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**An Analysis of the Relationship Between Compensation, Performance and Motivation in the Financial Sector**

**Kaltrina Bunjaku Pasuli**

Department of Economics, Faculty of Business and Economics, South East European University

**Abstract:** The aim of this research is to analyze the relationship between compensation, performance and motivation of employees in the financial sector in Kosovo. The research analysis was conducted by combining quantitative and qualitative methods. For the purposes of this study, two data collection techniques were used. One includes the literature review, while the other includes the interviews. Questionnaires compiled in the form of closed and open questions were used as an instrument for data collection.

The results show that the increase in compensation does not have a significant impact on the increase in the performance of employees in the financial sector in Kosovo in the long term. An increase in the level of compensation can increase the motivation of employees. Employee motivation is related to performance evaluation, compensation, non-monetary rewards, provision of training for individual development, gratitude, feedback, etc. Correct reporting and management approach on performance evaluation affects the motivation of employees in the financial sector. The feeling of equality and justice in the compensation level is one of the basic conditions for the motivation process. There is no real reward system (economic or psychosocial) that is applied in financial institutions in Kosovo.

This paper is original in nature and the motivation to study this topic is the success, sustainability and stability of the financial sector in Kosovo. The findings of this study will contribute to the management of the financial sector, through the implementation of the recommendations based on the conclusions reached, in increasing the productivity and performance of the employees of the financial sector in Kosovo.

**Keywords:** Compensation, Performance, Motivation, Financial institutions

# **Introduction**

The financial system in Kosovo consists of the Central Bank of Kosovo (CBK) and financial institutions, such as: commercial banks, microfinance institutions, insurance companies, pension funds, credit associations and non-banking financial institutions, licensed and supervised by the Central Bank of Kosovo (CBK, 2022).

Kosovo as an upper-middle-income country (World Bank, 2022) is characterized by a financial system that has a high level of sustainability in all its constituent sectors. The financial system faced the biggest challenge in the history of its operation, caused by the pandemic crisis, but it managed to successfully cope with it. As a result of the improvement of the situation with the pandemic, the easing of restrictive measures of movement as well as government support packages, the financial system in Kosovo marked a rapid recovery in 2021 (CBK, 2022). The start of the war in Ukraine in February 2022 has influenced the creation of high uncertainty for macroeconomic prospects. The war in Ukraine exacerbated inflationary pressures, leading to further increases in energy, oil and food prices and increased overall risks to financial stability (CBK, 2022).

Although the growth of globalization is causing an increase in the uncertainty and complexity of doing business in the world, companies are faced with the obligation to continue their activities. This obligation has caused the necessity that in order to work efficiently, to gain competitive advantage and to make better use of human resources, companies in the center of attention must be worker-oriented (Arnolds & Bashoff, 2002). Today, companies are facing great difficulties in finding solutions for the very specific requirements of their customers due to hierarchy and rigid organizational structure. Companies' goal of gaining competitive advantage is closely related to their ability to engage in a performance measurement management process. Measurement is the key to success and what you cannot measure, you cannot control it. If you cannot control it, you cannot even manage it. And if you don't manage it, you cannot even improve it (Harrington, 1999). Although these statements made by James Harrington are more than 20 years old, they have not lost their meaning. If we take a look at most financial institutions in Kosovo, the performance measurement of employees leaves much to be desired.

The main aim of this research is to analyze the relationship between compensation, performance and motivation of employees in the financial sector in Kosovo.

The research hypotheses of this research paper are as follows:

H1: *An increase in compensation does not have a significant impact on the increase of the performance of employees in the financial sector in Kosovo*.

H2: *An increase in compensation can increase the motivation of employees*.

H3: *The motivation of employees is directly conditioned by the evaluation of their performance*.

The results of this research can have an impact on the management, through the implementation of the recommendations based on the conclusions reached, in increasing the productivity and performance of the employees of the financial sector in Kosovo. The data used in this study came from questionnaires collected by 150 employees of the financial sector in Kosovo, in the form of closed and open questions.

The results show that compensation is not the main factor that affects performance, there are other factors such as working conditions, environment, collegial relationships, institutional climate, etc. Compensation encourages the employee to reach higher levels at work and is one of the main motivators among employees. Employee motivation is related to the evaluation of their performance, but it is not directly conditioned only by the evaluation of their performance, but also by compensation, non-monetary rewards, the provision of training for individual development, recognition, feedback, etc.

The paper is organized as follows: the second section presents the literature review, followed by the research methodology and data. The fourth section presents the results, while the fifth section presents the conclusions of the paper.

# **Literature review**

## Compensation

Employees compensation is one of the biggest costs of doing business (Williams et al. 2006). Compensation is a basic incentive that encourages people to work and includes direct or indirect payments to workers, such as wages, bonuses, shares and benefits (Barry & Milovich, 1991). The nature of people is based on the immutable principle that for a given input a particular output is required in return. Therefore, a contribution made for a specific job requires an appropriate compensation. If altruistic behavior is disregarded, each person will ultimately seek compensation for performing tasks or fulfilling contracts (Shieh, 2008). The modern definition of compensation highlights two components: internal (psychological) and external (tangible). The second component includes monetary and non-monetary rewards. Internal factors however refer to employees' mental satisfaction, such as job satisfaction (Bhattacharyya, 2009). Determining the compensation for human work is not so simple, since the work is of various kinds and associated with numerous psychological and physical conditions (Hill, Stevens 2001).

Compensation objectives include the following categories:

*Equality* - this category refers to inequalities. The objectives of this category refer to internal and external equality. Internal equality strives for similar pay for similar jobs. Whereas external equality means a worker's pay in the labor market is related to the comparable worker's pay in another firm. Different abilities or contributions represent compensation differences that are related to the concept of equity (Belcher, 1969).

*Efficiency* - is closely related to equality. Therefore, efficient compensation is seen as equal if the reward is seen as fair, and unequal if the reward is perceived as unfair. The main purpose of efficiency is to combine a part of the wages in productivity or profit, group or individual performance, etc. (Gurbuz, 2007).

*Macroeconomic stability* - is a factor that may have been driven by the high level of employment and low inflation. However, if the government sets a very high minimum wage, this will not have a favorable impact on the level of employment. Therefore, compensation and compensation policies are two of many factors that affect macroeconomic stability (Agirbas et al., 2005).

*Efficient labor allocation* - it has to do with the rate that workers will be able to move to obtain net profit. These moves can be geographical or work-related (within the enterprise). Such examples can be: movements from low-wage areas to high-wage areas through the acquisition of new skills (Bozkurt & Bozkurt, 2008).

*Other objectives* - there are many other objectives that also affect compensation. It is therefore important to: recruit qualified workers, retain current workers, reward desired behavior, control costs, comply with legal provisions, facilitate the understanding of compensation systems, and ultimately more administrative efficiency (Bhattacharyya, 2009).

## 2.2 Performance evaluation

Performance evaluation serves to measure the results of an activity through previously defined criteria, such as evaluating workers by judging the level of success of workers based on quantitative and qualitative results, promoting workers, determining training needs and training them, determining the rate of success, reward, salary increase, job change, giving new tasks, until it is time to retire (Canman, 1993). The performance appraisal system has been partially implemented in previous periods, but since 1980 it has started to be implemented by many countries (OECD, 2005). According to Mc Gee Wanguri, professor at the University of Houston, performance evaluation systems are considered "a necessary evil in institutional and corporate life" (Wanguri, 1995). Employee performance measurement is part of the performance evaluation system. Performance evaluation is a continuous process and can be done in a formal or informal procedure (Feldman, 1981). Informal evaluation can have several advantages for the evaluator, it is done daily, does not require any complicated structure and does not require papers in the hands. But, an informal assessment has more disadvantages. Each supervisor evaluates as he wants and when he wants, the objectives and methods of evaluation are unclear and can vary from one service to another, workers do not know much about what they are evaluated for, they do not always know what is expected of them and what is thought of their performance. Therefore, in practice, formal evaluation is mostly used (Shuli, 2011). After creating performance evaluation goals, employees need to know what is expected of them to be successful in their jobs. If employees meet the criteria defined in the goals, then it is easier for them to understand what is expected from them. At the end of the performance evaluation period, the supervisor and the worker jointly review the worker's performance (performance meeting) and compare actual performance to benchmark performance. Based on this comparison, it is revealed to what extent these standards have been fulfilled, the reasons for the lack of realization of the expected performance standards are revealed and finally a plan is created on how to improve these problems (Joshi, 2013). Studies show that managers encounter difficulties when evaluating the performance of subordinates. Employee performance evaluation meetings pose many dilemmas for managers. On the one hand, managers should provide constructive criticism so that employees can increase their work performance. On the other hand, they don't want to give negative feedback because of the bad feelings that come as a result. It is not surprising that there are cases when managers avoid the relevant evaluation for workers by giving only a general summary (Posthuma & Campion, 2008).

## 2.3 Motivation

The role of motivation and the impact on productivity and effectiveness has been discussed for years in various management and organization literatures, since the success of the enterprise depends on the skills and willingness of the workers employed in an enterprise. An employee who is not motivated cannot be expected to show positive performance. The main objective of using motivation in business is to ensure high performance of employees to realize the company's goals (Agirbas et al., 2005). Motivation is a stimulus in the workplace that enables employees to perform to the best of their abilities in pursuit of the organization's goal (Poon, 2004). The impulse that drives the individual to move and have a certain behavior can sometimes be for internal, sometimes external reasons. In intrinsic motivation there is a natural force that drives the individual to perform a certain activity and stops after achieving satisfaction. This strength comes from within the person and the individual motivates himself. An intrinsically motivated individual makes an effort only because he wants to and rewards himself (Newstrom & Davis 1993). Theories of motivation are mainly divided into three groups, self-explanatory models, content models and process models. Contemporary models can also be included in this division. Self-explanatory models try to explain how management can motivate workers. The scientific management model and the human relations model belong to this group. Content models investigate what are the factors that motivate people. The most popular theories that belong here are Maslow's hierarchy of needs, Herzberg's two-factor theory and Alderfer’s existence relatedness and growth theory. Process models deal with the issue of how behaviors arise and manifest. These models are expectation, equity and reinforcement models. Contemporary models are models that give space to individual purpose, evaluation, perception and comments (Agirbas et al., 2005). There is a direct relationship between the performance of a job and the reward, and the employee receives this reward by performing this job (Kuvaas, 2006). Whereas in cases where the individual is controlled from outside, the factors that lead the individual to act are external factors. In external motivation, to motivate the individual, there must be rewards set by the organization, the environment or the supervisor. Extrinsic rewards are rewards that are not directly related to the nature of the work and satisfaction occurs after the action is completed, not while the work is being done. Examples of extrinsic rewards include retirement plans, health insurance and vacations (Benton & Halloran, 1991). In addition to planning, organizing and controlling, motivation is also part of the manager's duties. Managers who try to motivate workers using the needs of higher levels, after building the motivation system that works in a stable way will form a basis for higher performance in the work environment and organizational climate. Workers through increased performance and productivity will satisfy both personal needs and better serve the company's goals (Dalton, 1971).

To summarize, many papers and published reports related to compensation, performance and motivation have been reviewed, and this paper will attempt to contribute to the issues by analyzing the relationship between these variables in financial sector in Kosovo.

# **Research methodology and data**

The research analysis was conducted by combining quantitative and qualitative methods. For the purposes of this study, two data collection techniques were used. One includes the literature review, which presents the review, analysis and commentary of sources of information on the compensation, performance and motivation of employees in the financial sector in the region and the world. While the other includes the interviews, which present the different views regarding the relationship between compensation, performance and motivation in the financial sector in Kosovo. Questionnaires compiled in the form of closed and open questions were used as an instrument for data collection. For conducting the interviews, 150 employees of the financial sector in Kosovo were selected, of which 48% were women (n=72) and 52% were men (n=78). The questionnaire was completely anonymous, participants were not asked for their name, or the name of the institution they work for. The research has been extended in seven cities of Kosovo, respectively in the financial institutions of Kosovo and the finance departments of public and other institutions.

# **Results**

The age of financial sector employees in Kosovo is quite young, 59% of employees are aged 19-35. Taking into account the importance of commercial banks in the financial sector in Kosovo, they had the largest participation in the research with 31%, followed by microfinance institutions, insurance companies, public institutions, other and CBK. The majority of employees are economists 52%, followed by lawyers 19%, engineers 15%, other 13% and architects 2%. Employees of the financial sector have an average work experience of 3-10 years with a total of 60% of the responses from the respondents. The most powerful weapon in the hands of business to motivate employees is money. Money is also an effective tool to attract skilled employees to the enterprise and to work harder. Compensation, in addition to satisfying the physiological and safety needs of employees, can also be a symbol of reputation. Employees of the financial sector in Kosovo think that they have a low level of compensation. The results show that 39% of employees think they have a moderate level of compensation, 46% of employees think they have a low level of compensation. And according to the weighted average, the level of compensation is 2.62 degrees, therefore it can be understood that the employees see the level of compensation a little lower than the average level (3). The level of compensation with a weighted arithmetic average of 4.13 is one of the main elements in the performance of employees of the financial sector. As can be seen in figure 1, 78% of the employees have circled answers 4 and 5 as options, while those who have declared that the level of compensation has no importance or very little importance are only 4%. The sense of equality and justice is one of the basic conditions for the motivation process. The lack of these feelings prevents employees from being motivated to show higher performance.

Figure 1: The importance of the level of compensation in the performance of employees

Source: Author’s calculation

According to the results of the survey, employees of the financial sector in Kosovo attach great importance to the fair determination of compensation. In Figure 2, it can be seen that 89% of respondents estimate that the correct determination of compensation is very important, while only 3% declare that it is not very important. With an average of 4.40, the fair determination of compensation is ranked as the second most important factor evaluated by employees of the financial sector.

Figure 2: The importance of the correct determination of compensation in the motivation of employees

Source: Author’s calculation

While the most important factor evaluated by the employees of the financial sector in Kosovo is the impact of the compensation level on employee motivation with a weighted average of 4.41. In figure 3 it can be seen that 89% of employees see the level of compensation as a very important factor in their motivation. These percentages show us that although not every time and under all conditions, compensation is one of the primary motivating factors that should not be overlooked.

Figure 3: The importance of compensation level in employee motivation

Source: Author’s calculation

According to the employees, the reward system for the successes achieved in the financial sector in Kosovo is very low. With an average of 2.12, it is one of the factors rated with the weakest average. 68% of employees believe that rewards for achievements are too low. From these results it can be understood that there is no real reward system that is applied in financial institutions in Kosovo. The employee who shows any kind of success is rarely rewarded with any economic or psychosocial reward. From the collected answers, it can be seen that the employees of the financial sector attach great importance to the reward system for the successes achieved in their performance level. 80% of employees attach great importance to the reward system, 14% show a moderate importance, while only 6% do not attach much importance to it. These values show us that in order to achieve high productivity, the reward system is an important motivator. 51% of financial sector employees estimate that they have excellent relations with colleagues and supervisors, 31% estimate that they have good relations and 14% moderately good relations. While another 4% estimate that they do not have good reports. From the results it can be understood that in general the reports in the financial institutions in Kosovo are good and work is done in a very social environment. From the results it can be seen that the relationships with colleagues and the supervisor have a very big impact on the employees with 55%, great impact with 31%, average impact with 9%. And the percentage of those who have no influence on motivation is only 4%. With an average of 4.31, it can be seen that relationships with colleagues and the supervisor are among the most important factors in the motivation of financial sector employees. Meanwhile, regarding the current work schedule, the results show that the schedule is very suitable with 80%, the schedule it fits in a moderate way with 16%, while for 4% of employees, the current work schedule does not suit them. From this it can be understood that in general the employees of the financial sector are satisfied with the current working hours. The results show that compensation for overtime work is not implemented at all by 45%, 26% implement it a little, 16% moderately, while 13% think it is implemented very well. With an average of 1.99, it occupies the last position in the table and it can be understood that the implementation of compensation for overtime work is very low and far from the average. While the implementation of compensation for overtime work in the motivation and performance of employees is quite important with 79%, moderately with 11% and not important 10%. 63% of the employees who participated in the survey stated that the performance evaluation in the institution where they work is implemented every year, 34% is implemented every 6 months, while 3% every month. From the data analysis, it can be seen that the employees of the same department in some institutions declare different frequency of implementation of performance evaluation. From this it can be understood that the performance evaluation system is not being implemented as it should be, it is not being done directly with the employees and still needs improvement.

Regarding the question "What is your opinion why compensation is directly related to the performance of employees in the financial sector in Kosovo?" different answers have been gathered, such as compensation is not directly related to employee performance, it may be one of the criteria that affects performance, but not every time it is directly related. Compensation is a type of motivation why one chooses to work in a certain position, it fulfills the financial needs of the employee, it can influence the increase of employee satisfaction and that employees have a greater commitment to the workplace. Due to the low economic situation in the country, for most employees’ salary income is the main source of income, therefore compensation affects family well-being and any movement in the level of compensation directly affects the well-being of the employee and the family. The employees think that it would be good if each financial institution would have in written form the levels of promotion in addition to the position and qualification, as well as the advancements in the position and make them public for all employees. Very often there are high compensation differences from the supervisor to the subordinate, which causes dissatisfaction among the employees. It is important to take into account the way compensation is done in institutions, because an employee sees through compensation how much he is appreciated for the work he has done. Applying pay for performance can bring benefits to both managers and employees. The increase in the individual performance of the employees can also cause the increase in the performance of the institution in general, which is beneficial for both the employee and the institution. Compensation is an appropriate tool to increase the employee's passion for his work. Rewards are an important mechanism by which the behavior of employees can be calculated with the interests of the institution. Therefore, compensation is not the main factor that affects performance, there are other factors such as working conditions, environment, collegial relationships, institutional climate, etc. From the collected answers, it can be seen that the first hypothesis has been proven: *An increase in compensation does not have a significant impact on the increase of the performance of employees in the financial sector in Kosovo*.

Regarding the question "What is your opinion why compensation is interactive with the motivation of employees in the financial sector?" there were different opinions that compensation is not the only factor, but it influences to motivate employees and makes them more loyal to their workplace. Most employees feel motivated to help the respective institution on its way to success if the employer compensates employees fairly for the work performed. If the employee finds out, or feels that he is being treated unfairly at the level of compensation, then the collegial atmosphere with colleagues or management will stand out and motivation for work will fall. It is important that if the employee feels valued and rewarded, in this way he will be more motivated to work. Fair compensation increases motivation for work, increases the will to perform work with dedication, dignity, professionalism, correctness and up-to-dateness. In most companies in Kosovo, compensation is seen as the only tool for motivating employees, while other methods of motivation are in most cases completely neglected. Compensation encourages the employee to reach higher levels at work and is one of the main motivators among employees. Compensation in the form of salary, or other rewards influence the employee to show a higher performance to meet the company's goals. Bonuses also influence the motivation of employees. Bonuses show the evaluation of positive results of special events that the employee has shown during the period in the fulfillment of work tasks. The burden, pressure and stress in the financial sector can only be repaid with compensation, while the satisfaction and rewards for the successes achieved motivate employees to work even harder. From the collected answers, it can be said that the second hypothesis has been proven: *An increase in compensation can increase the motivation of employees*.

In order to keep qualitative employees, to motivate them to work effectively and efficiently, institutions should also apply other methods of motivation, such as various benefits, health insurance, specialization in the field of work, etc. Benefits may be applied to employees based on demonstrated performance. Therefore, it is very important to evaluate the performance of employees fairly by the management. From the collected answers, it can be said that the third hypothesis has not been proven: *The motivation of employees is directly conditioned by the evaluation of their performance*. Employee motivation is related to the evaluation of their performance, but it is not directly conditioned only by the evaluation of their performance, but also by compensation, non-monetary rewards, providing training for individual development, recognition, feedback, etc.

# **Conclusions**

From the results of this research we saw that the increase in compensation does not have a significant impact on the increase in the performance of employees in the financial sector in Kosovo in the long term. An increase in the level of compensation can increase the motivation of employees. Employee motivation is related to performance evaluation, compensation, non-monetary rewards, providing training for individual development, gratitude, feedback, etc. Financial compensation has a greater impact on employee motivation than setting standards for performance evaluation. Correct reporting and management approach on performance evaluation affects the motivation of employees in the financial sector. The feeling of equality and justice in the compensation level is one of the basic conditions for the motivation process. There is no real reward system (economic or psychosocial) that is applied in financial institutions in Kosovo. The collegial relationships in the financial institutions in Kosovo are good and work is done in a very social environment. Relationships with colleagues and the supervisor are among the most important factors in the motivation of employees of the financial sector. Employees of the financial sector are satisfied with the current working schedule. The implementation of compensation for overtime work is very low and far from the average. Performance evaluation is not being implemented on a regular basis.

The reward system is an important motivator, therefore to achieve higher productivity it is recommended to improve the reward system. The pressure and stress to achieve results is forcing employees of the financial sector to work overtime, while compensation for overtime work is rated at a lower average by employees. Therefore, to increase the motivation of employees and consequently the performance of employees and the institution in general, it is recommended to implement compensation for overtime work. Employee performance evaluation should be improved through the implementation of performance evaluation on a regular time basis. it is recommended to measure and communicate the performance result at least twice in a year, in order to warn for good performance or train those who do not show sufficient performance. The performance measurement process in institutions should be closely monitored.

The establishment of performance evaluation criteria should be done in cooperation between the manager and the subordinate, and the same performance evaluation template should not be used for all positions and departments of the institution.

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