carrying out an audit that fell short of international standards (Menya 2016). Waweru (2015) note that, there was high staff turnover at the office of the Auditor-General.

1.1.1 Compensation Strategy

According to Beer et al. (1995) compensation strategy is a plan showing how employees are rewarded for the service they offer. Chabra (2001) argued that compensation is what is given to employees as payment for their services offered to the firm. DeNisi and Graffin (2001) defined compensation as a reward given to an employee or a person for performing certain task by a firm or in exchange for his or her willingness to perform. Holt (1993) defined compensation as the reward workers receive as compensation. According to Gerhart and Milkovich (1990) employee compensation serves as a motivator to employment relationship, being of critical importance to both employees and the organization. He also noted that compensation decisions contributes to the organizations ability to compete in the labour market, attract and retain employees and also changing employee behaviors and attitudes towards the organization.

Rajagopalan & Finkelstein (1992) noted that compensation strategy is a plan that dictates how employees are paid and rewarded for their work. Compensation is the reward earned by employees in return for their labour or service they render to the firm and can be in two

forms direct financial and indirect financial compensation. The balance between internal equity and competitiveness in any firm is called compensation and it acts as the source of happiness which affects the productivity of the firm resulting to good or bad performance of the firm, thus helping the firm effectively realize its objectives.

1.1.2 Firm Performance

Ansoff (1990) defined firm performance as the yardsticks by which the present and future performance of the firm is measured. Firms have to know where they will sit in tomorrow's world but not where they hope to sit by assessing where they are today to make decision on where they want to be. This will be achieved through positive thinking and well-focused employees who are willing to support the firm achieve its objectives. Hansen (1987) said firm performance is determined by the organizational climate like decision making practices, flow of communication, organizations goals, human capital, tasks and leadership condition that contribute to employee behavior resulting to firm performance.

According to Richard et al. (2009) firm performance is the results or the actual output of a firm being compared against its intended set goals of the firm. It contains three types of firm outcomes which includes; return on assets, profit and return on investment. Another area of firm outcome is product market performance which entails sales and market share. The final one is shareholder return which include total shareholder return and economic value added. Organizations have used systems consisting of financial and non-financial measures to track their progress and performance. Khandekar & Sharma (2006) defined firm performance as the outcome that reflect the effectiveness and efficiencies of an organization in terms of financial performance, competencies and corporate image.

Kaplan & Norton (2000) defined balance scorecard as a strategic tool which enables the firm to bridge the gap between strategy and action. It is a tool that can be used to measure firm performance and it entails financial and non-financial. Balance Scorecard helps members recognize long term drivers, translates the vision and strategy of the organization which helps to build consensus around the vision and mission for success of the organization.

1.1.3 Office of the Auditor-General

According to the Kenya Constitution (1964) the Office of the Controller & Auditor General (C&AG) was created as an Office in the Public Service during the Country's independence in 1964. Its mandate was to audit government institutions and any other institution funded by the government. After the enactment of the Audit Bill (2002) it changed the name from C&AG to Kenya National Audit Office (KENAO). After the promulgation of the Kenya new Constitution in August 2010, it changed the name from KENAO to the Office of the Auditor General (OAG). The Office of the Auditor - General draws its mandate from the Constitution of Kenya. Chapter 12, Part 6, Article 229 establishes the Office of the Auditor-General. Chapter 15, Article 248, Section 3 and Article 249, Section 2 (a) and (b) provides for the independence of the Office of the Auditor-General.

The Office of the Auditor-General is a Constitutional Office. The Auditor General is appointed by the president as the accounting officer to audit all institutions of the government and any other body that uses public funds to run its activities. The Auditor-General should audit and give a report of that years audit within six months of its audit.

The audit report of National and County governments, Accounts of Courts, Commission and Independence offices. It should also report on accounts of National Assembly, the Senate offices, political parties, county assemblies and any other body funded from public funds. Whether public funds have been utilized correctly or not in the respective bodies, audit reports have to be submitted to Parliament or the relevant county assembly.

1.2 Research Problem

According to Armstrong (2007), compensation is given to employees to motivate them intensify their desires and willingness to work; to encourage them work hard to achieve the set objectives of the organization. The compensation given to workers induces them to improve on their performance, have a positive attitude towards the firm and work effectively and efficiently without being supervised by their employers. He noted the importance of compensation strategy to motivate and reward acceptable behavior which lead to positive attitude by employees towards work and this improves their performance. If compensation strategies are designed properly, employees are happy about it and they significantly improve on their performance which translated to better performance of the organization. According to Johnson (2015) compensation in form of salaries and incentives are a means of encouraging the workers to be committed to their duties. If employees are not well compensated, they tend to think that they are not valued members of the firm and in most cases they are unable to give the best of their services in order to achieve the set goals of the firm. Employee's morale is not only boosted by the salaries but also other fringe benefits such as leave allowances, retirement plan and medical allowances which shows they are valued by the organization.

According to the Kenya constitution (2010) employees of the Office of the Auditor-General play a very important role as they act as a link between the organization and the public. The office of the Auditor-General was accused of submitting the audit report later than the stipulated time as mandated by the constitution. The office was also being accused of carrying out an audit that fell short of international standards (Menya 2016). Waweru (2015) noted that, there was high staff turnover at the office of the Auditor-General. General observation indicated that the above complaints of the report being delayed were brought about by inadequate staff the office had. The poor work performance and complaints from the public made the management team realize that there was a problem which needed to be addressed and action take to provide a lasting solution.

Kazan (2016) did a study on the impact of CEO compensation on firm performance in Scandinavia. The aim of the study was to examine the impact of CEO compensation on firm performance for Scandinavian firms. The study found out that there was non-significant negative relationship between CEO compensation and firm performance. Mbugua (2009) did a study on investigation of strategies for competitive advantage and their effects on performance of the tea processing companies in Kenya. The study was to establish the strategies for competitive advantages used by tea processing companies in Kenya and their effect on performance of these firms. The researcher found out that majority of tea firms have been unable to apply for competitive advantage on either of the dimensions of cost leadership, differentiation or focus.

A research conducted by Obasan (2002) on the Effect of Compensation Strategy on Corporate Performance: Evidence from Nigerians found that compensation strategy has

the potential beneficial effects of enhancing workers' productivity and by extension improving the overall firm performance. Aduda and Musyoka (2011) did a study on the relationship between executive compensation and firm performance among nine commercial banks listed at the Nairobi securities exchange. The study found out that there is a negative non-significant relationship between executive compensation and bank performance.

Effect of compensation strategy on firm performance has received considerable importance showing effective connection between compensation and firm performance. According to the available literature, most of the studies examining relationship between compensation strategy and firm performance were done in the private sectors and profit making organizations. None of these studies was done on public sectors therefore there was need for additional evidence to support effects of compensation strategy on organization performance relatively from different sectors and context.

The quoted studies have attempted to link compensation strategy with different outcomes and have also been done in a different context. Many scholars have done research on compensation strategy and the effect it has on organizational performance but none was done at the office of the Auditor General. What is the effect of compensation strategy on performance of the Office of the Auditor General in Kenya?

1.3 Research Objective

The objective of the study was to establish the effect of compensation strategy on the performance of the office of the Auditor General in Kenya.

1.4 Value of the study

This study was to help the existing theories in that, it has helped to compare the theories used in the study to find out if they concur. The study will also serve as a stepping stone by other researchers when doing their research because they can use it as their reference or they can also challenge the findings of this study. The study will help researchers to establish the influence of compensation on firm performance and also the link between compensation and organizational performance.

The study will be useful to policy makers like the Government since it will use these findings as a policy of compensation for rewarding other employees in other government entities to improve on the organizational performance. The study will identify the methods of awarding compensation to different level of employees that will help them improve on their performance hence leading to improving the performance of their organization. The outcome of the study will enable the policy makers at the office of the Auditor General to establish effect of the current compensation for the office, establish whether it has had positive or negative effect on its performance as an organization and help in establishing an effective strategy of awarding it.

This study has added value to strategic management practice since it has served as knowledge base on how to improve on firm performance by giving elaborate strategy on how to compensate and retain the employee by an organization. The study will expand the existing body of knowledge on growth of strategies to use to improve firm performance and stimulate interest that will lead to further research in related facets of growth.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

In this chapter, the researcher reviewed relevant theories on compensation strategies, past studies and also existing literature concerning the subject of compensation and firm performance. The chapter entails theoretical underpinning of the study which gives theories that guide the study. It also gives different types of compensation, measures of firm performance, Compensation strategy and firm performance.

2.2 Theoretical underpinning of the study

This study was based on two theories that is the Equity theory by Adams (2007) and expectancy theory by Vroom (1994) which are used by organizations to understand how employee should be treated in order to get the best performance out of their efforts. It also showed the link between compensation and firm performance as described and elaborated by other researchers.

2.2.1 Equity Theory

Adams (2007) Equity theory helps explain compensating employees and its effect on their performance in comparison to other employees doing the same job and what they receive as compensation. It also brings out the fact that promoting one employee or paying high salary to one employee can lead to poor performance from other employees. When employees feel appreciated and well treated, they are motivated to perform better or give the same performance but when they feel unappreciated, they feeling demotivated and poor performance given as a result. Equity theory emphasizes on quality and quantity of the

employee's effort to task. Outcome includes job security, self-esteem, recognition, reputation, thanks, sense of achievement, praise and responsibility.

Compensation remains the source and cause of equity or inequity. An employee wants to feel important and to see his/her contribution and performance of tasks recognized and rewarded accordingly, but if the employee feels underpaid, it will result to hostility towards their tasks, organization, co-workers and can lead to poor performance by the employee translating to poor performance of the firm. This theory brings about the issue of comparison with other people performing the same tasks as the employee in the same market place. Equity theory explains the reason of employees being motivated one time at their work place but when working condition and terms does not change while their colleagues receive better compensation then they are demotivated.

2.2.2 Expectancy Theory

Vroom (1994) expectancy theory states that the magnitude of behavior to perform in a particular manner is dependency on the high expectation that the performance will receive as reward. The likelihood that employee's effort will lead to expected performance by the employer and the belief that the performance will lead to reward to the employee motivates the employee to perform the task better. Expectancy is determined by possession of required skills for the task to be performed, availability of resources and favorable environment.

Vroom found out that employees consciously decide whether to perform a task or not which is contributed by employee's motivation level. This theory suggests that employee's

motivation level should be continually assessed by use of questionnaires, personal interview, or any other method that can determine employee behavior. In any situation, the greater the value of the rewards to individual as long as their needs and wants are met, the more the motivation and the high the performance of the employee. The office of the Auditor General managers can use this theory to estimate the reward an employee expects to get at the end of a certain task and also know the situations which affect the effort of the employee.

2.3 Types of Compensation

According to Dessler (2011) compensation is of two types which are direct financial compensation and indirect compensation. He defines direct financial compensation as direct cash pay that an employee receive on monthly weekly or daily basis in exchange for the service they offer to an organization. It can also be inform of stock bonus compensation where employee is given a certain percentage of shares of the firm and pay dividends for the shares after a certain period of time or increase their savings. Direct financial compensation includes salaries, wages, bonuses and commissions. Armstrong (2009) referred to indirect compensation as remuneration given to employee or reward he receives in exchange for service he provides. Indirect compensation are packages like retirement plan, leave allowance and medical covers. It is through these types of compensation that enable an organization to attract potential employees, retain them, get total commitment, reduce absenteeism, reduce staff turnover and strengthen firm to institute a comprehensive programs to run the firm (Noel et al. 1996).

2.3.1 Direct Financial Compensation

According to Kappel (2012) describes direct financial compensation as the monetary benefit paid by the firm to its employee in exchange of the service they offered or work done. It can be inform of salaries, wages, bonuses and commissions and is paid on regular basis. It's a way of inducing employees and reducing staff turnover if this compensation is high compared to what is offered in the market. It refers to monetary benefits for a specific period like an hour, a week, a month or a year. Mwangi (2014) cited the work of Armstrong who opined that, direct financial compensation holds basic pay as the amount that constitutes the rate for the job which depends on the job or for manual workers, the level of skills required. Further it also involves the contingent pay which has been described by Armstrong (2008) as additional financial rewards that may be given for their performance, contribution, competence, skill or experience.

Ruby (2012) defined direct financial compensation as a psychological force that determines the direction of a person's behavior in an organization. It's the level of effort and persistence of an individual in the face of obstacles. Direct financial compensation is the recognized form of compensation which employees look for and it is paid directly to employees in exchange for their labor. The financial benefits include wages, salaries, bonuses and commission which are provided at an expected period at a definite time.

2.3.2 Indirect Financial Compensation

Indirect financial compensation is the financial rewards that form part of social contract between employee and employer and are not included in direct compensation; it has a monetary value but is not a direct financial payment (Mike 2012). Indirect compensation

refers to the non-monetary benefits paid to the employees by the organization. Indirect compensation is not directly paid to the worker but given as an additional component to the base salary pay. These rewards include medical cover which enables an employee to access medical services in different hospitals under the cover without paying cash. This makes the employees happy and feel secure both with their families.

Retirement plan is another type of indirect financial compensation which offers attractive incentive to employees. A retirement plan of a firm can contribute to retention of employees by the firm because before they make a decision to leave to another firm, they have to compare their current retirement package with that of the intended firm and if it is not attractive, they would not leave. This is a plan that a firm has to pay an employee who retires upon retirement. A firm may also offer its employees leave allowances and educational sponsorship to help them (Kappel 2012).

2.3.3 Non-Financial Compensation

Non-financial compensation is the satisfaction an employee gets from his work environment and does not have any monetary value. It can be emotional or psychological satisfaction which makes the job more enjoyable and satisfying (Mike 2012). It can also improve the work environment by ensuring their policies are appropriate and fair. Hiring of good and capable managers who are supportive to both employees and the firm is a start of the better management of non-financial compensation schemes. Career development, opportunities for recognition, advancement opportunities and work life balance help to improve employee performance.

Non-financial compensation doesn't have any monetary value but it has the satisfaction that an employee gets from his work environment. The satisfaction may include emotional and psychological. Non-monetary compensation is different from direct and indirect rewards because no monetary value is involved (Mike 2012). It deals with the psychological feelings of the workers towards the treatment they receive from their organization.

2.4 Measures of Firm Performance

To measure firm performance, inputs like human resources, employee time and finances used to run the activities of the organization have to be considered. The output is a specific objective of a specific program which has been designed to achieve objectives. Balance score card is popular method of measuring firm performance (Kaplan & Norton 2001). It includes the following perspective;

The Financial Perspective aim is to evaluate firm's strategies to see whether they are translating into bottom-line improvement of the firm. Financial measures of a firm are historical and so they do not reveal the situation of the firm as it is at that particular moment and also it does not predict future performance of the firm. Firm's financial performance such as profitability are very important to the firm's success and therefore it should not be ignored. Barney (2006) said one way of measuring performance is by use of accounting measures which includes liquidity ratios, debt ratios, profitability ratios, market ratios, return on Assets and return on Equity. Langat (2006) gave four used measures of performance as Tobin's Q which compares firms' investment rate of return to its cost of capital; total return index, economic value added, cash value added.

The Customer Perspective enables firms to align core customer outcome measures that is loyalty, satisfaction, retention, acquisition and profitability to targeted customers and market segments. It also enables firms to measure and identify the value proposition which they will deliver to targeted customers and markets (Kaplan and Norton 2001). Firms exist to deliver products and services to their customers and they have to do their level best to meet the expectations of customers in order to retain them.

In past days, firms were concentrating on their internal capabilities emphasizing on product performance and technology innovation to be used. Most firms did not consider the value of understanding their customers' needs which led to success of their rivals who took advantage and offered better products and services aligned to their customers' preferences. Nowadays firms are putting more emphasis on their customers' preferences. The core measurement group of customer outcomes are customer acquisition, customer satisfaction, market share, customers' retention and customer profitability. To measure market share one needs to identify the specific target customers group or market segment, then trade associations, industry groups, government statistics and other public sources to get an estimate of the total market size. To measure customers or segments, firms can do so through how much customers' and market segment business they are receiving (Hayes 1992).

The Internal Business process Perspective helps to identify the processes which are critical for achieving customer and shareholders objectives. Firms develop their objectives and formulate ways of measuring them considering how they will measure financial and customer perspectives – which enable the firm to focus on internal business processes

metrics which will deliver the objectives stashed for shareholders and customers. Firms should develop internal process value chain like innovation process by identifying current and future customer needs. They should also develop solution for these needs through operations process like post sale services, after sale service and delivering products and services to customers (Kaplan 1996).

The difference between the balance scorecard and traditional performance measurement systems is through the process of deriving objectives and measures for the internal-business process perspective. Traditional performance measurement systems focuses on improving and controlling existing responsibilities and departments and they are referred to as financial measures. Financial measurements and monthly variance reports which are used for controlling departmental operations have limitations (Kaplan 1993). Organizations nowadays are moving beyond using variance analysis of financial results as their primary method or their method of evaluation and control. Quality, cost, time and throughput measures are being used to measure business processes like order fulfillment, procurement and production planning of firms. Through this they improve quality, increase yield, reduce wastes and time cycle, lower costs and maximize throughput for the business process.

The Learning and growth Perspective drives organization learning and growth process established objectives in the customer, financial and internal business process perspective and identifies where the organization excels to achieve expected performance. To achieve the other three perspectives, objectives in the learning and growth perspective and the objectives in the learning and growth perspectives are the key drivers for achieving

excellent outcomes in the scorecard perspectives. These perspectives include employee training, corporate cultural attitude related to corporate self-improvement and individual.

Kaplan and Norton (2004) said that learning is more than training since it include things like mentoring, tutoring within the organization, eased communication among workers and technological tools which is termed as high performance work systems. For the work force to build and enhance innovative business process, it has to be enabled with knowledge, innovation and advanced skill sets which will help to retain and acquire new customers and also to finance objectives. Firms should invest in infrastructure – people systems and procedures instead of investing on new products research, equipment and development in order to achieve their long-term financial growth ambitions. The factors that contribute to growth of learning and growth are primarily employees, systems and organizational alignment. Non-financial performance measures of measuring firm performance measure performance in non-monetary terms which include customer response time, market share, customer satisfaction, innovation, new product development, employee turnover and productivity (Kaplan & Norton 1992).

2.5 Corporate Strategy

Dransfield (2001) defined corporate strategy as the organization's vision and tactics to outperform its competition. It entails a firm's corporate actions with the aim to achieve company objectives while achieving a competitive advantage. To implement a better action and satisfy customers, corporate strategy ensures that long-term goals set by the organization are met, creates corporate values and encourage employees. According to Wheelen (2008) general attitude of organization management and growth on product line

and business is always described in the corporate strategy and it fits in the category of retrenchment, growth and stability.

To establish superior performance in order to achieve vision and mission of a firm, corporate strategy is necessary since it understands the customers, competitors and costs, segment the market, target the customers, better supply chain, use social network for marketing products, adapt innovative technology, develop a brand image, maximize intellectual property and profitability. It is through corporate strategy that firms change business mix to achieve high value, make more profits and look for market opportunities across the globe. It aims at answering the question – what kind of a business the firm should be in? How should it be finance and what kind of structure should it have?

Corporate strategy encompasses framework growth and development of the firm. The growth of a firm is the main objective of corporate strategy and entails implementation of policies and objective design by determining the vision, mission and long-term development goals and growth of the organization. Corporate strategy focuses on the resources it has like the assets of the firm, technologies the firm uses, skill and management capabilities.

When the firm provides financial incentives as reward, it helps in the improvement of its performance to achieve various competitive advantages. Compensation strategy of any firm should be aligned to the corporate strategy. Competitive advantage is achieved through innovation, quality of work and low costs by the firm and to achieve this, corporate

strategy has to provide financial incentives and recognize innovation by the employees (Mohanta 2013).

2.6 Compensation Strategy and Firm Performance

Kadhim (2017) did a study on relationship between compensation strategy and reward management on organizational performance on Iraqi Oil Companies. He found out that compensation plays a vital role to organizations success and performance. The study highlighted an optimistic and positive association between compensation and reward management on organizational performance. He found out there is a direct link between compensation and organizational performance since it influences employees' attitudes and behaviors, which ultimately influences organizational performance. Compensation and rewards management have a significant relationship with organizational performance.

Ozkan (2007) did a study on CEO compensation and firm performance, an empirical investigation of UK Panel Data. The study found a positive and significant link between CEO cash compensation and firm performance. He also noted a positive but not significant relationship between total compensation and firm performance. Aduda (2011) did a research on the relationship between executive compensation and firm performance in the Kenya banking sector. The study found out a negative non-significant relationship between executive compensation and performance of commercial banks in Kenya.

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Dobre (2013) did a study on employee motivation and organizational performance. The aim of the study was to analyze the drivers of employee motivation to high levels of organizational Performance. The study showed that, factors such as empowerment and recognition increase employee motivation. If the empowerment and recognition of employees is increased, their motivation to work will also improve, as well as their accomplishments and the organizational performance. Katua (2014) did a study on effect of reward and compensation strategies on the performance of commercial banks in Kenya. The study sought to investigate the effect of reward and compensation strategies on the performance of commercial banks in Kenya. It was found that, reward and compensation strategies have a significant positive effect on performance of commercial banks in Kenya. The study established that banks are currently emphasizing on rewarding and compensating their employees.

CHAPTER THREE: RESEARCH METHODOLOGY

3.0 Introduction

This chapter discusses the methodology of the study. It includes the research design, data collection showing the instruments and the process of data collection then summarizes by describing the procedures to be used to analyze data so as to achieve the objectives of the study.

3.1 Research Design

A case study research design was applied by the researcher in this study. The main objective of the case study was to establish the degree of compensation effect on the performance of Office of the Auditor General, Kenya. According to Singh (2006) a statement of the problem to be studied and how to collect data as evidence, how to analyze the collected evidence and giving an account of the observation or investigation is what is referred to as research design.

An in-depth investigation to an individual, group, institution or phenomena is the study which is referred to as a case study (Mugenda 2001). Hartley (2004) defined research design as a summary of step by step a researcher takes to link research question(s) and the evidence collected then analyze and give report of the findings. Mugenda (2001) refers to a case study as a powerful form of quantitative analysis and involves a careful observation of a social unit, personal family, institution, cultural, group or even an entire community.

3.2 Data Collection

In this study, primary sources of data were used. Data was collected through personal interview guide consisting of open-ended questions covering on issues relating to compensation strategy and firm performance. The researcher collected data from two top managers who head; Human resource section and Operations section.

The interview guide consisted of three parts which were – part A consists of organizational data, part B was compensation strategy and firm performance questions and finally part C contained questions about firm performance. Office of the Auditor General is a government institution and has two key departments headed by managers and from those managers data was collected from Human Resource Manager and Operations Manager by interviewing them by use of the interview guide.

3.3 Data Analysis

Data collected was analyzed using content analysis technique because the study obtained data which was qualitative in nature. The approach allowed categorization and making valid and replicable inferences to the context. The technique was chosen on the basis that most of the data collected was in qualitative form. Content analysis will be used to analyze data from open-ended questions. To get predictable, directed and comprehensive results from an open-ended questions, one has to use content analysis (Creswell 2003).

Content analysis is an analysis strategy that gives overall approach that enables systematic examination of information or data provided objectively (Marshall 1995). Content analysis was relevant to this study because it does not have barriers on respondents' answers and

they can fully express their opinion. Difficult issues to be studied are explored and analyzed by content analysis.

CHAPTER FOUR: DATA ANALYSIS AND PRESENTATION

4.1 Organizational Information

The Office of the Auditor-General (OAG) is an old office which was constituted long time ago. The respondents mentioned that the Office of the Auditor-General has been in existence since independence specifically year 1955. This office is essential for carrying out various audits in government institutions and other organizations as it is mandated to carry out its operations. It was found that it is a large office and is composed of 1250 employees. It was established that the Auditor-General employees are not all on permanent and pensionable terms. Some of the employees are on contract and probation basis. However, the employees who are on probation should be confirmed to permanent unless they breach the terms of employment contract.

4.2 Direct Financial Compensation and Firm Performance

Employees are offered various direct financial compensation in line with employees' remuneration Act. It was found that in the Office of the Auditor-General, 100% of the employees have direct financial compensation in terms of salary. Bonuses are also paid to the employees for outstanding performance as stipulated by the office. Bonuses are rewarded to employees who achieve outstanding performance indiscriminately.

Direct financial compensation to employees is always important in improving organizational performance. It is a source of motivation to the staff and rejuvenate their performance. The study found that, in the office of the Auditor-General, direct financial compensation facilitates the employees to offer their desired services for the daily running

of the organization. It was also found that this improved and increased their productivity and efficiency. Good performance of organizations are achieved when employees are comfortable and financially compensated commensurately.

It is important for any employer to comply with the terms and conditions of employment in the public service. The office of the Auditor-General is also a public institution and therefore is expected to comply with the terms. It was found that office of the Auditor General complies with the terms and conditions in the following manner; adhering to the terms and conditions; following the Human Resource (HR) policies and Code of Regulations (COR). HR policies stipulate all the terms and conditions that employers should adhere to in the public service offices. The Office of the Auditor-General has complied and it was found that compensation to the employees done according to the requirements of HR and COR.

4.3 How Office of the Auditor-General has ensured the amount paid as Salaries are standardized with the current Economic Trends

There have been inflations in the country's economy due to various factors, both natural and human which has affected the country's economy. Some of these human factors are poor political environment that leads to poor competition in the market and also Stock exchange is affected and this weakens our currency and raises the cost of living. This, therefore compel the office of the Auditor-General to ensure the amount paid as salaries is standardized with the current economic inflationary trends. The OAG offers its employees automatic annual salary increment to safe guard the inflation and for the office to remain competitive. It also carries out job evaluation and matching job role size and the salaries.

4.4 Measures taken to improve on Direct Financial Compensation

Measures being taken by the Office of the Auditor-General to improve on the direct financial compensation for its staff are reviewing salaries, paying bonuses and promoting employees. It was found that some of the critical measures that are taken are promoting employees, awarding bonuses for good performance by employees and salary reviews (Figure 4.1).

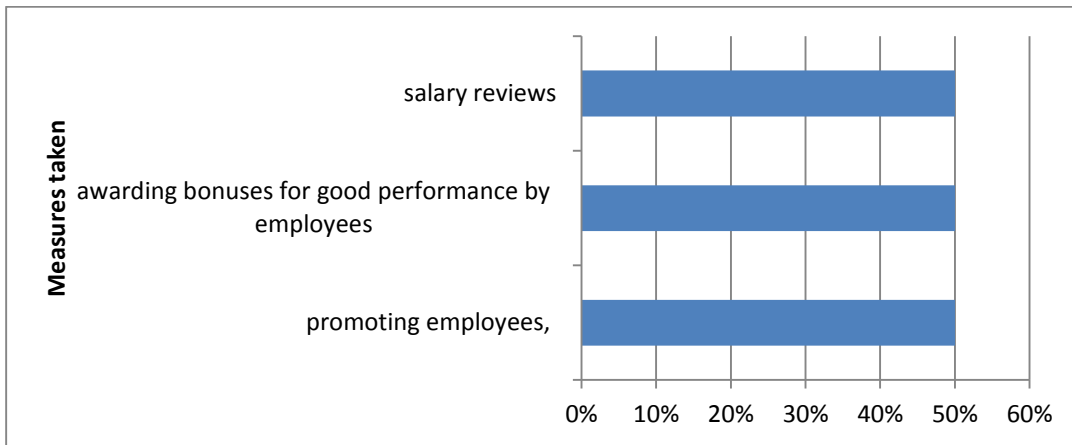


Figure 4.1: Measures taken by the Office of the Auditor General in Kenya to improve on the direct financial compensation

4.5 Indirect Financial Compensation and Firm Performance

It was observed that other than direct financial compensation offered to employees there is also indirect financial compensation that the Office of the Auditor-General gives to employees. These are to ensure the welfare and career development of the staff is well taken care of. The OAG provide various indirect financial compensation such as medical insurance cover, paid leave and sponsoring the training of employees to capacitate them for efficient productivity and good performance (Figure 2).

The indirect financial compensation has helped the Office of the Auditor-General to improve on performance in many ways. Medical insurance cover is very important since it helps in the improvement of the employee wellbeing and good health. The training through sponsorship offered to the employees is also important in their career progression, building their confidence, provision of quality reports and help in retention of the staff. Paid leave helps employee to meet financial obligations and this improves their morale resulting to high performance by the organization. The indirect financial compensation offered by the Office of the Auditor-General are all important in the performance of the employees as mentioned by the respondents.

Medical insurance cover was the type of indirect compensation which contributed more on the performance of the Office of the Auditor-General. Training through sponsoring employees is another factor which has helped the office to improve on performance. Due to the sponsorship offered to the employees, good skills are acquired and this helps to improve on performance resulting to good performance by the organization.

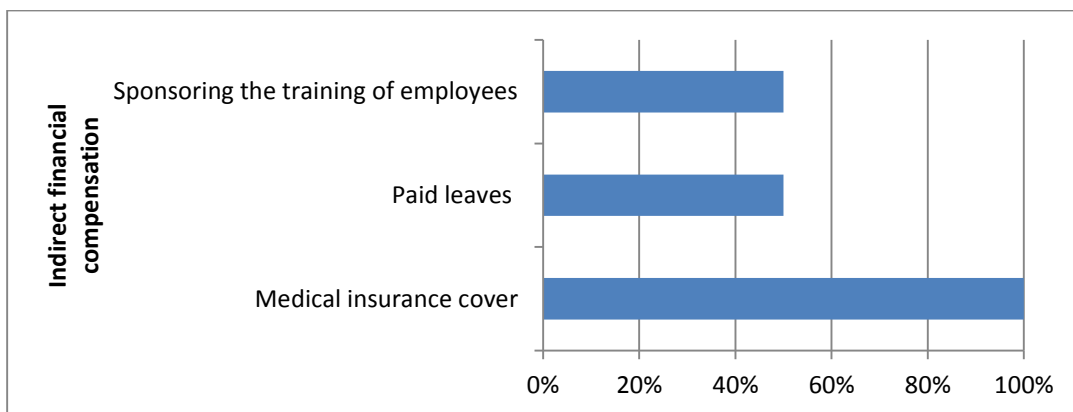


Figure 4.2: Indirect financial compensation that the Office of the Auditor-General gives to employees

There are measures that the Office of the Auditor-General wants to put in place for its employees in order to improve on performance. The measures that the OAG is working on is improving on retirement benefits and increase medical cover to employees. It was found that the Office of the Auditor General always focuses on giving the employees a better retirement benefits. The Office of the Auditor-General as an employer contributes some percentage of employees' gross salary into the pension scheme. Employee on the other hand remits some percentages to show commitments for their pension contributions. It was found that good health is directly proportional for good performance and growth of the Office of the Auditor-General. Therefore, the office wants to increase insurance health cover limits to enable employees to access good health facilities. This would keep the employees' health in good condition to work effectively and efficiently for the Office of the Auditor-General.

4.6 Non-Financial Compensation and Firm Performance

The type of non-financial compensation which the Office of the Auditor-General offers to employees to help improve on the performance of the office are safe working environment, fair and appropriate policies which helps in improving job satisfaction of employees. Non-financial compensation offered by the Office of the Auditor-General helped in the improvement of performance through safe working environment which improve on the reputation of the office thus attract the best employees. Safe working environment contributed to improve on job satisfaction of employees. This factor is essential for organizations to consider when focusing on the firm performance. Ensuring policies are fair and appropriate is another factor that helps improve on the performance of the Office of the Auditor-General.

The type of non-financial compensation which has contributed more to the improvement of the Office of the Auditor-General performance are fair and appropriate policies. One of the non-financial compensation that was listed as key in improving performance was ensuring policies are fair and appropriate to all. It was found that if policies are fair and appropriate, employees are comfortable working in the organization and this gives the Office of the Auditor General an upper hand in improving on its performance.

4.7 Balance Scorecard and Firm Performance

In monitoring the organization performance and employees performance, balanced score cards are used to verify and monitor the trend within the stipulated time. This is a routine check which are monitored to focus on the performance of the organizations. The balance scorecard has helped the Office of the Auditor-General to improve on performance because it helps the staff in meeting their targets and this implies the office satisfies customers by meeting their expectations, targets and deadlines set by customers which contribute to improve on performance. Without balance scorecard, an organization will not be in a position to where it is in terms of performance and where it will be in future.

Customer perspective is an important tool of performance measure thus it has helped the OAG to monitor on performance. The Office of the Auditor-General has many clients who have high expectation to be met in regards to the services offered. The customers are free and allowed to give feedback on the services they are offered. These feedbacks from customers are essential as they guide organizations to know their strengths and weak point. Objective critics from clients are essential to the performance of organizations and the OAG has provided this platform to interact with the clients so as to provide quality services.

The respondents mentioned that, customers perspective helped the office to improve on its performance by requesting quality reports that are simple to understand, the office also gives reports that are based on factual data that can be cited anywhere thereby upholding their integrity and maintain the organization to client relationship.

Learning and growth perspective has contributed to the performance of the Office of the Auditor-General in several ways. Most organizations including the Office of the Auditor-General embrace learning and growth of the employees because if it is well done, it translates to good organizations performance. Learning can be implemented in various models depending with the organization. Skills are passed through office training, prolonged experience in the organization or by attending learning organization systems through sitting in a class. Respondents of the Office of the Auditor-General mentioned that improving skills of the employees through learning and growth improves performance of the office. It was also found that learning and growth improves professionalism at work thus improving morale and confidence of the staff. Giving opportunities to employees to learn new skills and grow improve their confidence and efficiency. New challenges which emerge motivate employees to learn and also to apply the skills acquired which is essential in improving the performance of the Office of the Auditor-General.

The Office of the Auditor-General has to put several measures in place to improve on performance. One of the measures is by improving on staff welfare and benefits which will promote teamwork and encourage high quality work production. Another measure the Office of the Auditor-General should put in place to improve on performance is by improving on compensation to staff and this will lead to retention of the best employees

resulting to improved performance of the Office of the Auditor-General. Creating a good working environment is another measure which will contribute to high performance of the office because good working environment is conducive and habitable to employees and this helps to improve on the performance of the Office of the Auditor-General.

CHAPTER FIVE: SUMMARY CONCLUSION AND RECOMMENDATIONS

5.1 Summary of Findings

Office of the Auditor-General is a large institution with about 1250 employees and has been in existence since independence. The office therefore require strategic compensation either financial or non-financial for efficient performance. The Office of the Auditor-General has infrastructures and well laid down policies and procedure of conducting its duties to ensure that the reports they give to the customers are accurate and factual. The findings revealed that, the OAG has employees whose terms are some on permanent terms, others on contract terms and others on probation.

It was found that direct financial compensation facilitated the employees to offer their desired services for the daily running of the organization. Direct financial compensation acts as a source of motivation to staff and rejuvenates their performance and so it is important since it helps in improving the organizational performance. Indirect financial compensation like medical cover has an impact on employee's health and so it was found that good health is directly proportional to good performance and growth of the Office of the Auditor-General. The findings revealed that, non-financial compensation such as good working environment has contributed to job satisfaction at the Office of the Auditor-General. Fair and appropriate policies has brought about equity and as a result, there is improved performance at the Office of the Auditor-General.

The researcher found that, customer perspective has contributed to the OAG monitoring its performance through feedback received from their customers. Customer perspective has contributed to the performance of the OAG through objective critics from clients which are essential and the OAG has provided this platform to interact with client in-order to get feedback from them so as to provide quality services in return. It was found that, for the OAG to uphold integrity and maintain their client relationship, they give their clients reports that are based on factual data that can be cited anywhere. Learning and growth perspective was found to be a measure that helped the office to identify the weak areas of performance and improved on them through training of employees. It was also found that learning and growth improves professionalism at work thus improving morale and confidence of the staff. Balance scorecard tools used such as customer perspective and learning and growth perspective have contributed a great deal in enhancing the performance of the Office of the Auditor-General.

5.2 Conclusion

The study showed how direct financial compensation contributed to the performance of the Office of the Auditor-General. Salaries and Bonuses were instrumental on the improvement of the performance of the Office of the Auditor-General. Medical insurance cover and retirement plan being the indirect financial compensation used by the Office of the Auditor-General helped improve on performance. A positive contribution by indirect financial compensation to the performance of the Office of the Auditor-General realized acts as a baseline to other organizations to imitate.

Another factor which the Office of the Auditor-General banked on to improve on performance was non-financial compensation. Non-financial compensation like good policies and good working environment are important on improving the performance of Organizations as seen in the case at the Office of Auditor-General. The Office of the Auditor-General used customer perspective as a yardstick to measure the performance and the results they received were positive and satisfying. Another tool of measuring performance that was embraced by the Office of the Auditor-General was learning and growth perspective where skills are passed through office training which helps the employees to gain knowledge. The Office of the Auditor-General sponsor their employees to attain more knowledge by attending learning organization systems through sitting in a class and by so doing, the results were found to have a positive impact of the performance.

5.3 Recommendations

The office should continue improving the employee skills through sponsoring various training programs which are in line with the objectives of the Office of the Auditor-General. Another area that the researcher found important for the OAG to consider improving on was non-financial compensation like career advancement will motivate employees to give their best service and this will improve on the performance of the organization. Work life balance enhances employee commitment to the organization leading to the organization retaining the best employees therefore the OAG should consider implementing it. Employee voice allows employees to air their views and participate in decision making and this makes them have that ownership attitude of the organization. Some of the measures that the Office of the Auditor-General in Kenya should put in place

to improve on its performance are improving staff welfare and benefits, improving on compensation in terms of salary increment and also give commissions to staff and creating good working environments. Creation of good environment will boost the confidence and efficiency of the staff since some of them have the fear of being sacked or not confirmed on permanent and pensionable basis.

Internal business process is an important measuring tool of performance which the Office of the Auditor-General should not ignore. Communication channels are very important because they create good relationship between employee to employee and manager to employee as these mutual relationships are key in the performance of any organization that wants to improve on its performance and the OAG is not an exception. The Office of the Auditor-General should continuously embrace and thrive to improve on the quality and enhance professionalism among employees. The office should also focus on the services offered to customers by ensuring customer expectations are met. The staff members should also focus on addressing any emerging issues promptly and efficiently.

5.4 Limitations of the study

Some of the limitations of the study were informants were too busy with their office work and it took a lot of time for them to be available for the interview. Also there was the tendency by interviewee to volunteer only the positive side of information despite the assurance from the researcher that the information offered was purely for academic use and would be no wide circulation of the findings. This notwithstanding, the limitations did not have any adverse effects on the findings of the study.

5.5 Suggestions for further studies

The study suggests further research on the effect of compensation strategy on the performance of the county government. The study will supplement the findings of this study by providing information on the effect of compensation strategy on public institutions and the role of compensation strategy in influencing organizations performance. This research therefore should be replicated in other public institutions around the country in order to establish whether there is consistency in the institution.

Secondly, since this study sought to establish the effect of compensation strategy on performance of the Office of the Auditor-General, similar studies should be done in other different private organizations as well as non-governmental organizations that offer services for comparison purposes and to allow for generalization of findings on the effect of compensation strategy on performance in different organizations.

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APPENDICES

APPENDIX I – LETTER OF INTRODUCTION

Letter of introduction to the respondent

University of Nairobi

School of Business

Department of Business Administration

P.O. Box 30197

NAIROBI

Dear respondent,

COLLECTION OF SURVEY DATA

I am a postgraduate student at the University of Nairobi, School of business. In order to fulfil the degree requirement, I am undertaking a management research project on effects of compensation strategy on performance at the office of the Auditor General. You have been selected to form part of this study therefore, I kindly request your assistance to fill the interview guide. The information provided will be used exclusively for academic purposes and will be held in strict confidence.

Thank you.

Yours faithfully,

Christine N. Muthengi

Dr. Mercy Munjuri
Supervisor

APPENDIX II: INTERVIEW GUIDE

SECTION A: Organizational Information

1. For how long has the Office of the Auditor General been in existence?
.....
.....
2. How do you categorize the Office of the Auditor General in terms of size, small, medium or large?
.....
3. How many employees are there at the Office of Auditor General.....
.....
4. Are all employees of Office of the Auditor General on permanent and pensionable terms or which terms of service are they in?
.....

SECTION B: Compensation Strategy {HR Manager}

5. Which types of direct financial compensation are offered at the Office of the Auditor General in Kenya?
.....
6. How has direct financial compensation to employees helped the Office of the Auditor General to improve on its performance?
.....

7. How does the Office of the Auditor General ensure that it complies with terms and conditions of employment in the public service?
8. How has the Office of the Auditor General ensured the amount paid as salaries are standardized with the current economic trends.....
9. What measures is the Office of the Auditor General in Kenya taking to improve on their direct financial compensation?.....
10. Which types of indirect financial compensation are offered at the Office of the Auditor General in Kenya?
11. How has indirect financial compensation to employees helped the Office of the Auditor General to improve on its performance?
12. Which type of indirect financial compensation have contributed more on the performance of the Office of the Auditor General?.....
13. What measures does the Office of the Auditor General in Kenya wants to put in place to improve on their indirect financial compensation?.....
14. Which types of non-financial compensation are offered at the Office of the Auditor-General in Kenya?

.....
15. How has non-financial compensation to employees helped the Office of the Auditor General to improve on its performance?

.....
16. Which type of non-financial compensation have contributed more on the improvement of the performance of the Office of the Auditor General?.....
.....

SECTION C: Firm Performance {Operations Manager}

17. Which types of balance scorecard measures are used at the Office of the Auditor General in Kenya?

.....
18. How has balance Scorecard helped Office of the Auditor General to improve on its performance?

.....
19. How has customer perspective helped the Office of the Auditor General to improve on its performance?

.....
20. How has internal business process perspective helped the Office of the Auditor General to improve on the performance?

.....
21. How has learning and growth perspective contributed to the improvement of the performance of the Office of the Auditor General?

22. Suggest measures that the Office of the Auditor General in Kenya can put in place to improve on their performance?.....

.....