

Human Resource Practices and Enterprise Performance in Small and Medium Enterprises of
Pakistan

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Abstract

Human resource management (HRM) is a new concept for Pakistani Small and medium enterprises; there are few studies on HRM practices and its impact on enterprise performance in Pakistani small and medium sized enterprises (SMEs). The investigation of the relationship between human resources management and the company performance has mostly been carried out in big companies only. The question we have raised is whether the development of an intensive HRM is profitable for small and medium enterprises or not. This paper attempts to provide a pilot study of examining the status quo of HRM practice in Pakistani small and medium enterprises, and searching for possible relationship between HRM and enterprise performance. The results of the study are based on analysis data that has been collected through questionnaires that were responded by the managers of 150 small and medium enterprises of Pakistan, the analysis of in-depth interviews with seven owners of SMEs in various cities in Pakistan and two focus groups. The paper concludes with four hybrids of feasible interrelationships between HRM practice and enterprise performance within Pakistani small and medium enterprises. The results of our investigations show that HRM intensity has a strong positive effect upon the productivity, the innovation capacity and the profitability of small and medium enterprises.

Key words: Human resource management, Small and medium enterprises, human resource practices.

Introduction

Small businesses of Pakistan have experienced tremendous growth in recent years. To benefit from growing market, small businesses require right people for the right Job to minimize cost. To attract, retain and add value innovative in the business Human Resource Management practices are required to be implemented. Thus, One of a source of competitive advantage for any business is its human resources. When it comes to developing nations like Pakistan the role of human resources is visible only in those organizations which are either knowledge organizations or are technology intensive organizations. In developing economies like ours, implementation of Human Resource practices in SMEs are a recent phenomenon.

Few things are relatively understood concerning the needs and practices of small companies related to HR. In particular, the impact of human resources practices upon the small companies has not been studied so much. Since, it was noticed that for big companies the HRM impact upon the performance is a positive one a much higher number of authors have underlined the need for similar researches for SME.

To run a successful organization the main challenge is to identify, retain, and trigger the adequate employees. This challenge is valid for all organizations regardless of their size. HRM concept involves treatment of the employees as resources. As resource type “the human capital” means the organization’s employees introduced in terms of training, intelligence, relationships, and empathy characteristics that can add economic value to the organization. This approach supports the idea that the employees of the SMEs are not interchangeable parts, but the very source of the success or failure of a company.

The company size is strictly related to the implementation of HR instruments. In general, the small companies are less susceptible to appeal to HRM. This statement does not relate only to the level of individual HRM instruments, but also to the level of the configuration of these

instruments. Small companies usually have a more modest score concerning the HRM formalization. However, it is guessed that HRM will also matter in small companies, although their possibilities and practices in the field are different from those of the big companies and even their mentality of becoming aware and measuring the HRM effects upon performance, innovation, increases.

There are many issues in Pakistani SMEs that need to be addressed, however, this paper just concentrates on human resources management practice in SME sector, discussing the interrelationship between HRM practice and enterprise performance that has not been studied before in Pakistan. A pilot study based on analysis of in-depth interviews with 5 SMEs in various cities in Pakistan attempts to examine the status quo of HRM practice in Pakistani small and medium enterprises, and searching for possible relationship between HRM practices and SMEs performance.

To further strengthen the research findings a questioner has also been floated among 150 managers of small and medium enterprises. The variables in the questioner have been taken on the basis of available literature in the relevant field.

Literature Review

To respond to the need of the customers of the business and to move forward in their business, SMEs should utilize their employees' special skills as they are viewed as an important source of competitive advantage. Succeeding to attract, retain and motivate a skilled workforce companies have to effectively manage their different HR activities such as recruiting, selecting, hiring, training, employee development, communication, and rewarding personnel. A highly committed and competent workforce helps companies in succeeding these strategies.

There is a considerable debate in the literature related to whether the HRM and related HR strategies is an *outcome* or a *process*. For some academics such as Snell et al. (1996) the HRM is an “outcome” where they view the HRM as an organizational systems designed to achieve sustainable competitive advantage through people. While for others, it is a process of linking HR practices to business strategy (Ulrich, 1997). HRM is the process by which organizations seek to link the human, social, and intellectual capital of their members to the strategic needs of the firm (Bamberger & Meshoulam, 2000). Many researchers (Arthur, 1994; Huselid, 1995) have suggested that company’s HRM practices contribute to increase its performance. Traditionally, human resources have been viewed as a cost to be minimized and subject to be downsized in order to reduce these costs, rather than a source of value creation and a strategic lever that can have economically significant effects on the firm’s performance (Becker & Huselid, 1998). There is a close connection between human resources management and firm strategy, which in turn refers to the business environment and organizational development (Becker & Gerhart, 1996). It is widely accepted that a company's human resource management (HRM) practices should be matching to the strategy of the whole company. HRM implies that if people are considered and managed as valuable strategic resources, the firm can achieve a competitive advantage and as a consequence demonstrate superior performance (Pfeffer, 1994). This means that the management of human resources should be corresponding to the firm strategy, as the goals and prerequisites of each of the strategy profiles are different (Armstrong & Baron, 2002).

Companies should consider people as assets rather than costs and that they are valuable and constitute a source of competitive advantage (Legge, 1989). People and their collective skills, abilities and experience, coupled with their ability to deploy these in the interests of the

employing organization, are now recognized as making a significant contribution to organizational success and as constituting a significant source of competitive advantage (Armstrong & Baron, 2002). Business objectives are accomplished when human resource practices, procedures and systems are developed and implemented based on organizational needs, that is, when a strategic perspective to human resource management is adopted (Baird & Meshoulam, 1988).

HR develops knowledge and skills of employees, and therefore, contributes to productivity improvements in firms (Becker & Gerhart, 1996). Employees can obtain company-specific knowledge in training (Huselid, 1995). In addition, training improves specialization of employees in their occupation, and therefore, increases employee involvement with managerial decisions (Bratton & Gold, 2007).

Batt (2002) examined the relationship between human resource practices, employee quit rates, and organizational performance in the service sector. His findings confirm that, firms emphasizing high skills, employee participation in decision making and in teams, and human resource incentives such as high relative pay and employment security, have lower quit rates and higher performance.

More recently, Wattanasupachoke (2009) had explored the relationship between HR strategies and the performance of 124 Thai companies and found that the extra pay and profit sharing is the only factor group that has a statistically important correlation with the companies' financial performances such as sales, profits and liquidities.

As a result of the above, an extensive body of literature about the impact of HR practices on firm performance had emerged as a dominant research issue in the HRM field. The results of these studies confirm the dependency of firm success on the caliber of its employees and how

effectively they are managed. Performance evaluation allows company to align compensation with performance of employees. Therefore, performance-base payment connects efforts and work to organization's operational goals. Thus, pay for performance reduces absenteeism (Harel & Tzafrir, 1999).

The existent researches focus upon the managers' perception on the importance and/or the success of HR practices. However, translating the theory into practice can cause many problems. Many authors have studied the connection between HRM and performance empirically.

Theoretical framework

In this study the variables have been selected on the basis of prior studies and books and the relationship has been developed to find the relationship on the basis of qualitative analysis. The relationship shows that the driving force is human resource practices and it affect employee outcomes and ultimately it affects the firm's performance. This phenomenon has been divided into hypothesis and hypothesis has been checked through interviews, focus group, questioner.

Figure 2

Sequential Effects of HR Practices on Enterprise Performance



The figure two represents the sequential affect of human resource practices on the enterprise performance.

Objectives of the Study

The research study titled “Human Resource Practices and Enterprise Performance in Small and Medium Enterprises of Pakistan”

1. To find the importance of human resource practices on organizational performance.
2. To find the impact of hiring criteria on organizational performance.
3. To find the impact of training on organizational performance.
4. To find the impact of employee participation in decision making on organizational performance.
5. To find the impact of performance appraisal on organizational performance.
6. To find the impact of performance base compensation on organizational performance.

Qualitative Data Collection and Analysis

The authors interviewed 2 general managers (GM) for HRM issues. 3 interviews were carried out from the owners of SMEs. The interview questions cover the following aspects:

- HRM practice and performance in SMEs in Pakistan,
- SME ownership,
- SMEs years of establishment,
- Corporate performance including sales/production since firms’ establishment, market position and future five years’ plan,
- Problems and favorable factors encountered in their developmental process.

Most of enterprises were randomly introduced by the author’s friends and their circle of influence. However, the samples selected were mostly small and medium sized private owned enterprises. These enterprises demonstrate relatively competitive market position and growth

tendency. It is observed that HRM and corporate performance of enterprises is not much influenced by ownership, which has to manage the human resource.

Summary of Key Findings

Most of the contacts did not feel comfortable talking about HR practices, as they were not sure what if any HR practices their company used. We found that most of the companies did use HR practices, but the HR practice label was not how they would describe the practices that they had in place. We found that the contacts were more comfortable when we described these practices as how they managed their people. The data from the interviews suggested that managers and owners of small companies are aware of and can identify the employee outcomes that affect the ability of their company to compete and succeed in their marketplace. Participants suggested that they attempt to use management practices to shape and affect these employee outcomes. The interviews support the notion that the extent to which the company has done a good job of choosing the employee management practices that are appropriate for their organization. In turn, these employee outcomes are likely to have strong, positive effects on the performance of the company.

Quantitative Data Collection and Methodology

For quantitative analysis survey research was conducted survey research. The data has been collected through self administered questionnaire. Questionnaire was adopted as survey instrument because the study was of explanatory nature and the respondents were better able to identify the factors of human resource practices which could influence the performance of SMEs in Pakistan. Moreover, the respondent would be more comfortable with questionnaire rather than interview because they could fill questionnaire according to their own convenience and availability of time. 200 questionnaires were distributed for collecting the data and 150 were returned by the respondents. The response rate was very good. The data was then entered into SPSS for analysis. Simple linear regression was run to find the significance of variables on the bases of responses of managers of small and medium enterprises. The variables that were taken in the questionnaires were chosen on the basis of prior studies that have been reviewed in literature.

Results

Regression

Model	r	r square	Adjusted r square	Std. Error of the Estimate	Durbin-Watson
1	0.866 ^a	0.7396	0.7313	0.406	1.966

In the model mentioned above regression and correlation analysis has been calculated between the dependent and independent variables. The value of r is 0.866 which shows that there is 86.6% correlation between the dependent and independent variables. This shows that with 100 percent change in the independent variables will result 86.6% change in the dependent variable.

The value of r square is .7396 or it can be said that the value of r square is 73.96 %. The value of r square is explained variation. The value shows that 73.96 % change is explained by the mentioned independent variables. Thus, it can also be said that more than 73.96% variation in enterprise performance of SMEs is explained by its linear relationship with the independent variables. The value of Durbin Watson is 1.966 which is above 1.75 if the value of Durbin Watson is above 1.75 to 2.25 then it shows that there is no autocorrelation between the independent variables.

ANOVA^b

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	68.462	16	4.283	25.96	.000 ^a
	Residual	10.561	64	.175		
	Total	78.943	80			

In the above mentioned ANOVA table the value of F is 23.573 which is more than 5 which shows that the overall fitness of the model is good. The value of F test and then level of significance 0.00 at 10 % level of significance and hence H_0 is rejected and model is over all good fit.

Coefficients

Model		Un-standardized Coefficients		Standardized Coefficients	t	Sig.
		β	Std. Error	Beta		
1	(Constant)	.398	.973		.297	.768

Human resource practices	.237	.053	.128	2.405	.019
Hiring criteria	.355	.062	.165	2.654	.010
Employee training	-.695	.041	-.114	-2.098	.040
Employee participation in decision making	.275	.071	.241	3.641	.001
Performance appraisal	.219	.065	.218	3.369	.001
Performance based compensation	-.351	.073	-.207	-3.315	.002

a. Dependent Variable: Enterprise performance

The linear regression equation that has been drawn on the basis of data collected through questionnaires is as follows.

$$Y = \beta_0 + \beta X + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5$$

The model variables are listed below along with their names.

- X Human resource practices
- X₁ Hiring criteria
- X₂ Employee training
- X₃ Employee participation in decision making
- X₄ Performance appraisal
- X₅ Performance based compensation

The equation has been drawn on the basis of t values. All variables were regressed to the level of significance to find their influence on the performance of SMEs. It was found that all variables have significant effect on the growth of SMEs in Pakistan as they have high t-ratios and near to zero p values. Human resource practices, hiring criteria, employee training, employee participation in decision making, performance appraisal and performance based compensation

have significant effect on the performance of SMEs of Pakistan. All these statistical significant variables have positive impact on performance of SMEs in Pakistan. Thus, all the variables have positive impact on the performance of SMEs showing a positive relation with the dependent variable.

Conclusion and Recommendations

Overall the results of this study show that most of the respondent small and medium enterprises in Pakistan are now practicing at least some elements of human resource practices within their firms. However, the focus on employment training is still rather weak in the small and medium enterprises of Pakistan. There is also room for improvement in the areas of performance appraisal, especially in terms of institutionalization of performance evaluation process. Performance evaluation should be based; on skilling, training, and education rather than on general manager's personal opinions and relationship with subordinates or on the basis of length of the services. In this study six variables were tested and all the variables tested have shown a significant relationship according to the interviewed employees of small and medium enterprises, on the basis of focus group discussion and questioners. The interviews and the analysis of the interviews showed effective human resource planning is positively associated with organizational performance; it further suggests that good selectivity in the hiring process is positively associated with organizational performance which is a part of human resource practices. The analysis also reveals that the greater participation of employees in decision making is positively associated with performance.

Examination of small and medium enterprise performance indicates that Pakistani small and medium enterprises that were interviewed are growth-oriented, having relatively market advantages and will be continuously expanding. Nonetheless, it is difficult to conclude that the

performance is necessarily the direct result of human resource practices. It is interesting to find that human resource practices in the studied companies have a direct causal relationship to performance obtained by asking the different top management about their perception. This can be seen as a significant finding in human resource practices research, especially in the Pakistani context where, at my knowledge no past research had been conducted. This finding is in conformity with previous studies (Pfeffer, 1994; Huselid, 1995). It follows that these companies should continue in enhancing more the competence of its employees to attain better performance goals.

In spite of the expected good results obtained from mixed methodology, the limitation of this study can be theoretical. Theoretically, although in many studies the company strategy appeared to influence the choice of human resource strategy, the resource-based view suggests that companies will choose the appropriate business strategies according to the available human resource pools. Therefore, the relationship between business and human resource practices is dynamic and need to be reviewed constantly.

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