

**FACTORS INFLUENCING EMPLOYEE PERCEPTION OF EQUITY
IN COMPENSATION AMONG MEDIUM SIZED COMMERCIAL
BANKS IN NAIROBI**

By

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Declaration

I hereby declare that this is my original work and has not been submitted for any award at any other institution.

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Dedication

I dedicate this research project to my lovely wife Jeniffer Ngali who has been a great source of inspiration and joy in my daily endeavors to better my best. To my late mother, Mary who made me be whom I am. Mum; your memories have been a pillar to me.

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Abstract

The main purpose of the study was to investigate factors influencing employee perception of equity in compensation in medium sized commercial banks in Nairobi. Employees perceive equity in compensation when their input output ratio is equal compared to other reference group. On the other hand perception is a complex process by which people select, organize and interpret sensory into stimulation into a meaningful and coherent picture of the world. Compensation includes direct monetary payment, indirect payments in the form of employee benefits and incentives to motivate employees to strive for higher levels of productivity.

The population of this study consisted of all the employees in the thirteen (13) commercial medium sized banks in Nairobi. This was a cross sectional descriptive survey design since data was collected and provided insight into the research problem by describing the variables of interest among the units of study.

The study found out that perception of fairness in compensation affects the relationship with your colleagues as well as perception of fairness in compensation influence your motivation to work, external equity influence on wages over internal equity influence, workers often rank job security, working conditions, advancement opportunities, management appreciation, relations with co-workers, and flexibility of hours or job assignment ahead of compensation. It recommended that further research should be done on the relationship between perception of equity and job satisfaction under the other financial institutions.

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CHAPTER ONE: INTRODUCTION

1.1 Background of the study

Countries all over the world thrive economically when the standards of people is continuously improved (Kent et al, 2008). Human resources are key inputs in product development and service delivery in an organization. How an organization manages its human resources forms an integral part of how it's going to achieve its objectives (Armstrong, 2006). Since the early 1980s, compensation professionals began designing and implementing compensation that contribute to the company's competitive advantage. Equitable compensation practices contribute to competitive advantage by promoting more productive and skilled workforce For example, well-designed merit pay programs reinforce excellent performance by awarding pay raises commensurably with performance attainments (Pfeffer, 1995).

Employment is typically characterized as an exchange relationship. Employees provide organizations with something of value (their lab our) and in return receive something of value, (Rynes et al, 2000). Warren (1992) argues that Companies encounter constantly changing needs which require new approaches. In the field of compensation management, compensation professionals can help managers handle new developments with fresh ideas. These business consultants must understand the company's view of and commitment to quality. Likewise, they should have a distinct idea of company team definition. Compensation professionals must also realize the value of employees, customer service, learn the process of corporate reorganization and value the interests of shareholders.

Adams (1963) notes that an employee will compare his/her ratio of outcome he/she gets from his/her employer to the input he/she contributes to the organization with the same ratio inside and outside the organization. Bank employees who perceive equitable compensation may be more motivated to perform better and support the banks goals and objective(Kent et al (2008).He further suggests that employees who perceive equitable compensation treatment may be more motivated to perform better or to support a company's goals. Individual employees, however, perceive equity in many different ways. Therefore, it is difficult to specify one definition of equity that is applicable to all situations. Equity in compensation plays a key role in human resource management strategy development and control.

1.1.1 Compensation

Cascio (1987) defines compensation as a form of pay which includes direct monetary payment, indirect payments in the form of employee benefits and incentives to motivate employees to strive for higher levels of productivity. Compensation may be defined as money received for the performance of work plus many kinds of benefits and services that organizations provide their employee. (Cole, 2002) Compensation is made up of basic pay, benefits and incentives. Basic pay is paid based on an hourly, daily, weekly, bi-weekly or a monthly rate. The base pay is typically used by employees for ongoing consumption. Benefits are indirect financial and non financial payments employees receive for continuing their employment in the company. There is a wide variety of employee benefits, such as paid time-off, insurances (life insurance, medical/dental insurance, and work disability insurance), pension plan, company car, and more. A benefit plan is designed to address a specific need and is often provided not in the form of

cash (Kent and Ken, 2008). Armstrong (2004) defines incentives as employee motivational program designed to encourage commitment to increasing productivity or in achieving some worthwhile objective such as reducing the number of man-hour lost due to accidents. They can be classified into individual, group and organization –wide incentive plans.

Compensation accounts for one of the greatest investments an organization makes. Although a fair compensation is the cornerstone of the contractual and implied agreements between employees and employers, the underlying assumption is that pay can directly influence behavior. An employee's compensation affects his commitment to the company. Employees who are paid minimum compensation or a small compensation are likely to want to earn more either through a promotion or compensation increase, or by looking for work elsewhere. They are likely less committed to the company, because the company has not invested as much money in them through their salary as it has in other employees. Employees who are compensated fairly are likely to be more committed to the company because they do not want to lose their high-paying jobs (Martocchio, 2000).

The compensation package is one of the most obvious and visible expressions of employment relationship. It is the main issue in the exchange between employer and employee, expressing the connection between the labor market, the individual's work and the performance of the employing organization itself (De Silva, 1998). He further notes that compensation represents the most important element in the employment relationship and is of equal interest to the employer, employee and government. Compensation is significant to the employer because it represents a significant part of costs, increasingly

important to the employees' performance and to competitiveness and affects the organization's ability to recruit and retain labor force of quality. Compensation is fundamental to the employees' standard of living and is a measure of the value of his/her services and performance. Compensation affects Governments' aspects of macro-economic stability such as employment, inflation, purchasing power and socio-economic development in general.

1.1.2 Equity in compensation

Equity is defined as anything of value earned through providing or investing something of value. Fairness is achieved when the return on equity is equivalent to the investment made. Employees perceive equity when their input and output ratio are equal compared to other reference group (Armstrong, 2006). The inputs that the employee brings to an organization would be time, efforts, loyalty, and qualification, flexibility in terms of work hours, experience, enthusiasm and personal sacrifices. On the other hand output would include recognition of work well done, work itself, advancement and growth, salary Increment and achievement (Traupmann et al, 1978). According to equity theory, people evaluate their relationships with others in terms of rewards, costs, investments, and profits. They expect what they invest and gain from a relationship is proportional to what the other party in the relationship invests and gains (Adams, 1965).

Most people in organization work to gain rewards for their effort. Employees are considering basic pay or variable pay the extent to which they consider the compensation to be equitable often affects their performance, how they view their jobs and employers (Carell et al, 1978). Equity in compensation is a central theme in human resource

management. An organization approach to equity is as important as the actual compensation programs it implements. Kent and Ken (2008) suggest that companies tend to focus on external equity especially when coming up with compensation structures and programs that are competitive in the labor markets. Equity examines and articulates the process in ascribing fairness to the exchange relationship between an employee and employer. The exchange between the two is not purely an economic matter, although significant, as there are elements of justice involved that supervene economics and underlies perceptions of equity or inequity (Adams, 1963). Equity theory expands on the anxiety and frustration produced by cognitive attributes the dissonance to the perceived inequity a person ascribes to a social exchange process. With this understanding of dissonance as the foundation of equity theory, equity theory explains how people's perceptions of how fairly they are treated in social exchanges at work (e.g., amount of pay increase each year, how well their supervisor treats them, etc.) can influence employees' motivation. Employees will compare their actual ratio to their perceived one (Ivancevich et al, 2005).

Adams (1965) equity theory suggests the following; compensation allocation is perceived to be to be fair then motivation among the employees is sustained; secondly is inequity that is underpayment in this case an employee is motivated to seek justice hence work motivation is disrupted and thirdly is inequity in terms of overpayment which could cause a problem of inefficiency among employees, in other cultures they could lose face. This is a clear indication that an employee will be more productive when compensation is fair.

1.1.3 Employee perception

Perception can be defined as a process by which individuals organize and interpret their sensory impressions in order to give meaning to their environment. Perception is not necessarily based on reality, but is merely a perspective from a particular individual's view of a situation. In dealing with the concept of organizational behavior, perception becomes important because people's behavior is based on their perception of what reality is, not on reality itself; the world as it is perceived is the world that is behaviorally important (Robbins et al, 2004). Bereslon and Steiner (1964) defines perception as a complex process by which people select, organize and interpret sensory into stimulation into a meaningful and coherent picture of the world. Barber et al (1976) refers it as the process of receiving , selecting , acquiring , transforming and organizing the information supplied by our senses.

Robison et al (2004) further notes that factors influencing a person's perception can be broken down into three main categories. These include: the situation, the perceiver and the target. For example the factors in the situation may include compensation, time or work setting. Whereas the factors in the perceiver may include attitude, motives, interests and expectations. Lastly, the factors in the target may include motion proximity and similarity. Employee opinion surveys are widely used for gathering and assimilating human resource related data in companies and agencies of all sizes across the world (Kraut, 1996). They have the potential to improve dramatically workplace environments and can be used to identify emerging hotspots and mitigate the downside of organizational change initiatives. They can also alleviate absenteeism and stress, address

issues of bullying and harassment and accurately identify workplace psychosocial risk factors (Cotton and Hart, 2003).

Employees' perceptions in an organization are crucial to researcher as employees are the driving force behind the success of any business (Ngang'a 2003; Kiiru, 2006 Kananu 2007). Mullins (1999) stresses the need for managers to be aware of the perceptual differences between themselves and that of their employees which may give rise to conflict. Perception is influenced by intelligence, personality, expectation, motivation and interest (Bennett, 1997). He further argues the case for managers to understand the process of perception in order to ensure that employees perceive the organization's objectives in a similar manner, provide equity policies which will motivate workers and feel appreciated and this will enable the managers and employees to interpret things in the same way.

Law and Wong (1998) also found that bank clerks in Hong Kong compared themselves to other clerks in the same office. If the actual ratio matches with their perceived one, reward equity is achieved. In contrast, if discrepancies occur, reward inequality is resulted. Armstrong (2006) states that equity involves feelings and perceptions and is always a comparative process. He further advances the two forms of equity as suggested by Adams (1965) i.e. Distributive and procedural equity, distributive equity deals with fairness with which people feel they are rewarded in accordance with their contribution and in comparison with others; Procedural equity is concerned with the perceptions employees have about the fairness with which company procedures in such areas as performance appraisal, promotion and discipline are being operated. An employee's

perception of equity is determined through comparing his inputs/outcomes ratio to that ratio of others inside and outside the employing organization. On the one hand, inputs here include all the contributions that the employee brings to the organization such as experience, time, effort, etc. On the other hand, outcomes include all the rewards/outputs that the employee receives from his organization in return to his contributions, and these include motivators and hygiene factors. Employees' perception of equity in compensation can influence a company's ability to attract, retain and motivate its employees to high levels of performance (Adams, 1963).

1.1.4 Factors influencing employee perception of equity in compensation

Employee perception of equity in compensation is the degree to which the actual compensation of an employee matches what he or she thinks to deserve. High compensation equity means high employee satisfaction with his or her job, low compensation equity increases the potential for absenteeism, grievances, strikes, and turnover. Also called compensation satisfaction (Adams, 1963). Robison et al (2004) notes that employees' perceptions of the compensation provided to them by their organization can influence employees' attitudes.

Two key factors that appear to influence the perception of equity in compensation by employees are compensation satisfaction and compensation importance. Compensation satisfaction is determined by two perceptions. The first perception is based on how much compensation the employee believes he should receive, and the second perception is based on how much compensation is actually received. Employees will be satisfied if the two perceptions are identical (Law & Wong, 1998). Compensation is a reward, and

“satisfaction with a reward is a function both of how much is received and how much the individual feels should be received” (Ivancevich, & Matteson, 2005, p. 216). Weiner (1980) suggested that perception of equity in compensation are affected by compensation satisfaction i.e. the individual’s income level rather than just the discrepancy between the amount that should be received and the amount actually received.

According to Armstrong (2006) compensation importance influences employees’ perception of equity when, the employee has a better basis for compensation comparison because he or she has a better idea of what that employee's job and job performance is. All this creates a much higher potential for morale problems and turnover. He further states that employee perception of equity in compensation can be managed by paying people within a pay range, and by compensating for performance According to Lawler,(1981) however, it was inferred that some compensation are perceived as rights that are owed to employees by the organization. The study proposed and tested a model of compensation perception that incorporates all of these factors. Results suggested that compensation satisfaction and the perceived motive of the organization in providing compensation both have a direct relationship with employee attitudes. The perceived right status of compensation appeared to moderate this relationship.

1.1.5 Medium Sized Commercial Banks in Nairobi

Currently there are thirteen (13) medium commercial banks in Nairobi County (CBK Supervision Annual Report, 2010). They offer corporate and retail banking. Medium commercial banks are responsible for customer deposits in a safe and liquid form and lending the proceeds to worthy commercial, industrial, governmental and nonprofit

institutions. They in addition provide consultancy and advisory services to customers as well as safekeeping and trust services (Kenya Bankers Report, 2010). According to Kenya bankers' website Medium commercial banks in Nairobi have entry level, middle level management and management categories of employees and have adopted a compensation scheme management which includes the basic pay, benefits and incentive systems for each of these categories of employees. The compensation system is a hierarchy based on the value to the banks.

Employees who work in medium commercial banks in Nairobi will tend to compare their input output ratio with comparable others within the same banking peer group. If they perceive the compensation to be equitable they could gear their energies towards the success of these medium banks. The choice of method to use to manage employee performance is a challenge most medium commercial banks face that requires only those with the best mix of personnel and objectives to survive (CBK Supervision Annual Report 2010). Performance of medium sized commercial banks depends on how employees perceive that they are being compensated fairly comparable to others within and outside the organization (Adams, 1963).

1.2 Statement of the problem

In the global business environment employee perception, fairness in compensation, productivity and commitment issues are emerging as most critical workforce management challenges of the immediate, future drive by employee loyalty concerns, corporate restructuring effort and tight competition for key talent (Caplan, 1997). Employee perception of equity in compensation is important in human resource

management and should be carefully considered when a company sets its overall objectives. Equity in compensation can influence both intrinsic and extrinsic motivation of employees and their attitude towards job satisfaction (Kent et al, 2008). He further notes that equity and inequity are equally important and should be carefully considered when a company sets compensation objectives. Equity in compensation affects staff motivation and level of job satisfaction this may lead to high turnover while satisfaction among employees may increase their morale, productivity and organizational commitment (Adams, 1963). Employee perception affects working relationships in many ways relating to the factors of organizational behavior, such as: individual, group or structure. For example, based on the situation, perceiver and target we may have the perception that the people we are working with are no good at their job, and therefore we may tend to avoid working with them, in fear of being held responsible for their mistakes, and in doing so, affecting working relationship with team members, and ultimately, the effectiveness and efficiency of the organization (Robbins et al, 2004).

Medium sized commercial banks play a crucial role in the effective and efficient delivery of financial services which are core to the functioning of a state economy. Success of medium sized commercial banks in Nairobi is one of the major driving forces for economic growth. Employees play a crucial role in achieving objectives set by these banks. Medium sized commercial banks employ large numbers of people to facilitate service delivery, increase performance and improve the banks competitive position in the market. Perception of equity in compensation can positively or negatively affect the perception of employees working in the medium banks (CBK Supervision Annual

Report, 2010). Chew and Wirtz (2002) states that people who perceive equity in pay for a behavior are more likely to engage in the behavior again. They further note that the more motivated they are, the more likely these employees will be committed to their jobs and stay longer with the organization. Thus, ensuring low employment turnover and higher probabilities of smooth succession planning.

A study by Mohamed (2010) on employee perception of equity in compensation and job satisfaction in the Egyptian private universities revealed that positive relationship between perceptions of equity in pay where a motivator was the outcome in comparison, and job satisfaction. The study also revealed that there was no relationship between perceptions of equity and job satisfaction where a hygiene factor was the outcome in the comparison. These studies were carried out in a setting which cannot be generalized to banking industry in Kenya. A number of studies have been conducted on employee perception and factors that influence these perceptions (Khasian 2006; Kinanu 2006; Gathungu 2008; Limo 2008; Kizitos 2007 and Balozzi 2010). These studies focused on perceptions of employees on various independent variables like performance based pay, change management, performance contracting and staff welfare study. Kizito (2007) study focused on employee perception of pay, job satisfaction and organizational commitment of employees working in state Corporations in Kenya. The study revealed that salaries paid to the employees were not attractive vis-à-vis what was on offer in the market and that the pay on offer in the majority of the organization was not commensurate with qualifications, skills and experience. However no study has been done on factors that influence employee perception of equity in compensation among

medium sized banks in Nairobi County. This gap in knowledge has thus necessitated the proposed study. The research problem statement leads to the following question: What factors influence employee perception of equity in compensation in medium commercial banks in Nairobi.

1.3 Objective of the Study

To establish factors influencing employee perception of equity in compensation in medium sized commercial banks in Nairobi.

1.4 Significance of the Study

Managers in banks will be able to reduce the consequences of low levels of motivation and job satisfaction such as high turnover and increase positive work outcome such as performance through increasing perception of equity in compensation among employees.

This study is expected to stimulate interest in this subject among researchers and add to the literature currently available on perception of equity in compensation among employees. For academician; this study will form the foundation upon which other related and replicated studies can be based on

Employees working in these banks will be encouraged to value the input they bring into the banks and be aware of channeling equity in compensation issues before they develop to become problems.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

Equity in compensation is not a new idea or issue. It has been a long time favorite among behavioral and industrial psychologist researchers. Perception of equity among employees provides a framework for ensuring that employees are treated fairly with the aim of achieving organizational objectives. Equity in research has had more than one form; compensation in equity, procedural and distributive justice, job security and complexity, pay administration equity, promotion opportunity equity and evaluation criteria equity (Roberts et al, 1999). Several studies have been conducted on equity however theoretical ambiguous and methodological limitations of the results have not advanced our understanding of equity. Studies done include:

Deconinck (2007) analyzed the relationship among the perceived equity in compensation, job satisfaction and organizational commitment. Perception of equity in compensation was reported to have a great impact on organizational outcomes.

Lambert et al (2007) also studied the effects of distributive and procedural justice on motivation and job satisfaction among correctional staff. Procedural justice but not distributive justice was reported to have a significant impact on motivation and job satisfaction.

Equity in compensation can help retain ambitious, capable employees instead of losing them to competitors.

2.2 Compensation

Carrel et al (1978) defines compensation as a form of periodic payment from an employer to an employee, which may be specified in a contract. It may be paid in any frequency but, in common practice, is paid on monthly and not on hourly, daily, weekly, or piece-work basis. He further states that compensation is determined by market compensation rates for people doing similar work in similar industries in the same region. Compensation is also determined by the pay rates and salary ranges established by an individual employer. Compensation is also affected by the number of people available to perform the specific job in the employer's employment locale. Different scholars in different countries have defined the word compensation from different perspectives. Globally, almost every country views compensation as a measure of justice. Also, some countries (particularly developed ones) consider compensation as a means of protection against potential job loss. Compensation should be fair, irrespective of economic consideration. Many scholars believe that compensation is the outcome of productivity (Kent et al, 2008)).

The modern definition of compensation, however, considers both intrinsic and extrinsic components of compensation. While extrinsic compensation covers both monetary and non-monetary rewards, intrinsic compensation covers both monetary and nonmonetary rewards; intrinsic compensation reflects the employees' mental satisfaction with their job accomplishments Armstrong (2004). He further notes that Compensation comprises of three components the base salary, incentives and benefits. The base salary is clearly in the ownership of the top management of the organization and the Human resource management functions. The role of the base salary is to attract and retain the talents from

the market to work for the organization. The Incentives are the part of the compensation policy, which should be fully in the responsibility of the line management. The incentives helps to get the targets immediately and the targets can change quickly. The benefits have the retention role in the compensation strategy. The benefits should be fully driven by the Human resource management function and the line management should provide their own products and services as the benefits to the employees of the organization

The design and operation of compensation systems in many organizations have often been institutionalized by customs and practice, tradition and collective bargaining mechanisms. The level of compensation is influenced by beliefs about the worth of jobs, labor supply and demand either at national level or in response to the local labor market, remuneration policy and strategy of companies, strength of bargaining groups, economic factors such as unemployment levels and job security, the cost of living and the government intervention, where the government may intervene in the employment relationship in terms of attempting to influence wage inflation through initiatives introduced in the public sector and encouraging certain types of compensation such as profit sharing and share option schemes(Beardwell and Holden,1997).

Trembaly & Chenvert (2004) examined the effectiveness of compensation strategies in Canadian technology-intensive firms by using a survey of two hundred and fifty two (252) firms, which showed that technology intensity had a significant influence on compensation policies .Kilika (1999) in a case study of the Co-operative bank of Kenya went out to identify managers compensation preferences and also to assess the extent by which such preferences were being met by the existing compensation schemes. He found

out that managers had several needs which formed the basis for their preferences. His study revealed that preferences differed for different items of compensation and that the non-economic rewards were relatively more preferred to the economic ones. Amamo (2005) in her survey of factors associated with employee retention in FM radio presenters in Kenya site compensation as the factor most associated with employee retention.

2.3 Concept of equity in compensation

Armstrong (2006) states that equity or fairness is a key component in creating a successful compensation system. It can be defined in the following three ways: Workplace equity refers to the perception that all employees in an organization are being treated fairly. External equity in compensation exists when employees in an organization perceive that they are being rewarded fairly in relation to those who perform similar jobs in other organizations. Internal equity in compensation exists when employees in an organization perceive that they are being rewarded fairly according to the relative value of their jobs within an organization Perception of equity among employees provides a framework for ensuring that employees are compensated fairly with the aim of achieving organizational objectives. Equity in research has had more than one form; pay equity, procedural and distributive justice, job security and complexity, pay administration equity, promotion opportunity equity and evaluation criteria equity(Roberts et al ,1999). The main theories of equity include: equity theory, expectancy theory and social exchange theory. Equity theory advanced by Adams (1963) attempts to explain relational satisfaction in term of perception of fair/unfair distribution of resources within

interpersonal relationship. Equity is based on the idea that employees basically expect a fair balance between the input and output ratio. Equity Theory is fairly parsimonious.

The expectancy theory by Vroom (1974) this theory basically concentrates on the outcomes. Vroom proposed three variables which would enhance equity and in turn motivate employees. They are expectancy, instrumentality and valence. Expectancy is the belief that action or effort will lead to an outcome, instrumentality is the belief that if we do one thing it will lead to another and valence stands for value. He further argues that employee expectation can affect an individual's motivational. Therefore the amount of effort employees exert on a specific task depends on the expectations of the outcome which should be equitable. In social exchange theory that stems from Gouldners (1960) norm of reciprocity which simply argues that people ought to return benefits given to them in a relationship (Buren, 2005). According to this theory there is no equity when the cost and benefit are equal in a relationship, then that relationship is not equitable. Equity is a core concept in social exchange theory. Garhen et al (1995) defines equity as employees on assessment of whether he/she is being fairly treated. Equity can help retain ambitious, capable employees instead of losing them to competitors.

Equity in compensation also referred to as comparable worth is a reform effort to compensate different job titles the same based on their value to their employer regardless of the gender predominance of those working in such titles. There are various forms of equity in compensation namely internal and external equity, individual and personal equity. Organizations are also concerned that compensation rates among jobs within the

organization are perceived as equitable often referred to as internal equity. Internal equity is traditionally achieved through job evaluation (Armstrong, 2004).

Kent et al (2008) states that internal equity exists when an employer compensates commensurate with the relative internal value of each job. This is established according to the employer's perception of the importance of the work performed. Job-evaluation methods are often used to develop a job hierarchy that reflects the relative value of jobs on the basis of skill, effort, responsibility, and working conditions. A number of job-evaluation approaches have been developed. Such approaches include whole job ranking, classification, point factors, factor comparison, and slotting.

External involves two important activities commonly practiced by organization which are directly related to attracting and retaining employees i.e. labor market surveys of wages and benefits and job evaluation. They are concerned with assuring that the organization compensation system is perceived as equitable (Armstrong 2004). External equity exists when an employer pays a wage rate commensurate with the wages prevailing in external labor markets. Assessing external equity requires measuring these labor markets. There is, however, no single labor market for a particular job. Supply and demand differ substantially among markets, resulting in significant variation in wages across labor markets. The following factors contribute to these wage differences among markets: Geographic location, industry sector, union status organization size, product competition, company prestige, education and experience level of available work force. Some combination of these factors determines the labor market for a particular job. Employers

should carefully define the appropriate markets to assure accurate external wage comparisons (Kent et al, 2008).

Personal equity, involves no direct comparison of one individual's compensation with another's. Personal equity exists when an employer's compensation rate satisfies an employee's own perception of his or her worth. The standards applied by each person relate to that particular individual's previous experiences and his or her knowledge of the market value of similar jobs. These internal standards can determine the employee compensation satisfaction or dissatisfaction. (Armstrong, 2004). According Wayne (2006) equity in compensation is about achieving equal remuneration outcomes in an organization. It is about eliminating sex discrimination from the wage-setting system by ensuring that employers use gender-neutral and gender-inclusive criteria to determine the value of job components such as skill, responsibility, qualifications and working conditions. Employers that ensure they remunerate staff fairly are signaling their commitment to their employees. This typically translates into increased job satisfaction, greater employee productivity and improved employee loyalty.

2.4 Employee perception

Kotler (2000) defines perceptions as the process by which individuals select , organize and interpret information inputs to create a meaningful picture of the world. He further states that a motivated person is ready to act. How the motivated person acts is influenced by his /her perceptions of the situation. Employees develop set of filters through which they make sense of the conditions they are exposed into. Cole (1997)

defines employees as individual who, over a given time, invest a large proportion of their lives in their organizations. Unlike others resources in an organization, employees are complex human beings who are influenced by and can act on the basis of their perception.

Kelly (1995) calls employees perception as personal constructs, which channel the way employees conceptualize and anticipates events. Thus employees will most likely have perception of equity in compensation and how management should address compensation equity issues affecting them. If the perceived expectations are not met, then discontentment results may lead to poor performance and mass exodus of employees. Perceptions differs from one individual to another, (Mulins, 1999) consequently employees will perceive issues differently and will have different expectations from the same employer. Different people may physically see the same things but they may have their own individual interpretations of what it is. Employee perceptions of equity in compensation in an organization are crucial to its success; since the driving force behind the success rests on its employees. Employers need to be interested not only with the physical presence of the employee in the working place but more importantly their emotional presence (Beardwell, 1997).

2.5 Factors influencing employee perception of equity in compensation

Jackson (1996) states that within the context of employment, employees' perception of equity in compensation has been found to have significant personal and organizational consequences. Adams (1965) proposed an equity theory which stated that compensation

satisfaction is determined by an employee's perceived input-outcome balance. Employees feel satisfied when compensation is equitable and feel dissatisfied if an inequity exists. In other words, compensation satisfaction is determined by the perceived ratio of what employees receive from the job compared to how much they put into the job. In 1968, Locke presented a discrepancy theory to explain satisfaction. According to Locke's theory, satisfaction is determined by the difference between what the person desires and what is actually received (as cited in Lawler, 1971). Lawler (1971) built the Model of the determinants of compensation satisfaction. This model emphasized the importance of social comparisons and proposed that compensation satisfaction is "basically determined by the difference between perceived compensation and the person's belief about what his compensation should be" (Lawler, 1971, p. 214). Lawler (1981) identified two factors perceived amount that should be received, and perceived amount received. Omar and Shittu (2005) conducted a study of compensation satisfaction among supermarket employees in the U.K. The researchers used a non-experimental, quantitative design of employees who worked for Tesco, Sainsbury, Asda, and Safeway, which are leading food retail organizations in the U.K. Findings indicated that only 32% of employees were satisfied with their compensation and over 55% of employees were dissatisfied, very dissatisfied or extremely dissatisfied using three-way analysis of variance.

The importance of compensation variability in influencing compensation importance has been demonstrated empirically under carefully controlled conditions. For example, Rynes et al (1983) showed that compensation explained an average of 65% of the variance in subjects' overall evaluations of job attractiveness when presented with jobs having a wide range of salary alternatives, as compared to only 40% when presented with a

compensation range half as great (Cole,2002). He further notes the fact that the importance of compensation changes with variability in compensation alternatives can also be seen by contrasting the effects of compensation in vibrant versus stagnant economies. During the late 1990s, for example, the importance of compensation in shaping behavior could easily be observed as many of the most marketable employees bailed out of large, relatively stable employers to pursue much

The most general theoretical explanation for compensation importance is the fact that it is useful for obtaining so many other desirable things (Lawler, 1971). For example, in addition to Maslow's (1943) frequently mentioned "lower-order" needs (such as food and shelter), money can also pave the way toward social status, a good education for one's children, or making it possible to retire early and enjoy increased leisure. Another general explanation for the importance of compensation is that compensation is frequently used as a yardstick for social status (Frank, 1999) and personal accomplishment *visa vis* others, particularly among high achievers (Rynes&Bretz, 2002). Status and accomplishment-based signals associated with compensation appear to be particularly sensitive to relative pay, or pay comparisons, rather than absolute levels of pay. Equity theory (Adams, 1963) has long emphasized the importance of compensation comparisons to individuals' sense of fairness and well-being.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter contains research design, population, sample design, data collection and data analysis.

3.2 Research design

This was a cross sectional descriptive survey design. The design was preferred because of the cross sectional nature of data to be collected and provided insight into the research problem by describing the variables of interest among the units of study.

3.3 Population

The population of this study consisted of all the employees in the thirteen (13) commercial medium sized banks in Nairobi. The numbers of employees in the medium sized commercial banks in Nairobi were six hundred and thirty (630) comprising of one hundred and fifty (150) in the management level and four hundred and eighty (480) in the non-management level (Central Bank Supervision Report, 2010 p g 6). Appendix III

3.4 Sample design

The sample size was 190 employees which were selected by use of proportionate stratified random sampling method from the management and non-management cadre in each of the thirteen (13) medium commercial banks in Nairobi County. A sample size of

30% of the population was considered adequate to make inference about the entire population (Terrel, 1979).

Table 3.1 Sample design

Banks	Mgt	Non Mgt	Sample mgt	Sample Non mgt	Sample size
African Banking Corporation Limited	22	60	7	18	25
Consolidated Bank Of Kenya	26	64	8	19	27
Development Bank Of Kenya	13	37	5	10	15
Equatorial Commercial Bank Limited	15	45	6	12	18
Fidelity Commercial Bank	7	23	3	6	9
First Community Bank	12	38	5	10	15
Giro Commercial Bank	5	27	3	7	10
Gulf Bank	7	28	4	7	11
Guardian Bank	8	28	4	7	11
Habib Bank	16	44	6	12	18
K-rep Bank	5	30	4	7	11
Trans-National Bank	8	32	4	8	12
Victoria Commercial Bank	6	24	3	6	9
	150	480	66	124	190

3.5 Data collection

A semi structured questionnaire was used to collect primary data. The questionnaire was divided into three Parts Part A focused on demographic characteristics of the respondents. Part B was concerned with employees' perception of equity in compensation and C focused on the factors that influence employees' perceptions of equity in compensation. The respondents were sampled from the management and non management staff in the thirteen (13) medium sized commercial banks in Nairobi County. The questionnaires were self-administered.

3.6 Data analysis

The completed responses was analyzed by use descriptive statistics such as mean, standard deviation, frequency distribution tables while tables and graphs was used for presentation of findings to summarize and relate the perception of employee of equity in compensation which was obtained from the administered questionnaire.

o

CHAPTER FOUR: DATA ANALYSIS, PRESENTATION AND INTERPRETATION

4.1 Introduction

This chapter provides an analysis of data collected from the field. The results are presented in tables to highlight the major findings. They are also presented sequentially according to the research questions of the study. Mean scores and standard deviations and factor analysis was used to analyze the data collected. The raw data was coded, evaluated and tabulated to depict clearly the results of the problem encountered in performance of firms.

4.2 Response Rate

The research was conducted on a sample of 190 respondents from the selected banks to which questionnaires were administered. The study targeted on Management, Non-Management staff. However, only 120 questionnaires were returned duly filled in making a response rate of 63%, which is an adequate response rate for statistical reporting.

4.3 Demographic Characteristics of the respondents

Majority of the respondent were male at 56% while female was 44% implying that most of the workers for in medium sized commercial banks in Nairobi were male. From the findings, those banks that were locally owned are; K-rep Bank, Trans-National Bank, development bank of Kenya and fidelity Commercial Bank. Those with are owned by foreigners are; African Banking Corporation Limited, Consolidated Bank Of Kenya,

Equatorial Commercial Bank Limited, First Community Bank, Giro Commercial Bank, Gulf Bank, Guardian Bank, Habib Bank and finally Victoria Commercial Bank

Table 4.1: Distribution of the respondents by Age Group

Years	Percent
60 Yrs>	19.6
50-59	18.6
40-49	24.5
30-39	25.5
25-29	11.8
Total	100.0

The results presented in Table 4.1 show that a large proportion of 25.5% the respondents were aged from the ages of 30 to 39 years; this was followed by a significant percentage 24.5% that had also attained ages from 40 to 49 years, while 19.6%, 18.6% and 11.8% are for above 60 years, 50-59 years and 25-29 years respectively. The age composition shows that most of the respondents were of the 30 to 39 years and therefore had rich experiences, could also appreciate the importance of the study, while those below the age of 30 were not conversant enough with factors influencing employee perception of equity in compensation in medium sized commercial banks in Nairobi due to lack of experience.

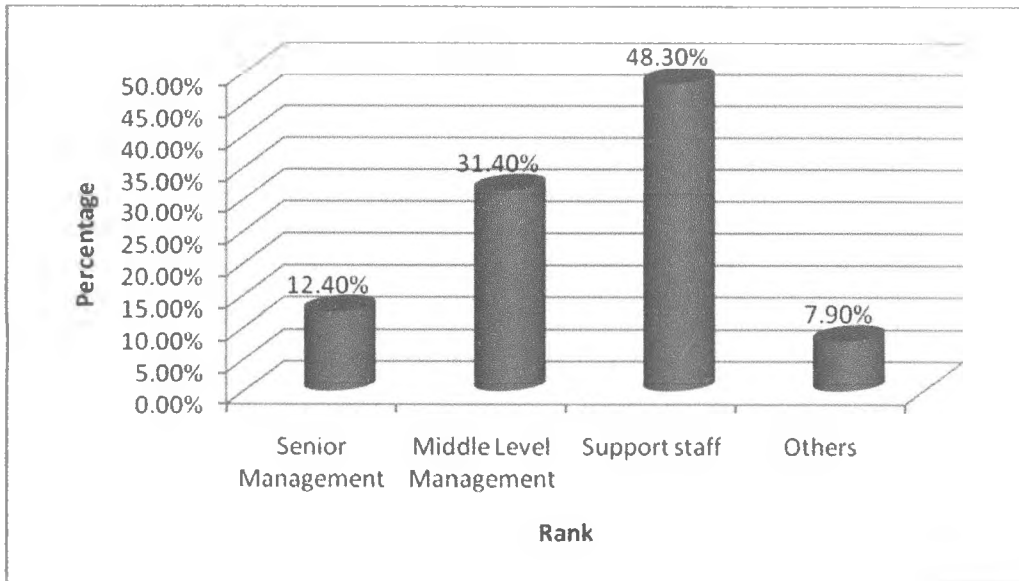


Figure 4.1: Position in the job place

Most of the respondents were support staff (48.3%). 31.4% of the respondents were of the middle level management while 12.4% were senior managers of the banks. This indicates that most of the employees in the banks are support staff.

Table 4.2: Length of Service in the Current Job

	Percent
3yrs and below	6.9
3 to 5 years	15.3
5 to 7 years	61.1
Over 7 years	16.7
Total	100.0

Most of the respondents indicated the 61.1% indicated that they had been in the company for 5-7 years, 16.7% over 7 years and 15.3% for 3-5 years while 6.9% indicated a period of less than 3 years. These findings indicated that majority of the staff at banks, have worked at their present company for a period of 5-7 years. From the findings 68.1% of the respondents had worked for the organization for a period of 6-15 years. 18.1% of the respondents had worked for a period of over 15 years. A percentage of 11.1% also had worked for the organization for a period of 3-5 years and 2.8%, 1-2 had worked for between 1 and 3 yrs. These findings indicate that majority of the staff at banks; have worked for a period of 6-15 years.

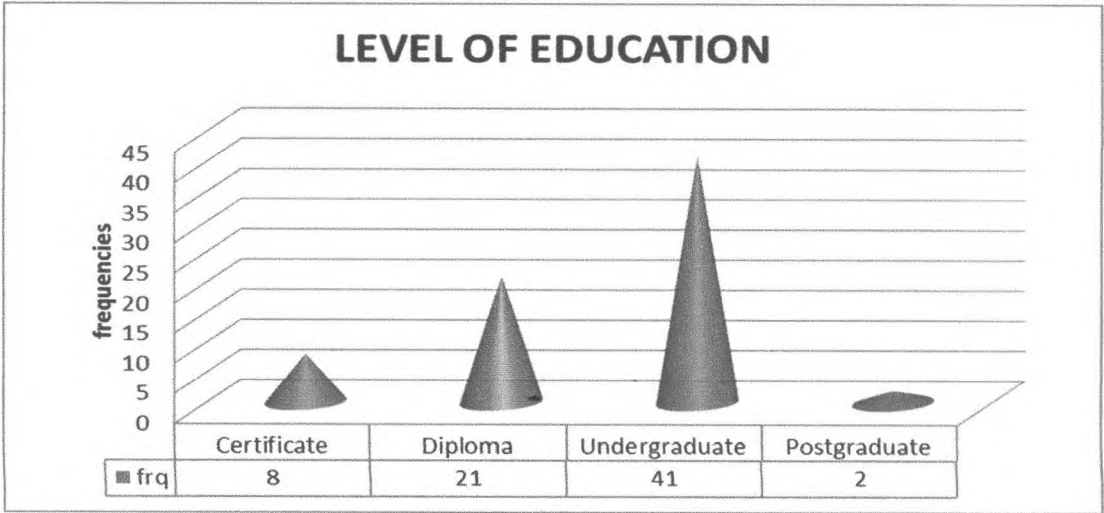


Figure 4.2: Level of Education of the Respondents

From the table, 56.9% of the respondents had undergraduate degree. 2.8% had postgraduate degree, 29.2% of the respondents were diploma holders while 11.1% said that they were certificate holders.

4.4 Employee Perception of Equity in Compensation

Research clearly demonstrates that employee' perceptions of compensation in equity, or inequity, can have dramatic effects on their motivation for both work behavior and productivity. Managers must therefore develop compensation practices that are both internally and externally equitable. Each of these compensation systems seeks to differentiate between the pay of average and outstanding performers. Employees must believe that wage rates for jobs within the organization approximate the job's worth to the organization. Also, the employer's wage rates must correspond closely to prevailing market rates for the employee's occupation. The bank compensation schemes is to the desired levels of employees inside and outside the organization, The bank ensures that the employees are satisfied with their compensation, The compensation perceived by employees is what is actually received, The bank pays close attention on the importance of compensation inside and outside the organization, The compensation I receive enables me to cater for my basic needs comfortably, The compensation I receive has changed my social status, The compensation I receive has enabled me to advance my education aspirations and The bank compensation schemes is to the desired levels of employees inside and outside the organization. The importance of compensation variability in influencing compensation importance has been demonstrated empirically under carefully controlled conditions. The study showed that compensation explained an average of 65% of the variance in subjects' overall evaluations of job attractiveness when presented with jobs having a wide range of salary alternatives, as compared to only 40% when presented with compensation. Status and accomplishment-based signals associated with compensation appear to be particularly sensitive to relative pay, or pay comparisons,

rather than absolute levels of compensation. The perceptions employees develop concerning their compensation are influenced by the accuracy of their knowledge and understanding of the compensation program. Perceived by the employees as actions to improve the overall working environment like any alternative solutions, these have varied risk ranging from increased employee turnover to substantial financial losses by the Company.

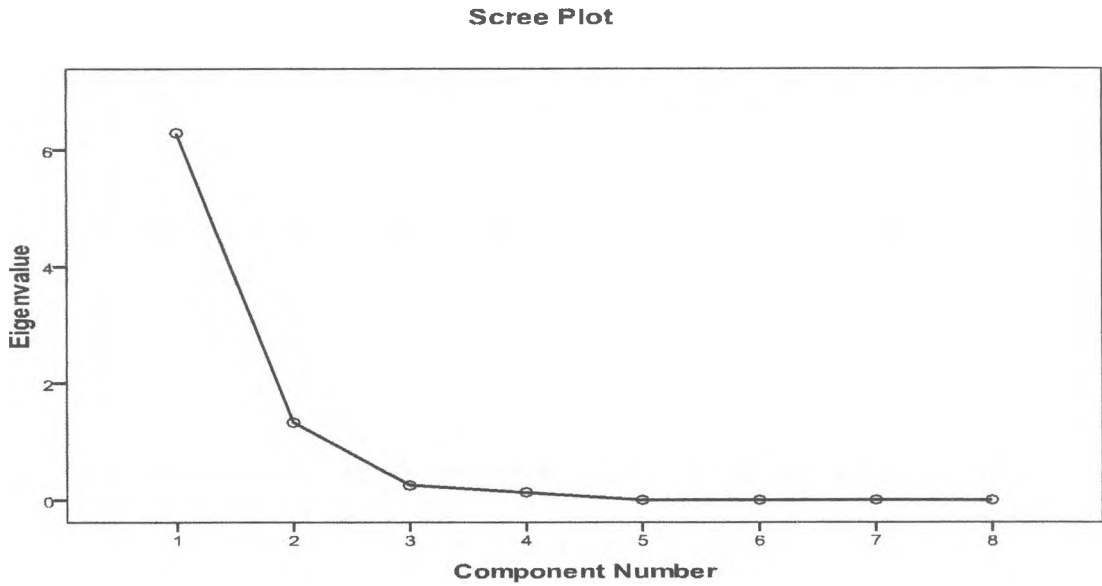
Perception of equity in compensation has been found to have significant personal and organizational consequences. Employees feel satisfied when compensation is equitable and feel dissatisfied if an inequity exists. Economic conditions and competition faced by employers can also significantly affect the rates they are able to pay. Competition and recessions can force prices down and reduce the income from which compensation payments are derived. In such situations, employers have little choice but to reduce wages and/or lay off employees, or, even worse, to go out of business.

4.5 Factors that Influence Employee Perception of Equity in Compensation

These were very important variables in analyzing and evaluate factors influencing employee perception of equity in compensation in medium sized commercial banks in Nairobi. The bank compensation schemes is to the desired levels of employees inside and outside the organization since perception of value is most often determined by evaluating both compensation and relational returns. Organizations create unique value propositions

by offering services and benefits that differentiate them from competition. Relational returns should be a strategic component of new total compensation systems.

Figure 4.3 Scree Plot



The scree plot graphs the eigen value against the factor number. The compensation I receive has enabled me to advance my education aspirations, The compensation I receive enables me to cater for my basic needs comfortably and The bank compensation schemes is to the desired levels of employees inside and outside the organization. From the third factor on the line is almost flat, meaning the each successive factor is accounting for smaller and smaller amounts of the total variance.

The study found out the perception of fairness in compensation affect the relationship with your colleagues as well as perception of fairness in compensation influence your motivation to work. Employee perceptions of equity and inequity are equally important and should be carefully considered when a company sets compensation objectives.

Employees who perceive equitable compensation treatment may be more motivated to perform better or to support a company's goals. Individual employees, however, perceive equity in many different ways. A company's approach to equity is as important as the actual compensation programs it implements. Companies typically emphasize external equity in the design of their compensation structures. This focus on external equity enables a company to develop compensation structures and programs that are competitive with other companies in appropriate labor markets. Perceptions of equity can also influence a company's ability to attract, retain, and motivate its employees.

Employees' perceptions of compensation in equity, or inequity, can have dramatic effects on their motivation for both work behavior and productivity. Managers therefore develop pay practices that are both internally and externally equitable. Employees believe that wage rates for jobs within the organization approximate the job's worth to the organization. Also, the employer's wage rates must correspond closely to prevailing market rates for the employee's occupation. Employees desire compensation systems that they perceive as being fair and commensurate with their skills and expectations. Pay, therefore, is a major consideration in Human Resource Management because it provides employees with a tangible reward for their services, as well as a source of recognition and livelihood.

The results show that workers often rank job security, working conditions, advancement opportunities, management appreciation, relations with co-workers, and flexibility of hours or job assignment ahead of pay. But because job security is linked to stability of income, it is possible that pay is more important than these studies indicate. The fact

remains, however, that an individual's perception of equity is strongly affected by factors other than pay.

External equity influence on wages over internal equity. Certainly the power of a wage or salary to attract employees is based solely on external equity considerations. The retention power of a wage or salary is also influenced heavily by external equity considerations. Finally, there are certain geographic constraints; even if an employee gets a suitable offer that meets all other criteria, it will be unacceptable if it is too far away. But even if employees don't quit, the negative consequences of retaining dissatisfied employees who feel that they are being treated unfairly can have significant motivational and cost implications for a company.



CHAPTER FIVE: SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter presents summary of findings as discussed in chapter four and interpretations of the data analysis, conclusions and recommendations based on the findings. The aim of the study was to explore the factors influencing employee perception of equity in compensation in medium sized commercial banks in Nairobi

5.2 Summary of findings

The study on the factors influencing employee perception of equity in compensation in medium sized commercial banks in Nairobi targeted on Management, Non-Management staff. However, only 120 questionnaires were returned duly filled in making a response rate of 63%, which is an adequate response rate for statistical reporting. The age composition shows that most of the respondents were of the 30 to 39 years and therefore had rich experiences, could also appreciate the importance of the study, while those below the age of 30 were not conversant enough with factors influencing employee perception of equity in compensation in medium sized commercial banks in Nairobi due to lack of experience.

The scree plot graphs the eigen value against the factor number. The compensation I receive has enabled me to advance my education aspirations, The compensation I receive enables me to cater for my basic needs comfortably and The bank compensation schemes is to the desired levels of employees inside and outside the organization. From the third

factor on the line is almost flat, meaning the each successive factor is accounting for smaller and smaller amounts of the total variance.

The study found out the perception of fairness in compensation affect the relationship with your colleagues as well as perception of fairness in compensation influence your motivation to work. Employees desire compensation systems that they perceive as being fair and commensurate with their skills and expectations and the results indicated that External equity influence on wages over internal equity influence, workers often rank job security, working conditions, advancement opportunities, management appreciation, relations with co-workers, and flexibility of hours or job assignment ahead of compensation

5.3 Conclusions

The findings of this study provided a kind of an indirect support to findings that improving hygiene factors to explore the factors influencing employee perception of equity in compensation. Therefore; managers should not rely on communication of these factors equity to improve job perception of equity. However, they might be related to other important work outcomes such as dissatisfaction, stress and organizational commitment.

Internal equity is especially important in an organization where “teamwork” is critical to success. In environments that requires a cross-section of skills and talents and interdisciplinary teamwork, coworkers need confidence in themselves and their colleagues. An important part of creating an environment in which teamwork is effective,

is a compensation policy that reflects the true value of work to the overall organization, and helps all members of the team respect one another's contribution and role. The study tally with Kotler (2000), where perceptions as the process by which individuals select, organize and interpret information inputs to create a meaningful picture of the world. He further states that a motivated person is ready to act. How the motivated person acts is influenced by his/her perceptions of the situation. Employees develop set of filters through which they make sense of the conditions they are exposed into. Cole (1997) defines employees as individual who, over a given time, invest a large proposition of their lives in their organizations

Not only must compensation be equitable, it must also be "perceived" as such by employees. Research clearly demonstrates that employee's perceptions of compensation equity, or inequity, can have dramatic effects on their motivation for both work behavior and productivity. Managers must therefore develop compensation practices that are both internally and externally equitable. Employees believe that compensation rates for jobs within the organization approximate the job's worth to the organization. Also, the employer's compensation rates must correspond closely to prevailing market rates for the employee's occupation. The importance of compensation variability in influencing compensation importance has been demonstrated empirically under carefully controlled conditions. Rynes et al (1983) showed that compensation explained an average of 65% of the variance in subjects' overall evaluations of job attractiveness when presented with jobs having a wide range of salary alternatives, as compared to only 40% when presented with a compensation range half as great (Cole,2002).

5.4 Recommendations

The fact that all the measures come from the same source, which can contribute to common-method variance of the answers of respondents about their perceptions of equity. It would not have been possible to convince the respondents that their responses would be treated with 100% confidentiality. As stated by Adams, (1963) on Equity theory emphasized the importance of compensation comparisons to individuals' sense of fairness and well-being. Status and accomplishment-based signals associated with compensation appear to be particularly sensitive to relative pay, or pay comparisons, rather than absolute levels of pay.

Further, survey results might be biased since the majority of the respondents belonging to low-end career group. One other limitation to the study is that bank is unique in terms of socio-economic conditions (population groups, religion, competitiveness, etc.), thus survey findings cannot be generalized. The bank managers should conduct compensation surveys within the medium banks to ensure that the compensation rates within the industry are at par. This would enhance retention of competent staff and increase job satisfaction.

5.5 Suggestion for further Studies

A recommendation for further research is that researchers should study the relationship between perception of equity and job satisfaction under the other financial institutions.

Another recommendation is to investigate the relative importance of each facet of perception of equity in predicting each facet of job satisfaction especially those that were reported as significant predictors of job satisfaction in this study.

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APPENDIX I: LETTER OF INTRODUCTION

University of Nairobi,

School Business,

P.O Box 30197,

Nairobi.

12th September, 2011.

Dear Respondent,

RE: COLLECTION OF SURVEY DATA

I am a postgraduate student at the University of Nairobi, at the school of Business. In order to fulfill the degree requirement, I am undertaking a management research project on factors that influence employee perception of equity in compensation among medium sized commercial banks in Nairobi County.

You have been selected to form part of this study. This is to kindly request you to assist me collect the data by filling out the accompanying questionnaire. The information / data you provide will be exclusively for academic purposes. My supervisor and I assure you that the information you will give will be treated with strict confidence. At no time will you or your organization's name appear in my report.

Eric Mutinda

Student no. D61/75229/2009

Mr. George Omondi

Supervisor

APPENDIX 11: QUESTIONNAIRE
PART A: DEMOGRAPHIC DATA

1. Is your Bank locally owned [] foreign owned [] both local and foreign owned [] any other (specify) _____

2. What is your designation at the bank _____

3. Gender (Tick one) Male [] Female []

4. What is your age group?

- a) Below 30 years []
- b) 30 – 34 years []
- c) 35 – 39 years []
- d) 40 – 44 years []
- e) 45 years and above []

5. In which Level of management do you work in your department of the bank?

- a. Senior Management []
- b. Middle Level Management []
- c. Support staff []

5. Length of continuous service the current bank

- 5 yrs and below
- 6- 10 years
- 11-15 years
- 16- 20 years
- 21 years and over

How long have you been working in your present capacity?

Less than 3 years () 3 to 5 years () 5 to 7 years () Over 7 years ()

1. How long have you worked for the banking industry?

1 – 2 years () 6 – 10 years () Over 15 year ()

3 – 5 years () 10 – 15 years ()

8. Highest level of education

KCSE []

Diploma []

Undergraduate []

Masters []

Doctoral []

Any other (specify)

PART B: EMPLOYEE PERCEPTION OF EQUITY IN COMPENSATION

9. To what extent do you agree with each of the following statements? Rank by placing a tick in the appropriate column.

1. Strongly disagree
2. Disagree
3. Neither agree nor disagree
4. Agree
5. Strongly agree

	1	2	3	4	5
a) The bank treats all employees fairly in terms recognition for good performance					
b) The bank compensates each employee in same peer group fairly					

c)The bank uses fair job evaluation methods to determine the worth of each job					
d)The bank compensation scheme is fair comparable to other banks in the same peer group					
e) The bank uses fair performance evaluation methods					
f)The bank uses fair promotion and advancement procedures					
g)The bank provides benefits to all employees fairly in same peer group internally					
h)The bank provides benefits that are fair comparable to other banks in the same peer group					
I)The bank provides incentives fairly to all employees in the same peer group internally					
j)The bank provides incentives that are fair comparable to other banks in the same peer group					

10. Does your perception of fairness in compensation affect the relationship with your colleagues at the organization?

Yes ()

No ()

11. To what extent does your perception of fairness in compensation influence your motivation to work?

Yes ()

No ()

PART C: FACTORS THAT INFLUENCE EMPLOYEE PERCEPTION OF EQUITY IN COMPENSATION

12. Indicate the extent to which the following factors influences employee perception of equity in compensation at your Organization

You will be guided by the following scale

2. Strongly disagree

3. Disagree

- 4. Neither agree or disagree
- 5. Agree
- 6. strongly agree

	1	2	3	4	5
a)The bank compensation schemes is to the desired levels of employees inside and outside the organization					
b)The bank ensures that the employees are satisfied with their compensation					
c)The compensation perceived by employees is what is actually received					
d) The bank pays close attention on the importance of compensation inside and outside the organization.					
e)The compensation I receive enables me to cater for my basic needs comfortably					
f)The compensation I receive has changed my social status					
g)The compensation I receive has enabled me to advance my education aspirations					
h)The compensation I receive enables me to enhance my leadership					

Others.....

13. I often feel that there is fairness on within the bank in terms of compensation.

Yes () No ()

14. I feel that there is fairness with my chances for compensation increases.

Yes () No ()

APPENDIX III: LIST OF MEDIUM COMMERCIAL BANKS IN KENYA

1. African Banking Corporation Limited
2. Consolidated Bank of Kenya
3. Development Bank of Kenya
4. Equatorial Commercial Bank Ltd
5. Fidelity Commercial bank Limited
6. First Community Bank Ltd
7. Giro Commercial Bank
8. Gulf African Bank
9. Guardian Bank
10. Habib Bank Ltd
11. K-Rep bank
12. Trans-National Bank
13. Victoria commercial Bank

Source: CBK Directory 2009 page 6