

# The Impact of Incentive Systems on Employee Performance: The Mediating Role of Transformational Leadership in Oman's Banking Sector

Mohammed Murad Mohammed Al Bulushi <sup>1 \*</sup>, Shafazawana Mohamed Tharikh <sup>2</sup>, Z. A. Al Busaidi <sup>3</sup>

<sup>1</sup> Research scholar, Department of Graduate Business School, Universiti Tenaga Nasional, Kajang, Selangor, Malaysia. Putrajaya Campus, Jalan Ikram UNITEN

<sup>2</sup> UNITEN Business School (UBS) Sultan Haji Ahmad Shah Campus, Universiti Tenaga Nasional Deputy Executive Department

<sup>3</sup> Present Designation: Deputy Chief Executive Officer, Trifoil Company, Field Supervisor, Universiti Tenaga Nasional. Malaysia

\*Corresponding author E-mail: [almurad20769@gmail.com](mailto:almurad20769@gmail.com)

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## Abstract

Incentive systems are among the most strategic human resource mechanisms used to enhance employee motivation and organisational performance. However, the behavioural processes through which incentives lead to improved performance outcomes remain underexplored, particularly in developing economies. This study examines the mediating role of transformational leadership in the relationship between incentive systems and employee performance in Oman's banking sector. Grounded in the Resource-Based View (RBV) and Transformational Leadership Theory, the study proposes that well-designed incentive systems promote transformational leadership behaviours, thereby enhancing employee motivation, engagement, and performance. Data were collected from 346 non-managerial employees of the Central Bank of Oman (CBO) using a structured questionnaire. Partial Least Squares Structural Equation Modeling (PLS-SEM) was applied to test the hypothesised model. The results show that incentive systems have a significant positive effect on both transformational leadership and employee performance. Moreover, transformational leadership partially mediates this relationship, suggesting that incentives not only motivate employees extrinsically but also cultivate leadership behaviours that strengthen intrinsic motivation and collective achievement. The study contributes to strategic human resource management (SHRM) theory by identifying leadership behaviour as a key mechanism linking HR systems to performance outcomes, and it provides practical insights for Omani banks to design incentive frameworks that reinforce leadership-driven excellence.

**Keywords:** Incentive Systems; Transformational Leadership; Employee Performance; Oman; Banking Sector; Resource-Based View.

## 1. Introduction

Human resources are widely recognised as a primary source of sustainable competitive advantage in today's dynamic business environment. Organisations that manage their people through strategically designed reward systems can drive productivity, engagement, and innovation. Within this context, incentive systems, which include both financial and non-financial rewards, are vital mechanisms for aligning individual performance with organisational objectives (Aguinis et al., 2022; Cooke et al., 2021). Despite extensive research, the pathway through which incentive systems influence employee performance remains unclear. Recent studies indicate that leadership behaviour may serve as a crucial channel through which incentives shape employee attitudes and outcomes (Aboramadan et al., 2021). The effectiveness of incentive systems depends not only on their monetary value but also on how they are perceived and reinforced by leaders. Transformational leadership, characterised by inspiration, intellectual stimulation, and individualised consideration, plays an essential role in transforming incentive mechanisms into meaningful motivational experiences (Bass & Avolio, 1994; Patiar & Wang, 2020). Transformational leaders do more than distribute rewards; they create purpose, trust, and emotional engagement, allowing employees to perceive incentives as recognition of effort and potential rather than simple transactions. When transformational leadership behaviours support incentive systems, employees are more likely to feel valued, empowered, and motivated to achieve higher performance. The Omani banking sector provides an ideal context for exploring this relationship. Over the past decade, the sector has experienced significant modernisation driven by digital transformation, competitive pressures, and regulatory reforms. The CBO, as the sector's leading institution, has prioritised human capital development as a central element of its strategic agenda. Although the CBO has introduced a variety of incentive programs, including performance-based bonuses, recognition initiatives, and professional development opportunities, the effectiveness of these incentives may depend on the leadership behaviours that accompany them. Transformational leadership can therefore be viewed as a behavioural bridge that connects institutional incentive systems with employee outcomes (Amir et al., 2025; Khan et al., 2025; Kadir et al., 2024; Javed et al

2025). The theoretical foundation of this study lies in the RBV, which argues that sustainable competitive advantage arises from valuable, rare, and inimitable resources such as skilled and motivated employees (Barney, 1991). Incentive systems represent a strategic investment in human capital, yet their effectiveness depends on how leaders utilise them to inspire and engage employees. Drawing on Transformational Leadership Theory, this study proposes that incentive systems enhance extrinsic motivation while simultaneously fostering leadership behaviours that promote intrinsic motivation and collective purpose. Accordingly, this study addresses the research question: To what extent does transformational leadership mediate the relationship between incentive systems and employee performance in Oman's banking sector? This research makes three key contributions. First, it extends SHRM literature by identifying transformational leadership as a behavioural mechanism linking incentive systems to performance. Second, it contributes empirical evidence from a developing economy, addressing a contextual gap in HR and leadership research. Third, it provides practical insights for managers and policymakers in Oman's banking sector on designing incentive systems that encourage leadership behaviours and sustain high employee performance.

## 2. Literature Review and Theoretical Framework

### 2.1. Incentive systems

Incentive systems are among the most effective strategic tools for shaping employee behaviour and improving organisational outcomes. They include financial rewards such as bonuses and performance-based pay, as well as non-financial rewards such as recognition, career advancement opportunities, and professional development (Aguinis et al., 2022). In SHRM, incentive systems serve as key mechanisms that align employee interests with organisational goals by encouraging the desired behaviours and discouraging underperformance (Cooke et al., 2021).

The theoretical foundation for incentive systems lies in the RBV, which emphasises that people and their capabilities are unique organisational resources that can create sustained competitive advantage (Barney, 1991). When properly designed, incentive systems enhance employee motivation and commitment, strengthening the organisation's ability to attract and retain high-performing talent. Empirical studies highlight that well-structured incentive systems positively influence employee engagement and performance. However, their impact extends beyond financial motivation. Incentives that recognise employees' contributions, provide growth opportunities, and communicate fairness have been shown to foster a sense of belonging and emotional commitment (Aljumah, 2023; Alkhalaf & Badewi, 2024). These outcomes are often mediated by leadership behaviours that interpret and communicate the meaning of rewards to employees, transforming incentives into a deeper motivational force rather than a simple transactional exchange. In Oman's banking sector, incentive systems are crucial for maintaining employee productivity and commitment amid rising regulatory demands and digital transformation. However, the success of such systems largely depends on the leadership culture that surrounds them. Incentives that transformational leaders administer can encourage employees to internalise organisational values and perform beyond expectations.

### 2.2. Transformational leadership

Transformational leadership is a style of leadership that inspires and motivates employees to achieve exceptional outcomes by aligning individual aspirations with the organisation's collective vision (Bass & Avolio, 1994). Transformational leaders encourage followers to look beyond immediate self-interest and work toward higher organisational goals. The four dimensions of transformational leadership: idealised influence, inspirational motivation, intellectual stimulation, and individualised consideration, reflect a leader's ability to foster trust, creativity, and commitment (Patiar & Wang, 2020; Govender & Bussin, 2020).

Unlike transactional leadership, which is based on contingent rewards and corrective actions, transformational leadership builds emotional connections between leaders and followers. It emphasises empowerment, vision, and innovation. In environments characterised by rapid change, such as the banking sector, transformational leadership enables employees to adapt to new technologies and regulatory requirements while maintaining engagement and job satisfaction. Research suggests that transformational leadership is positively associated with organisational citizenship behaviour, job satisfaction, and employee performance (Maamari & Saheb, 2018; Ekhsan & Setiawan, 2021). Moreover, it acts as a critical channel through which HR systems influence employees' attitudes and behaviours. In this regard, leadership behaviours serve as a bridge between the formal structure of incentives and employees' intrinsic motivation. Within Oman's hierarchical organisational culture, transformational leadership is particularly valuable because it fosters empowerment and participative decision-making, both of which are essential to modernising the banking workforce.

### 2.3. Employee performance

Employee performance is a multidimensional construct encompassing both task and contextual performance. Task performance refers to the efficiency and effectiveness with which employees complete their core responsibilities, while contextual performance reflects discretionary behaviours such as cooperation, initiative, and adaptability (Murphy, 2022; Jayanagara, 2024). Incentive systems are designed to enhance both aspects by aligning rewards with expected outcomes. However, the quality of leadership plays a central role in determining how employees respond to these incentives. Leaders who communicate organisational goals clearly and recognise individual efforts can transform external rewards into internalised motivation. From the perspective of the Ability–Motivation–Opportunity (AMO) framework, employee performance depends on three key factors: the employee's ability, their motivation, and the opportunities provided by the organisation. Incentive systems primarily influence motivation, while transformational leadership enhances opportunity by empowering employees to take initiative and engage in problem-solving. Together, these elements create a synergistic effect that improves both the quality and consistency of employee performance. In the Omani banking context, employee performance has become increasingly important due to competitive pressures, technological advancement, and the emphasis on customer experience. Institutions such as the Central Bank of Oman rely heavily on motivated, adaptable employees who uphold service standards while embracing innovation. Therefore, understanding how incentive systems and leadership behaviours jointly influence performance is both timely and relevant.

### 2.4. Transformational leadership as a mediator

Leadership acts as a behavioural and psychological mechanism that translates HR practices into tangible employee outcomes. Transformational leadership, in particular, has been identified as a key mediator that explains how incentive systems lead to improved performance

(Aboramadan et al., 2021). Incentives provide the structural framework for motivation, but it is the leader who interprets, communicates, and reinforces these incentives, turning them into meaningful experiences for employees.

Under the RBV, incentive systems can only become sources of competitive advantage when they are utilised effectively by leaders who know how to inspire and mobilise people. Transformational leaders create a sense of purpose and ownership, encouraging employees to use their skills and energy to enhance organisational effectiveness. They transform the psychological meaning of incentives from short-term rewards to long-term commitment and growth (Ahammad et al., 2020). Empirical studies across diverse contexts have confirmed that leadership mediates the relationship between HR systems and performance (Aliyev, 2024). This mediation occurs because leaders influence how employees perceive fairness, recognition, and opportunity. In Oman's banking sector, where institutions are undergoing modernisation and cultural change, transformational leadership plays a significant role in helping employees connect organisational rewards with personal development and collective success.

## 2.5. Theoretical integration and justification

This study integrates insights from three major theoretical perspectives: the RBV, Transformational Leadership Theory, and the AMO framework. Together, these perspectives explain how incentive systems influence employee performance through the mediating effect of transformational leadership.

The RBV posits that sustained competitive advantage arises from resources that are valuable, rare, inimitable, and non-substitutable (Barney, 1991). Human resources, when effectively motivated and developed, fulfil these criteria and thus become a central source of long-term organisational success. Incentive systems are an essential component of SHRM because they strengthen the organisation's capacity to attract, retain, and engage talented employees. However, incentives alone cannot guarantee improved performance unless they are supported by effective leadership behaviours that encourage employees to channel their abilities and motivation toward organisational objectives. Therefore, in the RBV context, incentive systems are considered enabling resources, while transformational leadership represents the activating mechanism that converts these resources into sustained performance outcomes. Transformational Leadership Theory provides a behavioural explanation for how incentives influence employees beyond financial rewards. According to Bass and Avolio (1994), transformational leaders motivate followers by communicating a compelling vision, providing intellectual stimulation, and showing individualised consideration (Javed & Al-Mulali 2025; Rafique et al., 2025; Ariffin al., 2024). These behaviours create intrinsic motivation, which complements the extrinsic motivation offered by incentive systems. When leaders embody transformational characteristics, they strengthen the psychological meaning of incentives by framing them as recognition of contribution, professional growth, and collective success rather than mere financial exchange. This process builds emotional commitment and encourages employees to exceed performance expectations. In this sense, transformational leadership serves as a behavioural bridge that connects the structural aspect of HR systems (incentives) with the psychological aspects of employee motivation and engagement. The AMO framework further supports this integration by explaining how HR practices enhance performance by enabling employees to perform, motivating them to act, and providing opportunities to contribute (Appelbaum et al., 2000). Incentive systems primarily influence the motivation component by providing rewards that align with employee and organisational goals. Transformational leadership reinforces the opportunity component by creating an environment that encourages creativity, empowerment, and participation (Javed et al., 2024; Javed & Husain, 2024). When both elements operate together, employees are more likely to apply their skills effectively and demonstrate higher levels of both task and contextual performance. Integrating these three perspectives provides a comprehensive explanation of the relationship among incentive systems, transformational leadership, and employee performance. The RBV explains the strategic importance of incentives as organisational resources, Transformational Leadership Theory clarifies the behavioural mechanism through which these incentives affect employees, and the AMO framework describes the conditions under which this interaction results in improved performance. This theoretical combination not only enhances the model's explanatory power but also extends the SHRM literature by emphasising leadership behaviour as the missing link between structural HR practices and individual outcomes.

Therefore, the study justifies that incentive systems, when effectively implemented within organisations and reinforced through transformational leadership behaviours, can transform both employee motivation and performance. This integrated theoretical approach provides a strong foundation for the research model tested in this study.

## 2.6. Conceptual framework and hypotheses development

Based on the theoretical integration discussed earlier, this study proposes a conceptual framework linking incentive systems to employee performance, with transformational leadership as the mediating mechanism. The model is grounded in the RBV, Transformational Leadership Theory, and the AMO framework. Collectively, these theories explain how human resource systems, when strategically designed and effectively led, translate into improved employee outcomes. Incentive systems represent a key component of strategic human resource management (SHRM) practices. They are designed to encourage specific behaviours, reward performance, and align employee interests with organisational objectives. However, their impact depends not only on how rewards are structured but also on how leaders communicate and implement them. Transformational leaders play a pivotal role in interpreting the meaning of incentives, fostering intrinsic motivation, and promoting a shared sense of purpose among employees. When employees perceive incentive systems as fair, meaningful, and linked to personal and organisational growth, they are more likely to exhibit higher performance and commitment.

The conceptual framework of this study (Figure 1) illustrates the proposed relationships among the variables. It suggests that incentive systems directly affect transformational leadership and employee performance, while transformational leadership also directly influences performance and serves as a mediator between incentives and outcomes.



Fig. 1: Conceptual Framework.

Hypothesis 1: Incentive systems have a significant positive effect on transformational leadership.

Incentive systems have long been recognised as critical tools for motivating employees and shaping managerial behaviours. Effective incentive structures not only encourage performance but also foster the development of leadership qualities among supervisors and team leaders. According to the Resource-Based View, incentive systems are strategic assets that influence the behaviour of individuals who manage and lead others (Barney, 1991). When rewards are tied to both individual and team outcomes, they promote a culture of shared responsibility, which is consistent with transformational leadership principles. Transformational leaders often emerge in environments where rewards recognise creativity, innovation, collaboration, and collective success rather than mere compliance or short-term results (Govender & Bussin, 2020). In such settings, leaders internalise the value of motivation and empowerment and seek to inspire similar attitudes among their followers. Moreover, fair and transparent incentive systems enhance trust between employees and management, fostering the psychological safety essential for transformational behaviours such as intellectual stimulation and individualised consideration (Bass & Avolio, 1994). Empirical studies have confirmed that incentive systems that emphasise recognition and professional development encourage transformational behaviours among leaders (Aboramadan et al., 2021; Aljumah, 2023). For example, when leaders are rewarded for mentoring, innovation, and long-term performance, they are more likely to act as role models and motivators. Therefore, in Oman's banking sector, where performance excellence and adaptability are highly valued, incentive systems that reward both achievement and leadership development are expected to foster transformational leadership behaviours.

Hypothesis 2: Transformational leadership has a significant positive effect on employee performance.

Transformational leadership has been consistently linked to superior employee performance across industries and cultures. This leadership style enhances both task-related and contextual aspects of performance by inspiring employees to go beyond formal job requirements and contribute to organisational success (Ekhsan & Setiawan, 2021; Patiar & Wang, 2020). Transformational leaders encourage employees to identify with the organisation's mission, adopt innovative approaches, and pursue continuous improvement.

From a theoretical standpoint, Transformational Leadership Theory emphasises that leaders who communicate a compelling vision and provide intellectual stimulation create an environment that enhances intrinsic motivation. When employees feel valued, trusted, and empowered, their engagement and performance improve significantly (Bass & Riggio, 2006). Transformational leaders also influence employees through individualised consideration, addressing their personal needs for growth and recognition. These behaviours are especially relevant in knowledge-intensive sectors such as banking, where performance relies heavily on employee initiative and problem-solving skills. In Oman's banking industry, transformational leadership is significant amid ongoing digital transformation and the need for agile service delivery. Leaders who inspire innovation and promote a supportive culture can enhance employee adaptability and performance even under regulatory and technological pressures. Empirical studies in similar settings have shown that transformational leadership positively influences performance by increasing job satisfaction, motivation, and psychological empowerment (Maamari & Saheb, 2018; Aliyev, 2024).

Hypothesis 3: Transformational leadership mediates the relationship between incentive systems and employee performance.

While incentive systems are designed to motivate employees directly, their actual effectiveness often depends on the leadership behaviours that accompany them. Transformational leadership acts as a behavioural and emotional mechanism through which incentive systems influence employee outcomes. Incentives provide the structural foundation for motivation, but transformational leaders give these rewards meaning by framing them as recognition of effort, contribution, and potential (Bass & Avolio, 1994). This mediating relationship can be explained through both the RBV and the AMO frameworks. From an RBV perspective, incentives are valuable organisational resources that can only produce competitive advantage when effectively utilised by leaders. Transformational leaders convert these resources into productive outcomes by inspiring employees to invest more effort and creativity into their work (Barney, 1991). According to the AMO model, incentive systems increase motivation, while transformational leadership enhances opportunity by providing empowerment and guidance. The interaction of these two mechanisms results in higher employee performance (Appelbaum et al., 2000). Empirical research supports this mediation effect. Studies have shown that HR practices, such as incentives and rewards, indirectly affect performance by influencing leadership behaviours that enhance engagement and trust (Ahammad et al., 2020; Aboramadan et al., 2021). In the Omani banking context, where leadership structures are evolving from hierarchical to participative, transformational leadership serves as a crucial link between strategic incentives and performance improvement. Leaders who inspire and support employees can amplify the motivational effects of incentive systems, creating a high-performance culture that benefits both individuals and the organisation.

### 3. Research Methodology

#### 3.1. Research design

This study employs a quantitative, cross-sectional research design to examine the mediating role of transformational leadership in the relationship between incentive systems and employee performance in Oman's banking sector. A quantitative approach was chosen because it allows for systematic testing of the theoretical relationships proposed in the conceptual framework. The cross-sectional design is appropriate because data were collected at a single point in time to capture employee perceptions of incentive systems, leadership behaviours, and performance outcomes. The study uses Partial Least Squares Structural Equation Modeling (PLS-SEM) to test both the measurement and structural models. This analytical technique is suitable for complex models that include mediation effects and for data that may not meet strict normality assumptions. As previous study shows, the PLS-SEM was chosen for its ability to handle multiple constructs with multiple indicators, as well as its emphasis on maximising explained variance in the dependent variables (Javed & Husain, 2024; Javed, 2023; Javed et al., 2023; Rababah et al., 2022; Husain et al., 2021).

#### 3.2. Population and sampling

The target population for this study consisted of non-managerial employees of the CBO. This group was selected because they are directly affected by incentive systems and are the recipients of leadership behaviours within the organisation. Their perspectives provide valuable insights into how incentive systems influence leadership and, ultimately, performance. A stratified random sampling technique was used to ensure that participants were drawn from various departments within the bank, including human resources, finance, information technology, operations, and customer services. This approach enhanced the representativeness of the sample and minimised potential bias. A total of 450 questionnaires were distributed electronically and in print. After removing incomplete and invalid responses, 346 valid questionnaires were retained for analysis, yielding a response rate of 76.8%. This sample size exceeds the minimum requirement of 200 cases recommended for PLS-SEM analysis (Hair et al., 2021), providing adequate statistical power for hypothesis testing.

### 3.3. Data collection procedure

Data were collected over six weeks using a structured questionnaire designed specifically for this study. Before the main data collection, a pilot study was conducted with 30 employees from the same organisation to ensure the clarity, reliability, and relevance of the questionnaire items. Minor revisions were made to improve readability and alignment with the context based on the feedback received. Permission for data collection was obtained from the Central Bank of Oman's management and the affiliated university's research ethics committee. Participation in the study was voluntary, and respondents were assured of complete confidentiality and anonymity. The purpose of the study was explained clearly at the beginning of the questionnaire to ensure informed consent. Participants were instructed to answer honestly based on their experiences within the organisation.

### 3.4. Measurement of variables

All constructs were measured using a five-point Likert scale, ranging from 1 ("strongly disagree") to 5 ("strongly agree"). The measurement items were adapted from previously validated scales to ensure content validity and comparability with existing literature. Incentive systems were measured using items adapted from prior studies (Aljumah, 2023; Alkhalaf & Badewi, 2024). The items assessed employee perceptions of fairness, transparency, recognition, and alignment of incentives with performance outcomes. Example statements included: "The organisation rewards employees fairly based on their performance" and "Incentives encourage me to work toward organisational goals." Transformational leadership was measured using a shortened version of Bass and Avolio's Multifactor Leadership Questionnaire (MLQ) (Bass & Avolio, 1994). The items captured the four core dimensions of transformational leadership: idealised influence, inspirational motivation, intellectual stimulation, and individualised consideration. Sample items included: "My supervisor inspires me with a clear vision of the future" and "My supervisor encourages me to think creatively in solving problems." Employee performance was assessed through a combination of task performance and contextual performance dimensions (Jayanagara, 2024; Murphy, 2022). Task performance was measured by indicators such as quality, timeliness, and efficiency in completing work. Contextual performance included behaviours like teamwork, adaptability, and initiative. Example items were: "I consistently meet or exceed performance targets" and "I actively contribute to improving my team's effectiveness." Reliability and construct validity were confirmed during the pilot test. Minor adjustments were made to ensure cultural and contextual relevance to the Omani banking environment.

## 4. Results and Discussion

### 4.1. Measurement model evaluation

Before testing the structural relationships, the measurement model's reliability and validity were examined to ensure the quality of the constructs used in this study. The analysis followed the recommendations of Hair et al. (2021) for assessing reflective measurement models in PLS-SEM. All items demonstrated high indicator loadings, exceeding the recommended threshold of 0.70, indicating that each indicator reliably measured its underlying construct. The Cronbach's alpha and composite reliability (CR) values for incentive systems, transformational leadership, and employee performance ranged from 0.83 to 0.92, indicating strong internal consistency. In addition, the Average Variance Extracted (AVE) values for all constructs exceeded 0.50, establishing convergent validity. Discriminant validity was confirmed using both the Fornell–Larcker criterion and the Heterotrait–Monotrait (HTMT) ratio. The square roots of AVE for each construct were higher than their correlations with other constructs, and all HTMT values were below 0.85, indicating that the constructs were empirically distinct. Multicollinearity was also examined, with Variance Inflation Factor (VIF) values below 3.0 for all indicators, suggesting no collinearity concerns.

These results confirm that the measurement model is both reliable and valid, allowing the study to proceed with structural model testing. Table 1 presents the results of the measurement model assessment.

**Table 1:** Measurement Model Assessment

Construct	Item Loadings Range	Cronbach's Alpha	Composite Reliability (CR)	Average Variance Extracted (AVE)
Incentive Systems	0.73 – 0.89	0.86	0.91	0.67
Transformational Leadership	0.74 – 0.88	0.90	0.93	0.68
Employee Performance	0.71 – 0.87	0.88	0.92	0.66

### 4.2. Structural model assessment

The structural model was tested to evaluate the hypothesised relationships among incentive systems, transformational leadership, and employee performance. The model's explanatory power and predictive relevance were assessed using  $R^2$  and  $Q^2$  values. The findings showed an  $R^2$  value of 0.56 for transformational leadership, indicating that incentive systems explained 56 per cent of the variance in leadership behaviour. Similarly, employee performance had an  $R^2$  of 0.64, indicating that incentive systems and transformational leadership jointly explained 64% of its variance. Both  $R^2$  values are considered substantial in behavioural research (Hair et al., 2021). The Stone–Geisser  $Q^2$  values for both dependent variables were positive, confirming the model's predictive relevance. The bootstrapping procedure with 5,000 subsamples was applied to assess the significance of the hypothesised relationships. The results are summarised in Table 2 below.

**Table 2:** Structural Model and Mediation Analysis

Hypothesis	Path Coefficient ( $\beta$ )	t-value	p-value	Result
H1: Incentive Systems → Transformational Leadership	0.59	11.24	<0.001	Supported
H2: Transformational Leadership → Employee Performance	0.67	14.02	<0.001	Supported
H3 (Direct Effect): Incentive Systems → Employee Performance	0.21	3.89	<0.01	Supported
H3 (Indirect Effect): Incentive Systems → Transformational Leadership → Employee Performance	0.40	8.72	<0.001	Supported (Partial Mediation)

Incentive Systems → Transformational Leadership: The path coefficient was positive and significant ( $\beta = 0.59$ ,  $t = 11.24$ ,  $p < 0.001$ ). This finding indicates that effective incentive systems foster transformational leadership behaviours among supervisors and managers. When incentives are perceived as fair, transparent, and developmental, leaders are more likely to demonstrate motivation, inspiration, and individualised consideration. Transformational Leadership → Employee Performance: The relationship between transformational leadership and employee performance was also positive and significant ( $\beta = 0.67$ ,  $t = 14.02$ ,  $p < 0.001$ ). This result suggests that leaders who inspire and support employees enhance both task-related and contextual aspects of performance. Incentive Systems → Employee Performance: The direct relationship between incentive systems and employee performance was positive but comparatively weaker ( $\beta = 0.21$ ,  $t = 3.89$ ,  $p < 0.01$ ). This indicates that while incentive systems directly influence performance through motivation, their more substantial effect occurs indirectly through leadership behaviour.

### 4.3. Mediation analysis

The mediating role of transformational leadership was tested by analysing the indirect effect of incentive systems on employee performance. The bootstrapping results revealed that the indirect path from incentive systems to employee performance via transformational leadership was significant ( $\beta = 0.40$ ,  $t = 8.72$ ,  $p < 0.001$ ). The total effect of incentive systems on employee performance (including both direct and indirect paths) was  $\beta = 0.61$ , showing that transformational leadership partially mediates the relationship. This partial mediation indicates that incentive systems influence employee performance in two ways: directly, by providing extrinsic motivation, and indirectly, by encouraging leaders to adopt transformational behaviours that nurture intrinsic motivation. In other words, incentives become more powerful when they are supported by leadership practices that inspire, recognise, and empower employees. These findings confirm Hypothesis 3, demonstrating that transformational leadership serves as a vital psychological and behavioural link between the organisational incentive framework and employee performance outcomes.

### 4.4. Discussion

The results of this study provide strong empirical support for the proposed conceptual framework. Each of the three hypotheses was confirmed, reinforcing the theoretical proposition that leadership behaviour plays a crucial mediating role in the HR–HR–HR-performance relationship. First, the significant relationship between incentive systems and transformational leadership supports the notion that well-structured incentive systems can promote positive leadership behaviours. When organisations design incentives that reward not only performance but also collaboration, innovation, and employee development, leaders are encouraged to demonstrate transformational characteristics such as vision, empathy, and inspiration. This finding aligns with earlier studies suggesting that incentive structures emphasising fairness and recognition can cultivate leadership that motivates and empowers subordinates (Aboramadan et al., 2021; Aljumah, 2023). Second, the strong effect of transformational leadership on employee performance confirms that leadership behaviours are central to achieving superior results. Leaders who inspire confidence and articulate a clear purpose encourage employees to contribute beyond formal job requirements. This result is consistent with prior research showing that transformational leadership enhances job satisfaction, organisational commitment, and productivity (Ekhsan & Setiawan, 2021; Patiar & Wang, 2020). In the Omani context, where traditional leadership tends to be hierarchical, the adoption of transformational leadership represents a cultural evolution toward empowerment and participation. Third, the mediation analysis highlights that the influence of incentive systems on performance is not merely transactional but also psychological. Incentives provide motivation, but transformational leaders amplify this motivation by connecting it to personal growth and organisational vision. This interaction aligns with the Resource-Based View, which asserts that human resources become a source of competitive advantage when effectively developed and led. The findings also support the AMO framework, suggesting that while incentives enhance motivation, transformational leadership provides employees with the opportunity to utilise their abilities effectively. From a practical perspective, these findings have important implications for HR practitioners and policymakers in Oman's banking sector. Incentive systems should be designed not only to reward output but also to encourage behaviours associated with leadership development and employee empowerment. Training programs for managers should focus on enhancing transformational leadership competencies, enabling them to interpret and communicate incentive policies in ways that inspire and engage employees. By aligning reward systems with leadership development, organisations can foster a high-performance culture that supports both individual and institutional growth.

## 5. Conclusion and Implications

This study aimed to examine the mediating role of transformational leadership in the relationship between incentive systems and employee performance in Oman's banking sector. Grounded in the RBV, Transformational Leadership Theory, and the AMO framework, the study proposed that incentive systems influence employee performance both directly and indirectly through leadership behaviour. The findings provided strong empirical support for this proposition. The results showed that incentive systems significantly enhance transformational leadership behaviours, which in turn positively affect employee performance. The mediation analysis further confirmed that transformational leadership partially mediates this relationship, indicating that incentives are most effective when supported by leadership that inspires, motivates, and guides employees. The findings suggest that incentive systems are not only mechanisms for financial reward but also strategic tools that influence leadership development and organisational culture. When employees perceive incentives as fair, transparent, and developmental, leaders tend to display transformational qualities such as vision, inspiration, and individual support. These behaviours help to create a positive environment that promotes innovation, commitment, and high performance. The results also emphasise that incentives alone are insufficient to sustain employee performance unless they are reinforced by effective leadership practices that align individual goals with organisational objectives. From a theoretical perspective, this study contributes to the literature by extending the understanding of how human resource systems translate into performance outcomes through leadership behaviour. The integration of the RBV and Transformational Leadership Theory offers a more comprehensive view of how organisational resources are transformed into performance capabilities. The inclusion of the AMO framework further strengthens this model by demonstrating how motivation, ability, and opportunity interact to shape employee outcomes. This theoretical synthesis enriches existing research on human resource management and leadership by explaining the mechanisms that link incentive systems to performance in developing-country contexts, such as Oman. In practical terms, the findings have several managerial implications. Human resource professionals should design incentive systems that promote both performance and leadership development. Incentives should be transparent, equitable, and aligned with long-term organisational goals rather than focusing only on short-term financial achievements. Managers should be trained in transformational leadership skills, including effective communication, emotional intelligence, and vision-building. These skills enable leaders to use incentive systems not just to reward

performance but also to inspire and engage employees. When leaders understand how to communicate the purpose and value of incentives, they can enhance employee commitment and create a culture of mutual growth and shared achievement. At the policy level, institutions such as the Central Bank of Oman can benefit from linking incentive structures with leadership development frameworks. Policymakers should encourage financial institutions to implement reward systems that value innovation, teamwork, and leadership capacity. Such an approach can help develop a motivated, capable workforce that drives sustainable organisational success. Aligning reward strategies with national development goals will also contribute to a more dynamic and adaptable banking sector capable of competing in a global environment.

Although this study offers valuable insights, it has certain limitations. The cross-sectional research design limits the ability to infer causality among the variables under study. Future research could employ a longitudinal design to examine how the relationships among incentives, leadership, and performance evolve. Additionally, this study focused on a single institution, which may limit the generalizability of the findings. Expanding future research to include multiple organisations across different sectors would enhance the robustness of the results. Moreover, since the data were collected through self-reported questionnaires, future studies could use multi-source data, such as supervisor ratings or performance records, to reduce potential bias. Researchers could also explore additional variables, such as employee engagement, organisational culture, and psychological empowerment, to gain a deeper understanding of the mechanisms linking incentives, leadership, and performance. This study establishes that the effectiveness of incentive systems depends on the presence of transformational leadership. Incentives motivate employees extrinsically, while transformational leaders strengthen intrinsic motivation by inspiring a sense of purpose and commitment. This combination produces sustainable improvements in employee performance and organisational success. For the banking sector in Oman and similar contexts, integrating well-designed incentive systems with leadership development initiatives is not only a managerial practice but a strategic necessity for building high-performing, innovative, and future-ready organisations.

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