Job satisfaction not a persistent effect of wage increases

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Wage increases have no persistent effect on job satisfaction. Credit: Pixabay | CC0

After a wage increase, people tend to be more satisfied with their jobs—and even more so when what they have gained exceeds the wage increases of their colleagues. Yet, this effect on job satisfaction is not persistent. Two economists from University of Basel reported these findings in a study recently published in the *Journal of Economic Behavior & Organization*.

Dr. Patric Diriwaechter and Dr. Elena Shvartsman from the University of Basel's Faculty of Business and Economics have carried out an in-depth investigation on the relationship between job satisfaction and wage changes. This topic is also of interest to employers, since job satisfaction is one predictor of employee willingness to invest in firm-specific human capital and employee turn-over intentions.

For this study, almost 33,500 observations from the representative German Socio-Economic Panel were analyzed; the majority of individuals indicated job satisfaction of seven on a zero to 10 scale.

Even the expectation of a raise boosts satisfaction

In line with expectations, the study found that job satisfaction was positively influenced by wage increases. Social comparisons also played a part in this—job satisfaction increased further when an individual's wage rose by more than his/her peers' wages over the same period. Moreover, the researchers showed that employees were already more satisfied with their jobs one year before the effective wage increase, i.e., they appeared to be positively influenced by the mere expectation of a raise.

However, the rise in job satisfaction after a wage increase is only temporary, and the effect almost fades out within four years. According to behavioral-economic theory, this can be explained by the fact that people do not evaluate their income in absolute terms, but rather in relation to their previous income. Furthermore, people adapt to their new wage level over time, so a higher salary becomes the new reference point for future comparisons.

Small, regular increases are better

The same mechanisms appeared to be at work in the opposite direction. Negative reactions to wage cuts were also temporary, a finding that the researchers explain with reference point adaptations and social comparisons—since most wage cuts are associated with company- or industry-specific shocks, they typically also affect the respective individuals' colleagues.

The researchers conclude that wage increases can be a tool to motivate employees, yet only under carefully designed conditions, for instance, when they are implemented regularly and are accompanied by promotions. Diriwaechter and Shvartsman's results thus confirm the latest research findings from experimental economics, which indicate that wage increases in small, but regular increments—rather than less frequent but higher increases that add up to an equivalent amount—are the most effective way to motivate employees in the long run.

More information: Patric Diriwaechter et al, The anticipation and adaptation effects of intra- and interpersonal wage changes on job satisfaction, *Journal of Economic Behavior & Organization* (2017). DOI: 10.1016/j.jebo.2017.12.010

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