



Compensation and employee performance: mediation of work motivation

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ABSTRACT

This study aims to analyze the relationship between compensation provided by the company and employee performance by considering the mediating role of work motivation. The method used in this study is a quantitative approach using a questionnaire distributed to employees with a total sample of 97 people. In data processing, this study uses SmartPLS 4 to test measurement models and structural models. The results of the analysis showed that there was a significant positive relationship between compensation and employee performance. In addition, the study also found that work motivation plays a role as a mediator that strengthens the relationship between compensation and performance. These findings provide important implications for human resource management, where improving a fair and adequate compensation system can improve work motivation and, ultimately, overall employee performance. Therefore, an effective compensation management strategy should be a priority for companies looking to improve their employees' performance.

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INTRODUCTION

In recent years, many companies have begun making payments based on employees performance measures (Alkandi et al., 2023; Bartol, 2023; Obloj & Zenger, 2022; Su et al., 2023). Today, organizations are in an intensely competitive environment. An organization's competitive advantage depends on the development of human resources, and all employees, including managers, must achieve success above a certain standard. Businesses must identify and improve the performance of their human resources to achieve organizational goals and gain a competitive advantage. Of course, this requires optimal performance from all employees in the organization. Without optimal employee performance, it will be difficult for organizations to achieve the desired success (Diamantidis & Chatzoglou, 2019). In simple terms, performance describes how well an employee is doing in their job. Performance is the level of fulfillment of planned work and employee behavior. Performance is not only an individual, but also a quantitative and qualitative expression of how much a group or organization can achieve a targeted and planned work point

within a given period. To what extent the tasks that make up the work are successfully fulfilled is determined.

Performance is the quantitative or qualitative result of actions and efforts taken by individuals or groups in performing a job over a period of time (Bakker et al., 2023; Krijgshero et al., 2022). If the results obtained are positive, high performance has been achieved if the assigned tasks are met. Otherwise, the performance is considered low. Superior performance is synonymous with success. However, superior performance or success depends on many personal, organizational, and environmental factors. For example, the company's ability to compensate its employees and the organization's ability to motivate employees so that employees can improve their performance optimally.

Compensation refers to the aspect of human resources that handles all forms of rewards that individuals earn in exchange for completing tasks for an organization (Lazear, 2018; Wilton, 2022). The goal is to cultivate employees who feel interested in their work, feel fulfilled, and inspired to do well for the organization. This is a mutual relationship between employees and employers. This reward system is designed to increase employee satisfaction and loyalty, as it includes monetary and non-monetary incentives that attract, inspire, and fulfill essential talent, keeping top performers engaged as the compensation structure recognizes behaviors that contribute to the organization's competitive advantage.

Compensation, which includes both financial and nonfinancial rewards, plays a crucial role in shaping the motivation and ultimately the performance of employees within the organization. Compensation serves as tangible recognition of an employee's contributions, skills, and efforts, which fosters a sense of value and appreciation that directly influences their commitment to work. Compensation is defined as all forms of financial returns, services, and benefits received by workers as part of an employment relationship (Martocchio, 2011; Min et al., 2019). The design and implementation of performance measurement and compensation systems significantly affect employee motivation. One of the main reasons a person works is to make ends meet, and they will work optimally to get the appropriate compensation (Dhingra & Dhingra, 2020). A well-structured compensation system acts as a powerful motivator, incentivizing employees to strive for excellence and achieve organizational goals. Fair and equitable compensation practices foster a positive work environment, fostering trust and transparency between employees and management (Brown et al., 2022; Cullen, 2024; Murtiningsih, 2020). When employees consider their compensation fair compared to their peers and the market, they are more likely to feel satisfied with their work and committed to their organization. Therefore, compensation is one of the factors that most affect the quality and effectiveness of human resources (Zafar et al., 2021). In addition, compensation can also have a strong influence on increasing an employee's work motivation.

Employee motivation is one of the most important factors that affect job performance. Therefore, employers need to develop various strategies to increase employee motivation. Employee motivation is a factor that directly affects job performance. High motivation allows employees to work harder, achieve better results, and make fewer mistakes. At the same time, increased motivation can create a more positive atmosphere in the workplace and increase employee commitment to their work.

A significant gap lies in the limited mediating research that explicitly examines work motivation as a link between compensation and employee performance, especially in a dynamic industrial sector. A study conducted Kuvaas et al. (2017) revealed that financial-based (extrinsic) compensation risks lowering intrinsic motivation if not combined with other motivational strategies. Therefore, more in-depth studies are still needed that not only assess the direct relationship between compensation and performance, but also the application of the work motivation behind them.

RESEARCH METHOD

This research is a quantitative research with a causal approach. The causality approach is used to test and analyze the relationship between the variables studied, in this case, the variables studied are employee performance variables adapted from the research of Ozcelik & Barsade (2018) which consists of four statements, the compensation variable refers to Mogrovejo et al. (2025) which consists of three statements, and work motivation is adapted from Medina et al. (2024) which consists of ten statements. The population in this study is employees of PT Lung Cheong Brothers Industrial, with a sample of 97 employees using simple random sampling. As for the data collection of this study, data was collected through a questionnaire that was shared directly with respondents using a Likert scale of 5 points (1 = Strongly Disagree - 5 = Strongly Agree) (Russo et al., 2021). The data collected from respondents was carefully examined and edited. Each item on the questionnaire is tabulated based on the responses given, in the data processing this study is assisted by using a data analysis program known as SmartPLS version 4.0 (Ringle et al., 2024). The use of SmartPLS is because the program is able to analyze complex data, more than that, this data processing software has been widely used by researchers around the world, especially those focusing on management science (Hair et al., 2022). In addition, the advantages of SmartPLS are that it does not require normally distributed data and can be used on small samples (Hair et al., 2022). The test is divided into two stages, first, measurement model testing, and second, structural model testing (Hair et al., 2022).

RESULTS AND DISCUSSIONS

One approach to testing validity is through discriminant validity, which aims to ensure that the construct being measured is completely different from the other constructs. In this case, testing using cross loading is a significant method to evaluate the validity of the discriminant. Cross loading refers to a situation in which a measurement item has a significant load on more than one construct (Hair et al., 2022). In discriminant validity testing, each item should have a higher charge on the construct to be measured compared to the other construct (Rönkkö & Cho, 2022).

Table 1. Cross Loading

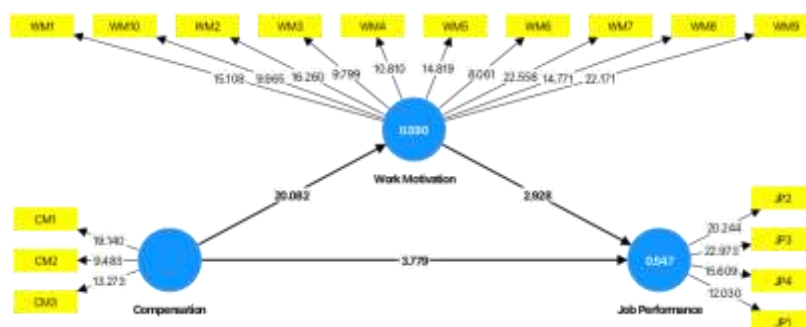
	Compensation	Job Performance	Work Motivation
CM1	0,813	0,526	0,590
CM2	0,682	0,499	0,438
CM3	0,744	0,543	0,669
JP1	0,523	0,737	0,558
JP2	0,576	0,812	0,547
JP3	0,577	0,841	0,533
JP4	0,516	0,745	0,530
WM1	0,676	0,517	0,745
WM2	0,633	0,453	0,734
WM3	0,581	0,470	0,590
WM4	0,583	0,609	0,669
WM5	0,553	0,548	0,769
WM6	0,447	0,355	0,646
WM7	0,583	0,496	0,800
WM8	0,505	0,523	0,769
WM9	0,498	0,546	0,794
WM10	0,396	0,399	0,679

Table 1 shows that all indicators tested have shown that the item has a higher load on the construct to be measured compared to other constructs. This means that all indicators in this study can be declared to have met the requirements for discriminant validity adequately.

Table 2. Reliability and R-square

Variable	Cronbach's alpha	Composite reliability	AVE	R-square
Compensation	0,607	0,792	0,560	
Job Performance	0,791	0,865	0,616	0,547
Work Motivation	0,897	0,916	0,522	0,590

Table 2 shows the results of reliability tests using Cronbach's Alpha (CA) and Composite Reliability (CR). Cronbach's Alpha value above 0.6 is considered the minimum limit that indicates acceptable reliability (Raharjanti et al., 2022). Meanwhile, a good Composite Reliability value is more than 0.7 (Hair et al., 2022). Based on Table 2, the CA value ranges from 0.607-0.897, while the CR value ranges from 0.792-0.916, meaning that all variables can be declared reliable. The ideal AVE value should be greater than 0.5 (Hair et al., 2022), and in testing the AVE value ranges from 0.560-0.616. R-square indicates the proportion of variance of the dependent variable that can be explained by the independent variable. The R-square value for the job performance variable is 0.547 and the work motivation variable is 0.590.

**Figure 1.** Research Model**Table 3.** Hypothesis

Hypothesis	Original sample	STDEV	T statistics	P values
Compensation -> Job Performance	0,412	0,109	3,779	0,000
Compensation -> Work Motivation	0,768	0,038	20,082	0,000
Work Motivation -> Job Performance	0,375	0,128	2,928	0,003
Compensation -> Work Motivation -> Job Performance	0,288	0,103	2,800	0,005

Table 3 provides an explanation of hypothesis testing using the bootstrapping technique. A hypothesis is declared acceptable if the statistical T values are greater than 1.96 and the P values are less than 0.05 (Hair et al., 2022). Compensation and Job Performance had a positive and significant effect ($\beta=0.412$; $T=3,779$; $P=0.000$); Compensation and Work Motivation had a positive and significant effect ($\beta=0.768$; $T=20,082$; $P=0.000$); Work Motivation and Job Performance had a positive and significant effect ($\beta=0.375$; $T=2,928$; $P=0.003$); Work Motivation can mediate positively and significantly on Compensation to Job Performance ($\beta=0.288$; $T=2,800$; $P=0.005$).

Compensation, encompassing financial and non-financial rewards, is pivotal in shaping employee behavior and, consequently, organizational performance. It is a tangible acknowledgment of an employee's contributions, sacrifices, and dedication to the organization (Dina et al., 2017). A well-structured compensation system attracts and retains talent and motivates employees to perform at their peak potential (Baffoe & Bediako, 2021; Dina et al., 2017). The design and implementation of performance measurement and compensation systems profoundly influence employee motivation, as economic and psychological theories (Van Herpen et al., 2005) suggest. Compensation serves as a crucial tool that signals an employee's value to the company and ensures a decent standard of living (Abbas & Astuty, 2023; Achmad et al., 2020). The importance of compensation extends beyond mere financial remuneration, as it fosters a sense of

recognition, appreciation, and value among employees. Employees who feel adequately compensated are more likely to be engaged, committed, and productive (Baffoe & Bediako, 2021; Kholilah & Sari, 2021). Designing effective compensation programs necessitates a comprehensive understanding of various factors such as organizational strategy, industry benchmarks, and employee demographics (Hong, 2017).

A critical aspect of compensation management involves aligning compensation strategies with organizational culture (Madhani, 2014). A supportive organizational culture should reward team success and align the compensation strategy accordingly. The degree to which employees feel fairly treated directly impacts their motivation and commitment (Zhou & Shaw, 2019). Compensation must be perceived as fair and equitable to foster a conducive and productive work environment (Putra & Masdupi, 2019). Organizations should ensure employees feel valued and well-compensated to maximize productivity and encourage positive behaviors (Madhani, 2014). Although compensation does not always provide satisfactory results in improving employee performance (Sahito & Vaisanen, 2020), compensation should also not be ignored because neglect of compensation will result in a decrease in performance which ultimately decreases organizational performance (Amjad et al., 2021; Zafar et al., 2021).

An effective compensation strategy requires a thorough understanding of the intricacies of designing pay structures, administering benefits, and recognizing individual and team accomplishments. Compensation policies should be transparent, consistently applied, and communicated effectively to all employees. Compensation strategies must be customized to fit each organization's specific needs and goals. Globalization has increased the importance of having effective compensation programs in organizations (Gašić, 2021). Organizations must recognize the vital role compensation plays in encouraging the behaviors and competencies required to achieve corporate objectives (Hong, 2017). An organization's compensation strategy reveals its priorities (Boudlaie et al., 2020).

Compensation strategies should be designed to incentivize the behaviors and competencies that drive organizational success (Hepner, 2019; Marin, 2021). Organizations use incentive programs to motivate employees and to achieve various other objectives, such as cost management, promoting perceived fairness, and encouraging submission approval (Baffoe & Bediako, 2021). A comprehensive compensation strategy should encompass financial and non-financial elements, including base pay, bonuses, incentives, benefits, recognition programs, and opportunities for professional development. By carefully integrating these components, organizations can create a holistic compensation package that motivates employees and contributes to overall organizational success. Compensation professionals and departments aim to align compensation with business objectives and strategy (Kang & Lee, 2021; Patiar & Wang, 2020).

Compensation is integral to an organization's ability to achieve sustainable competitive advantage, with worker characteristics and interactions forming the bedrock of strategic planning and implementation (Kang & Lee, 2021). In conjunction with other human resource practices, compensation practices can significantly impact employee attitudes and behaviors (Hassan, 2022; Howard & Dougherty, 2004). Organizations should recognize the importance of aligning compensation strategies with their organizational culture to foster innovation and drive business growth (Hepner, 2019; Madhani, 2014). The compensation strategy should address attracting elites of the job market with maximum payment (Boudlaie et al., 2020). Compensation systems play a critical role in influencing employee performance and organizational performance (Anwar & Abdullah, 2021; Zafar et al., 2021). When compensation is aligned with company strategy, it incentivizes developing common visions within the organizational culture.

The mediating role of motivation becomes particularly apparent when considering the limitations of compensation as a sole driver of performance. While financial incentives can undoubtedly attract and retain talent and even incentivize increased effort, they are unlikely to foster genuine passion, creativity, and a deep sense of ownership over one's work. The intricate

relationship between compensation, work motivation, and employee performance has been a subject of extensive research in organizational behavior and human resource management (Dina et al., 2017). While adequate compensation is often viewed as a direct driver of employee performance, the underlying mechanisms through which it exerts its influence are far more nuanced (Dina et al., 2017). Motivation, in particular, plays a pivotal mediating role in this relationship, acting as a catalyst that translates the potential benefits of compensation into tangible improvements in employee output and overall organizational success. Compensation serves as a tangible acknowledgment of an employee's value and contribution to the organization, and this recognition can significantly impact their level of motivation (Kholilah & Sari, 2021). This positive emotional response, in turn, fuels their intrinsic motivation, driving them to invest more effort and dedication into their work (Baffoe & Bediako, 2021).

CONCLUSION

Motivational factors are equally crucial in achieving sustainable performance outcomes. Indeed, while monetary compensation is essential for meeting basic needs and creating satisfaction, non-financial rewards—such as recognition, career development opportunities, and a positive work environment—are vital for fostering long-term employee engagement and commitment. Organizations prioritizing holistic compensation strategies are better positioned to cultivate an empowered workforce. This involves balancing various forms of compensation and ensuring that employees understand how their contributions link to the organization's success. Reinforcing positive behaviors through recognition and appreciation often surpasses the motivational effects. Moreover, communication plays a critical role in the effectiveness of any compensation strategy. Employees who perceive fairness and clarity in compensation practices will likely improve their motivation and subsequent performance. Organizations must acknowledge that successful compensation strategies go beyond mere financial incentives. They should include a robust framework that addresses employees' psychological and emotional needs. By implementing an integrated compensation system that provides for financial and non-financial components, organizations can achieve higher employee satisfaction and retention and sustained organizational performance that aligns with their strategic objectives. The effective management of compensation, as part of a holistic human resource strategy, thus serves as a critical lever for organizations looking to thrive in competitive environments. The contribution of this research is to provide a scientific basis for HR management to design a compensation system that is not only financially fair, but also strategic in improving employee motivation and performance. As for the implications, organizations need to understand that providing compensation does not only have a direct impact on performance, but also indirectly through increased motivation. This underscores the importance of a holistic compensation strategy, both financial (salary, bonuses) and non-financial (recognition, career development opportunities). However, this study has limitations, where this research is only carried out on one specific industry sector, so generalizations to other sectors are still limited. Therefore, future research can be carried out on various sectors and geographical regions to test the consistency of the model.

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