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Enhancing Small Medium Enterprises Performance through Human Resource Practices: A Proposed Framework

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Abstract: There is a growing body of literature that recognises the importance of human resource management practices (HRM practices) in enhancing the organizational performance. To date, little evidence examined the link between HRM practices and performance in small organization. This paper therefore focused on the human resource practices and small medium enterprises (SMEs) performance in Malaysian context. More importantly, it is vital to understand how human resource practices influence the performance. The nature of what is the best HRM practice are remains unclear. Based on previous research, this paper proposed four essential HRM practices such as selective hiring, training and development, compensation and empowerment as a key practices that foster the performance of small medium enterprises.

Keywords: SMEs performance; selective hiring; training and development; compensation; empowerment

I. INTRODUCTION

In today's dynamic business world, an organization must stay competitive to ensure the success of the organization. Hence, the success is derived from the performance of an organization. Therefore, performance plays a critical role and has become a key variable of interest for the researchers, academician and managers as it is the outcome that can contribute to the success of the organizations [1]. Past literature suggest that one resource which has been the key factor to the performance that is common to all organization is that of human resource [2]. Human resource is the most crucial asset in the organization. Moreover, performance of an organization depends largely on the individual performance of human resources and their performance as a whole. The key aim of human resource management (HRM) practices is to influence and change the ability of employees, to motivate them to achieve the strategic goal of the organizations [3]. Previous studies has shown that many researchers suggested various HRM practices that foster organizational performance [4], [5], [6], [7] in developed countries. However, very few studies has been done in the

context of developing countries, in other words in small organization [8]. It is believed that small organization are not formally implementing human resource practices due to lack of formal human resource policies and informal HR structures [9]. Regardless of the type of the organization, all firms need to use the HRM practice in managing their workforce. Arguably, despite the linkage of HRM as a critical factor in the success of both large and small businesses, most of the research have mainly focused on large firms, leaving a wide gap to be filled in terms of empirical research between HRM practices and performance of small firm [10], [11], [12]. However, it is not clear which HR practices to be considered as the best practice; whether individual practice or bundles of HRM due to some scholars used individual practice while others used bundles of practice. Yet despite the extensive research, the link between HRM and performance remains debatable and controversial [9], [13]. Therefore, in order to fill in this gap this study presents a set of HRM practices such as selective hiring, training and development, compensation and empowerment. Furthermore, this study verifies whether this set of HRM practices affects performance. Past literature shows that there were inconsistencies and mixed reporting [14], [13], some studies reported to be positive significant relationship [15], [2], while others proved the relationship to be insignificant findings [16].

II. RESEARCH OBJECTIVE

This study aimed to examine the relationship between HRM practices and SME performance. Hence, the research is guided by the following objectives:

- 1) To examine the relationship between selective hiring and SME performance;
- 2) To examine the relationship between training and development and SME performance;
- 3) To examine the relationship between compensation and SME performance;
- 4) To examine the relationship between empowerment and SME performance.

III. CONTRIBUTION OF THE STUDY

Managing human resources effectively is critical to the success of all organizations whether large or small. Previous studies suggest that the use of certain human resource practices will significantly increase the level of performance [17], [9], [18], [19], [2]. Therefore, this study is important in terms of identifying the best human resource practices that lead to performance of SMEs. Meanwhile, from theoretical perspective, this study may help to add to the performance literature by extending the body of knowledge on the best practices of human resource can lead to the organizational success. In fact, the findings will provide a better understanding for the human resource department on how to manage human resource effectively.

IV. LITERATURE REVIEW

(A) Organizational Performance

Organizational performance is the ultimate variable of interest for scholars in any area of management. Organizational performance is generally used as dependent variables in academic literature today. At the same time it remains as one of the most important construct that faced so much attention by different scholars. According to [20], the impact of HRM practices on organization performance depends on how HRM practices affect employees' skills and abilities, motivation and organizational structure.

Moreover, organizational performance has been the most important issue for every small or large companies. That is why academic researchers as well as practitioners gave much attention to discover the determinants of the organizational performance and what other machinery that can influence, positively or negatively, the organizational performance [21].

Therefore, the improvement of performance become more challenging task for the organizations when it relates to the practices of human resource management. Organizational performance and HRM have received much attention in the field of behavioural sciences indicating that there is a relationship between HRM practices and performance [15], [22], [23]. However, there is still lack of studies pertaining to the relationship between organizational performance and human resource management. In particular, HRM practices such as empowerment, extensive training and performance-contingent incentive compensation are widely believed to improve the performance of organizations [24]. The common thought of these studies is that human resource practices affect organizational performance. As far as this paper is concern, the study on organizational performance is refers to SMEs performance.

(B) Human Resource Management and SMEs performance

HRM has become one of the most popular topics within the management literature. There are several combination of HRM best practices that have been studied by several authors and yet still no consistency on which combination of practices or ‘HRM list’ has been adopted by SMEs or the organization. However, over the years there has been a change in the needs of human resource for the SMEs. Comparatively, not much research on HRM-performance link was performed in utilizing small medium enterprise as their samples [25].

Table 1
Summary of best HRM practices in SMEs performance

<i>HRM practices</i>	<i>Authors</i>
Staffing/Selection/Recruitment	[26], [27], [17], [2],[28], [19], [26]
Training and development	[26], [30], [27], [17], [2], [28], [31], [19], [25]
Performance appraisal/Performance Evaluation	[26],[27], [17], [2], [25]
Compensation/Reward	[26], [27], [17], [2], [28], [31], [19], [29], [25]
Information sharing	[2], [31]
Communication	[28]
Maintaining morale	[27]
Job description/Job assignment	[17], [28]
Job security	[31]

Based on previous literatures, the practices considered to be discussed in the relationship between SMEs performance are selective hiring, training and development, compensation and empowerment. The selected practices are ones that are commonly included in the extant literature.

V. HRM PRACTICES AND HYPOTHESIS DEVELOPMENT

(A) Selective Hiring

According to [16], selective hiring is one of the key practice that improves performance of the company. In most organization, selective hiring is the main activities of HRM. Selective hiring can be defined as the process of attracting potential applicant to the required positions as per offered by the organization [32]. Therefore, selecting the right employees is important for performance . In short, the right employees for the right job. Effective recruitment depends on how the organization select the right candidates for the right position.

An organization needs to be clear about what are the critical skills needed and must ensure the candidates are based on the specific job offered. There are several selection procedure to be considered when conducting a recruitment exercise. Several studies [20], [33] examined the effect of selective hiring on organizational performance has confirmed a positive and significant relationship. Hence, it could be hypothesized as:

H1a: *There is a positive relationship between selective hiring and organizational performance.*

(B) Training and Development

Training has been considered as one of the key practices in human resource management [34], [35], [36] and considered as the core of organizational practice. Training is also defined as “any attempt, within or outside the organization, to increase job related knowledge and skills of either employees or managers [37]. According to [38] training and development comprises of several activities such as implementation of staff training & development plans in order to ensure the staff have career opportunities in the organization. In other words, training refers to activities that teach employees how to perform better in their current job. According to [39], training and development of employees will benefit the organization which seek to gain competitive advantage through a highly skilled & flexible workforce. Similarly, [40] pointed out that training and development has become a necessity to the employees in sustaining and improving their work.

Furthermore, training programs may help employees to acquire the necessary knowledge and skills to work effectively for the organization. In contrast, lack of training has become major constraint among SMEs as it is believed to be the contributing factor to the failure of SMEs in Ghana [41]. The implication, therefore is important for the SMEs to understand the importance of training and development as it helps in the capacity of building which can be beneficial to the business survival. There is a lot of studies pertaining to training and organizational performance [6], [42], [43] in large organization, however, training related to small medium enterprise (SMEs) is still in its infancy [44] with little empirical evidence that support the association between training and the performance of SMEs [37].

In contrast, [44] in their study on the owner managers of SME in Mauritius found that the owner managers were aware of the benefits of the training as the important component for business survival. As a result, about 93 percent of the sampled firms which is from the full time employees was doing the training frequently. Several studies have found positive results on the relationship between training and development and organizational performance for instances, the study conducted by [45] and [39]. In a similar study, [46] has shown that an adequate training to employees is positively related to organizational performance. In the same vein, [47] found that training positively significant with organizational performance.

Similarly, as stated by [30] in a study among middle-sized companies in UK, proposed to consider the element of training and development as part of the organizational practice in order to enhance the organizational performance. In a similar case in Kisumu Municipality, whereby SMEs has been a subject of research to determine the relationship between HRM practices and SMEs performance and found out that recruitment and selection; training and development; and performance appraisal are significant determinants of the performance of the SMEs [48]. Therefore, to make sure employees perform their work effectively, it is mandatory for an organization to develop the training programs that could enhance the employee's knowledge. Hence, it could be hypothesized as:

H2b: *There is a positive relationship between training and development and organizational performance*

(C) Compensation

In a major review of the compensation literature, [49] highlighted that there is relatively strong support that individual incentives, merit pay and bonuses, and gainsharing can contribute to higher performance under the right circumstances. Compensation is described as employee's remuneration such as incentive or reward that has been given to employees for their work [50]. Compensation comprises of item of payment that includes both monetary and non- monetary. The objective of giving the compensation is to encourage employees to perform job effectively according to organization's goal. The goals of the compensation administration are to design a cost effective pay structure that will attract, motivate and retain competent employees. Thus, compensation administration aims to establish and maintain an equitable labor cost structure. Compensation administration includes two terms, namely wages and salaries [50].

Compensation is important to organization as it can retain the employee skill towards the organization [51]. A systematic compensation design could be implemented to the organization where the system that is fair internally and competitive externally. Critics have also argued that compensation is not for influencing and stimulating employee action that can lead to profit gains. In contrast, [24] argued that compensation should be given to the employees as incentive pay. As stated by [52], an effective compensation can influence key outcomes like performance and job satisfaction in organization in achieving and sustain a competitive advantage.

Numerous studies were conducted between compensation and organizational performance and found links and positive significant relationships. For instance, [53] has identified performance-based compensation as the single strongest predictor of firm performance. In a similar study, [16] found compensation policy correlated with the perceived sales, product quality, production cost and overall firm performance. In the same vein, [54] in their findings in a study of 200 Vietnamese SMEs showed that incentive compensation is the greatest practice related to performance followed by training and performance. Therefore, compensation is important and has become a major element for every organization to influence the employees. Hence, it could be hypothesized as:

H3c: *There is a positive relationship between compensation and organizational performance*

(D) Empowerment

Empowerment is one of the best practices and key concepts of human resources management [55]. In this era of globalization and competitive world, empowerment is seen as an important element in an

organizational practices which makes the employee always ready to execute in decision making to any changes in the organization [56]. Empowerment can be carried out from two perspective; the view from individual and organizational [57]. From individual perspective, empowerment is the perception of being empowered. While from the organizational point of view, empowerment consists of activities and practices of managers that delegate authority to the employees that can lead to contributions to the organization's success [55], [58].

Empowerment in organization involves less hierarchical and gives the employees more freedom in their jobs. There are relatively few studies on the relationship of empowerment and performance. For instance, [59] in the study on the effect of several human resource management practices has found that employee empowerment has increased the level of performance. In a similar study, [55] investigated activities of Polish small and medium-size enterprises (SMEs) and concluded that empowerment as a sources of competitive advantage in SMEs. Moreover, a study done in the UK manufacturing organizations also suggests the relationship between empowerment and firm performance [60]. Hence, it could be hypothesized as:

H3d. *There is a positive relationship between empowerment and organizational performance.*

VI. PROPOSED CONCEPTUAL FRAMEWORK

Based on the above theoretical and empirical discussion, a proposed framework illustrating the relationship between HRM practices and organizational performance is depicted in Figure 1 where HRM practices is an independent variables and organizational performance is a dependent variable. HRM practices is measured through selective hiring, training and development, compensation and empowerment.

While organizational performance could be measured by subjective measurement. Subjective measurement for organizational performance is considered due to its confidentiality and difficulty to obtain the data from the organizations. Thus, using a subjective measurement method to measure organizational performance has shown a correlation well with objective measure [61] and has certain degree of reliability and practical operability [62].

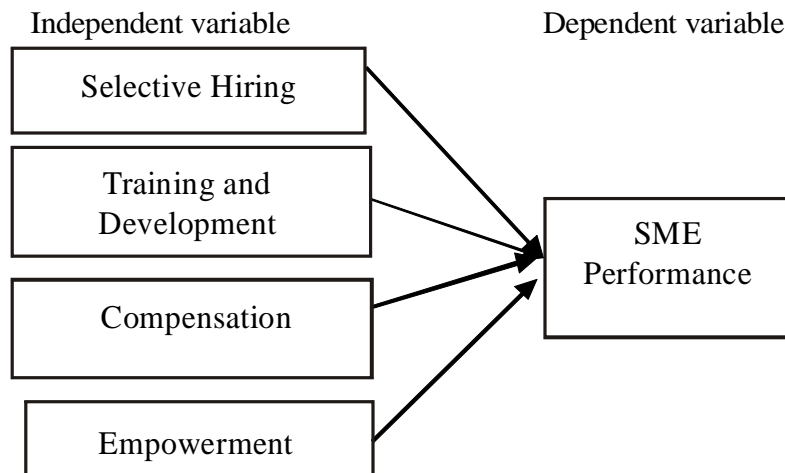


Figure 1: Proposed Conceptual Framework

VII. PROPOSED METHODOLOGY

This study uses a quantitative approach to investigate the relationship between HRM practices and SMEs performance. The primary data will be collected using a structured questionnaire which will be adopted from several scholars in the particular area. Unit analysis of this study will be represented by HR managers from the SME manufacturing industry. Population will be selected by using systematic sampling from the Federation of Manufacturing Malaysia directory. In determining of sample size, a sample size table of [63] will be used. Manufacturing industry is chosen because this sector is a key contribution to the Malaysia GDP, as an indicator of economic progress.

SmartPLS 3.0 will be used for the data analysis. PLS-SEM is a second generation analysis technique which came to overcome the shortcomings of the first generation statistical techniques like of Manova, Factor analysis, Analysis of variance and it also considered important in testing measured, latent variables and complex model [64].

VIII. CONCLUSION

Despite of abundance of research on HRM-performance linkage, there is still a lack of studies, especially the enhancement of performance of SMEs through HRM practices. To identify factors enhancing HRM practices, in this study, four essential HRM practices are recognized as a key practices as it is believed to effectively lead the performance of SMEs such as selective hiring, training and development, compensation and empowerment. Therefore, this research suggests that by understanding the importance of human resource practices in the organization, SMEs will continue to grow in their business successfully in global dynamic world. Based on the literature review, there is no doubt that the importance of SMEs as the backbone of economies [65], [66], development must continuously improve and implement appropriate HR practices that will allow them to stay in competitive world. Hence, this research suggests that organizations both big and small must continuously implement quality human resource management practices to enable them survive and stay strong and competitive. It is hope that if the proposed framework empirically validated, the findings of this study could be utilised to provide important insight to the policy makers, academicians and practitioners as well as organizations to look into the significant direct effect of HRM practices on organizational performance. In conclusion, Malaysian SMEs should figure out, value and adopt the best practices of human resource management to enhance the capabilities and skills development in order to increase their business.

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