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Journal of Economic Behavior & Organization

journal homepage: www.elsevier.com/locate/jebo

Locus of control and performance appraisal

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ARTICLE INFO

Article history:

Received 15 April 2016

Received in revised form 22 June 2017

Accepted 23 June 2017

Available online 27 June 2017

JEL Classifications:

D03

J33

M52

Keywords:

Locus of control

Risk attitude

Performance appraisal

Performance pay

Sorting

Extrinsic rewards

Intrinsic motivation

ABSTRACT

We show that West German workers with an internal locus of control sort into jobs with performance appraisals. Appraisals provide workers who believe they control their environment a tool to demonstrate their value and achieve their goals. We confirm that workers who are risk tolerant also sort into jobs with performance appraisals but explain why the influence of the locus of control and risk tolerance should not be additive. We demonstrate this by estimating a routinely large and significantly negative interaction in our sorting equations. We also show that important patterns of sorting are revealed only when taking into account the interaction of locus of control and risk tolerance.

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1. Introduction

Economists increasingly recognize the role of non-cognitive skills in both human capital formation and the functioning of the workplace (Almlund et al., 2011; Borghans et al., 2008; Heckman et al., 2005). Cobb-Clark (2015: p. 1) identifies the recent reframing of traditional models to accommodate such skills as drivers of market outcomes as “one of the most exciting developments in labor economics over the past decade.” Among the fundamental personality characteristics economists examine is the locus of control, a concept that has played a long role in psychology (Gatz and Karel 1993; Phares 1976; Ng et al., 2006; Rotter 1966). Locus of control identifies the extent to which individuals think that their actions cause the consequences they encounter. Those who see a tighter connection are identified as having a more internal locus (they more nearly think they control outcomes). Those who see a looser connection are identified as having a more external locus (they more nearly think that luck, chance or other people control outcomes).

Those economists who see it as driver of outcomes take locus of control to be stable and, if not completely exogenous, unlikely to change in response to the outcomes being examined. Indeed, Cobb-Clark and Schurer (2013) examine this directly as part of testing the underpinnings of using the locus of control in labor economics. They show that typical locus measures

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change only very modestly over the short to medium run, that any changes are concentrated among the young and very old and that the changes are not related to demographic, labor market or health events. They conclude that the locus of control is 'remarkably stable' and that applied researchers who limit their sample to working age subjects can, with suitable caution, take measures of the locus as drivers of economic behavior rather than as merely the reflection of labor market outcomes.

Previous research has shown a role for locus of control in a variety of settings. Those with a more internal focus believe that investing in human capital has a higher return than do those with an external locus. Thus, they perform better in school (Hadsell 2010; Mendolia and Walker 2014) and more likely complete high school and attend college (Coleman and DeLeire 2003).¹ They are also more likely to make long-term investments in personal health (Chiteji 2010; Cobb-Clark et al., 2014).² The unemployed with an internal locus believe that their search effort generates a larger increase in the job offer rate and have been shown to search more and retain higher reservation wages than those with an external locus (Caliendo et al., 2015; McGee 2015; McGee and McGee 2016). Similarly, individuals with an internal locus are more likely to become entrepreneurs (Caliendo et al., 2014). These results follow showings of a persistent earnings return to the non-cognitive skill of an internal locus (Bowles et al., 2001a; Duncan and Dunifon, 1998; Stefanec, 2010). While not exhaustive, this summary suggests that perceptions of returns can be critical in understanding behavior and that those perceptions reflect, in part, a reasonably stable locus of control.

We present a unique examination focused on performance appraisals. Performance appraisals remain the most common form of performance management.³ They measure individual worker performance based on combinations of objective and subjective evaluation. Such appraisals are used to provide feedback to workers, to make job assignments, to determine training needs, and to allocate both short- and long-term rewards including but not limited to annual bonuses and promotion. We examine the hypothesis that locus of control drives the sorting of workers into jobs with performance appraisal. Workers who have an internal locus should view performance appraisals as a mechanism that translates their efforts and skills into better assignments and greater earnings. Thus, they should sort into jobs with appraisals. By contrast, workers with an external locus should sort out of such jobs as they view the outcomes of their efforts as more nearly a random process such that performance appraisals are as likely to ignore as reward their efforts.

Using the German Socio-Economic Panel (SOEP), we confirm that those with an internal locus sort into jobs with performance appraisal. This result is particularly strong for performance appraisals that have consequences for workers' pay. The relationship with the locus of control remains when controlling for worker characteristics, basic firm characteristics, and for industry and occupation. It also remains when accounting for other major personality characteristics, namely risk preferences, time preferences, reciprocity, trust, and the Big Five.

Our results shed light on models arguing that more productive workers sort into jobs with performance pay (Booth and Frank 1999; Cornelissen et al., 2011; Lazear 1986, 2000). We show that a worker's belief that he or she can control outcomes plays an important role in such sorting. This belief influences the worker's motivation and job performance. We join the few economic studies examining the association between personality characteristics and performance pay (Dohmen and Falk, 2010, 2011). Only Curme and Stefanec (2007) test for an association between locus of control and performance pay. Their study is based on U.S. data.

While previous research focused on sorting into performance pay, our study provides a more nuanced view. We differentiate between performance appraisals with and without consequences for the worker's earnings. Economists may see locus of control primarily as a subjective perception of the expected value of extrinsic rewards. However, as we make clear in the next section, psychologists stress that locus of control contributes to self-esteem and happiness. Thus, performance appraisals may have intrinsic value to workers with an internal locus. These workers expect that they can influence performance appraisals through successful accomplishment of tasks to obtain positive feedback resulting in feelings of pride, competence and self-worth. Thus, workers with an internal locus should not only sort into performance appraisals with monetary rewards but also, albeit to a lesser extent, into performance appraisals without such rewards. Indeed, our estimates support this hypothesis.

We also examine the interaction of locus of control with risk attitude. While risk attitude reflects a worker's preference towards risk, locus of control involves expectations about the risks influencing the worker's outcomes. Thus, locus of control and risk attitudes should play an intertwined role in the sorting into performance appraisals. An internal locus implies that the worker expects to control the outcome of performance appraisals so that he or she perceives little uncertainty. Risk-averse workers positively value low uncertainty whereas risk-loving workers negatively value it. Thus, a high degree of risk aversion should reinforce the propensity of workers with an internal locus to sort into performance appraisals while a high degree of risk love should weaken that propensity. This prediction is supported by our estimates showing a large and significantly negative interaction of risk tolerance and internal locus of control. Moreover, the estimates demonstrate that the full pattern of sorting is only revealed when taking into account this interaction effect.

¹ We note the results from Cebi (2007) that the return to an internal locus of control as a teenager and young adult may not be in degree completion but in higher earnings later in life.

² Individuals with an internal locus of control also appear to be more resilient to negative life events such as illness and injury (Buddelmeyer and Powdthavee, 2016; Schurer, 2017).

³ In Australia and Britain, two thirds of the workplaces use formal performance appraisal systems (Heywood and Brown, 2005; Addison and Belfield, 2008). The share is modestly higher in the Netherlands (Jirjahn and Poutsma, 2013). In Germany, slightly more than half of private sector establishments use formal appraisal systems (Heywood and Jirjahn, 2014).

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