HUMAN RESOURCE MANAGEMENT PRACTICES AND THEIR IMPACTS ON THE PERCEIVED PERFORMANCE OF SME’S OPERATING IN KARACHI

Muhammad Usman Aleem ¹ and Mustaghis Ur Rahman ²

Abstract

SMEs provide a base to Pakistan’s economy. Besides, they are the largest job creator in the country. However, SMEs are facing challenges in its operations and development with reference to human resource effectiveness. Therefore, the present research explores the HR practices impact on SMEs Perceived Performance in Karachi, as SMEs too require HR practices to stay alive and uphold a competitive edge in order to get better firm performance. The sample size of this quantitative study is 443 SMEs’ owners and senior managers from manufacturing and service registered firms at four industrial associations. The data analysis was done by using SPSS for Multiple Linear Regression analysis. The findings of this study show the HR practices impact over SMEs perceived performance. This research work identifies key implications for owners or managers of SME’s, in the enhancement of their firms’ performance.

Keywords: Perceived Performance, Challenges, HR Practices, Human Resource Management

JEL Classification: M 590

Introduction

In last few years, SMEs (Small and Medium enterprises) have been accepted by the policy makers as well as researchers and recognized as single growth engine for accomplishing economic development by creating jobs as well as speeding up the economic activity in numerous countries by providing 90% employment on average. Some of the countries, for example, 99% in Europe, (Rauch, Frese, & Sonnentag, 2000), 99% in China, (Cunningham & Rowley, 2008), 99.7 % in America, (Hemen, Tansky, & Camp, 2000) and 99% in Pakistan (Bhatti, Syed, Shah & Shaikh, 2012) of all business are SMEs.

¹ Assistant Professor, Head of Academics Evening Program (North Campus), College of Management Sciences, PAF-KIET, Karachi, Pakistan. Email: musmanaleem@live.com
² Professor & Head of Management Science Department, Bahria University, Karachi Campus. Email: hodms.bukc@bahria.edu.pk
Even in developed countries, SMEs are considered as the largest firms giving employment to workforce (Lai, Saridkis & Johnstone, 2016).

The global setting of industry is diverging with the demands of liberalization from financial catastrophes. On the bright side, these catastrophes straighten out new prospects and opportunities for Pakistani SMEs. 90% workforce is working in SMEs in Pakistan which provide them with authority to act upon a significant responsibility in developing economy of Pakistan, under the flag of NEM (new economic model). In this regard, the government initiatives through SMEDA help innovation and development in varied areas of production and services by the SMEs. SMEs are considered as well proficient, organized as well as productive originators of employment (Rahman, 2010; Lai, Saridkis & Johnstone, 2016). HRM practices play an important role that impacts enterprise performance (Pfeffer, 2005). The theory of RBV (resource based view) which carries thought to facilitate resources that cannot be easily imitable (Liu, 2016).

Discussed in the above backdrop, the research explores the HR practices and its impact on perceived performance of SMEs operating in Karachi, in order to support and assist systems that are present for formally running the existing and establishing new SMEs in Karachi, Pakistan.

The article consists of six parts. Part one begins with the introduction to study whereas part two describes the problem statement, research questions and study objectives. The third part explains literature review on the subject followed by the fourth section which explains the methodology of the research applied. The fifth section explains the analysis of data with outcome as results and findings and lastly the sixth section encompasses critical discussion and conclusion.

**Problem Statement, Research Question and Objectives**

The economic unsteadiness of recent decades among nearly all areas compel the enterprises to move around reformation of human resource in the enterprise. It’s a general faith together in industry and in academic circles, that human resource in an enterprise is the basis for competitive edge and given that HR practices are guidance incorporated with strategic plan and enterprise culture and customs (Drost, Frayne, Lowe & Geringer, 2002). Apart from proving itself as an advantage for small and medium sized organizations, the HRM role currently is to distinguish an enterprise from its opponents (Zakaria, Zainal & Nasurdin, 2011). Moncarz, Zhao and Kay (2009) found that practices of HRM were not found in small sized enterprises while investigation delves into large SMEs.

If researched knowledge is not generated on the issues related to the HR applicable to SMEs, there is a possibility that SME’s management would not be informed of the affects of the knowledge gaps in the field. Consequently, small and medium sized organizations would not be practicing relevant HR policies and systems which will have insignificant impact on employees’ performance leading to organizational performances. This state of affairs will ultimately affect not only the SMEs’
performance but will also have detrimental reflection on Pakistan’s economy. Therefore, in order to fill up the gap in existing area of HR practices in SMEs. Though SMEs are important to Pakistan economy, it is vital to find the answers to the question: What is the impact of HR practices on SMEs perceived performance operating in Karachi? The answer to this question sought with an objective to find impacts of HR practices on SMEs perceived performance and at the same time learn and understand the relationship between HRM practices (hiring, training, performance appraisal and compensation) and the perceived SMEs performance.

**Literature Review**

The accomplishment of SMEs’ purpose depends upon the organizational performance (Katou, 2012). The firm performance can be evaluated in different ways. For example, the firm performance can be evaluated by the satisfaction of workers as well as by firm’ productivity. It can also be evaluated through non-financial variables like share of market, image of the firm and the products quality (Revenio, 2016).

The HRM is crucial for the success of a firm as the workers have some definite qualities which make them valuable. When we talk in terms of company strategy, a firm is able to succeed only if it is able to maintain and uphold the competition through competitive edge. Therefore, it can be said that firms need not just some kind of workforce, rather the type of force which can provide competitive edge and business advantage. The workforce or employees are, therefore, considered important for organization’s success and growth (Nongmaithem & Kassa, 2016). According to Boselie, Paauwe and Jansen (2001), firms with good and superior human resource management practices are likely to have dedicated, committed and loyal staffs or human resources. They further added that these people are motivated and are willing to provide extra time and effort in order to attain and achieve the firm’s goals.

Khan and Khan (2012) study revealed that an enterprises environment is dynamic, however attaining superior as well as better performance can only be done through applying effective HR practices. Whereas, human resource are considered as the source that provides competitive edge (Ibrahim & Zulkafli, 2016). This means for organization to stay alive in today's global environment, one should manage HR properly.

However, the accomplishment of SME’s purposes depend upon the degree of the enterprise performance. (Katou 2012). Pfeffer (1994) is of the opinion that an enterprise with good quality as well as effective HRM develops faithful, dedicated employees, for attaining enterprise aims. According to Zakaria et al. (2011), HR practices; training and compensation, particularly, affect SME’s performance considerably. Under this study resource based theory is discussed to see the association of HRM with organization’s performance. According to resource-base-theory, workforce also known as human resource is spotted as strategic firms’ resource due to which they result in far above the
ground performance of the firm. Human resource is strategic asset which is difficult to imitate and it is a one of its kind among the factors of production. This provides a firm with competitive edge (Ping-ping, 2016).

The model was adapted from Paul and Anantharaman (2003) study conducted on Indian software companies. The authors found association of operations with non-monetary and monetary performance of the organization. The undertaken study modified the mentioned conceptual model (mention which model give citation and references) as per the research objectives and has taken hiring, training, performance appraisal and compensation as HR practices. Further the model was modified as per the need of the SMEs’ performance.

![Conceptual Framework]

Figure 1: Conceptual Framework

Hypotheses

In the given background, four hypotheses were formulated using four variables to find the responses and answers of the research questions.

Nowadays the competition in modern era is at its peak, as a good number of SMEs develop their practices of HRM in a way that their employees productivity and organizational performance enhances. As effective hiring leads to job satisfaction (Jamsari, Nik, & Santhi, 2017). Gamage (2014) and Caliskan (2010) were of the opinion that those organizations which are involved in HR practices, are having a competitive advantage and edge over their competitors. With regards to the above discussion, the first hypothesis was formulated as:

H1: Hiring impacts SMEs nonfinancial performance significantly and positively.
Learning or training and development is a very important and vital element for developing workers knowledge or skills and intellectual capabilities for improving the performance of the firm (Jauhar, Abdul Ghani, Joader, Subhan, & Islam, 2015). A research on satisfaction was carried out by Saks (1995). The study result revealed that employees who were involved in this program have increased level of satisfaction, which had a positive effect on organizational performance. Employees’ training is another very important requirement for the performance of the organizations to have a competitive edge (Sajjad, 2016). With regards to the above discussion, the second hypothesis was formulated as:

\[ H2: \text{Training impacts SMEs nonfinancial performance significantly and positively.} \]

Therefore, a fair appraisal helps in extracting the best from the workers. An unfair appraisal system can result in unrest and dissatisfaction amongst employees (Sajjad, 2016). In a study conducted by Halachmi (2005), revealed that performance evaluation is essential practice for evaluating from appraiser’s or appraises point of view. It is given in a specified time slot and results are with the organization, which in turn satisfy the employees. Another research work carried out by Teclemichael and Soeters (2006), revealed that performance evaluation has a positive and significant relationship with perceived employee performance. With regards to the above literature discussed, the third hypothesis was formulated as:

\[ H3: \text{Performance appraisal impacts SMEs nonfinancial performance significantly and positively.} \]

The compensation is a kind of a method for providing financial benefits to workers in return of their job or work which they had performed. It can also be used for hiring skilled workers or employees, for giving them rewards for their performance, as well as support and push the firm’s loyalty through reduction in turnover (Hassan, 2016). A study was conducted by Singh (2004) on Indian firms performance with respect to compensation and its processes and how they are influencing. He found that the performance of organizations got improved. While in another study conducted by Teclemichael and Soeters (2006), it was found that firms got profitable when they paid attention to pay, than those which didn’t pay attention to pay. They found a positive relationship. With regards to the above discussion, the fourth hypothesis was formulated as:

\[ H4: \text{Compensation impacts SMEs nonfinancial performance significantly and positively.} \]

**Methodology**

This is an empirical research which is deductive in nature and the data and information has been gathered by applying survey method via five point Likert scale. The targeted population of SME’s was 1328 that have been known from the total population of 2016 registered firms from the four associations from Karachi’s five industrial zones. "The study sample size was 443 and was considered appropriate as per 20:1 subjects-to-variable (STV) ratio (Anderson, Tatham and Black (1995) in Hogarty, Hines, Kromrey, Ferron & Mumford, 2005)". 
The sampling type is random as the sampling frame was provided by the four industrial associatisns. The data gathered via a questionnaire was done and it was derived from studying the literature. The Questionnaire has been adapted from the earlier studies and researches. The questionnaire contains three parts: demographics, HRM practices and SME’s performance. It consists of four independent variables, hiring having 6 constructs, while training having 4 constructs, performance evaluation having 5 constructs and compensation having 4 constructs, where as dependent variable SME’s perceived performance have 5 constructs.

Results and Findings

Preceding towards testing of four formulated hypotheses, the reliability of the variables were determined and the derived hypotheses were tested through multiple linear regression.

The Constructs Reliability

For this study, the reliability was measured for overall constructs and for each construct as well. According to Nunnally (1978) and Nunnally and Bernstein (1994), they advise reliabilities of 0.70. The reliability measured or this study was 0.768 as shown in Table 1, for all constructs and for each construct i.e. for hiring its 0.762, for training its 0.744, for performance appraisal its 0.811, for compensation its 0.721 and for non-financial performance it’s 0.799, as shown in Table 2, which was an excellent confirmation of dependable tool.

Table 1

<table>
<thead>
<tr>
<th>Variables Reliability Statistics</th>
<th>No. of Items</th>
<th>Cronbach's Alpha</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hiring</td>
<td>6</td>
<td>0.762</td>
</tr>
<tr>
<td>Training</td>
<td>4</td>
<td>0.744</td>
</tr>
<tr>
<td>Performance</td>
<td>5</td>
<td>0.811</td>
</tr>
<tr>
<td>Compensation</td>
<td>4</td>
<td>0.721</td>
</tr>
<tr>
<td>Non Financial Performance</td>
<td>5</td>
<td>0.799</td>
</tr>
</tbody>
</table>

Confirmatory Factor Analysis (CFA) Results

Confirmatory factor analysis (CFA) is used for the purposes of measuring items and constructs. CFA is considered to be a legitimate schema associated with hypothesis testing approach to the conceptual validation of data (Brown, 2014). To simply put it, a model is created and then tested for its validity with the help of data sample. The factorial structure validity testing entails analyzing validity of the extent of items designed to measure a particular variable or a latent factor. Factors are
considered and represented in terms of their subscales in a measuring instrument and all items of a subscale are loaded to factor related to them (Byrne, 2016). The measuring instrument undertaken for CFA analysis contains 19 items in total. The subscale of hiring has 6 items, subscale training contains 4 items, subscale performance appraisal has 5 items and compensation subscale is composed of 4 items.

The hypothesized model is depicted in Figure 1. The model is hypothesized a priori that Best HR Practices contain four factor factors viz. Hiring, Training, Performance Appraisal and Compensation and each of their respective items has a non-zero loading on the factor and simultaneously these items have zero loadings on other factors of the construct under discussion. Moreover, the four factors are correlated and the error terms associated with these 19 items are uncorrelated.

Figure 1: Hypothesized model for CFA factorial validity analysis

With the above a priori hypothesized model CFA analysis was run in AMOS version 23 with a plugin “Master Validity Tool” developed for construct validity testing by Gaskin and Lim (2016).
The plugin adopted the seminal study’s threshold values (Hu & Bentler, 1999) for testing the construct validity, viz. convergent validity and Discriminant validity. The plugin produced the following table highlighting the result as no validity concerns were found in the model. However, the respective values for CR, AVE, MSV and MaxR(H) are presented in the table. MaxR(H) is another term for CR with inherent calculations for improved CR (McDonald, 1981). All of values CR is greater than AVE and MSV is less than AVE. The square-root of AVE is presented in the diagonal and in bold letters. The inter-construct correlation is also presented in the table below. There were no construct validity departures from the standardized threshold values were found.

Table-2
CFA Results

<table>
<thead>
<tr>
<th></th>
<th>CR</th>
<th>AVE</th>
<th>MSV</th>
<th>MaxR(H)</th>
<th>Hiring</th>
<th>Training</th>
<th>Performance Appraisal</th>
<th>Compensation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hiring</td>
<td>0.763</td>
<td>.582</td>
<td>0.129</td>
<td>0.772</td>
<td>.762</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Training</td>
<td>0.749</td>
<td>.561</td>
<td>0.497</td>
<td>0.753</td>
<td>0.446</td>
<td>.748</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Performance Appraisal</td>
<td>0.823</td>
<td>.677</td>
<td>0.483</td>
<td>0.834</td>
<td>0.426</td>
<td>0.557</td>
<td>.822</td>
<td></td>
</tr>
<tr>
<td>Compensation</td>
<td>0.761</td>
<td>.579</td>
<td>0.115</td>
<td>0.769</td>
<td>0.364</td>
<td>0.485</td>
<td>0.508</td>
<td>.760</td>
</tr>
</tbody>
</table>

Hypothesis Testing

According to Saunders et al. (2011) arithmetical manners take part in an essential function in data collection. Multiple Linear Regression were used for testing the four hypotheses.

Hypothesis Testing For SME’s Non-Financial Performance

The hypotheses one, three, five and seven were analyzed using Multiple linear regression to find the impact of hiring, training, performance appraisal and compensation with SMEs nonfinancial performance significantly and positively.

To discover the most excellent linear combination of HRM practices (i.e., hiring, training, performance appraisal and compensation) for predicting non-financial performance of SME’s test scores, Multiple regression was applied. The means, standard deviations and Intercorrelations can be established in Table 1. This combination of variables broadly predicted non-financial performance of SME’s, F(4,412) = 64.893, p<.005, with all four variables significantly adding to the prediction. The beta weights, presented in Table 1.1, propose that superior HRM practices provide a matchless numeral toward predicting non-financial performance of SME’s. The adjusted R squared value was 0.387. This explains that 38.7% of the variation in non-financial performance of SME’s was explained through the model. As stated by Cohen (1988 pp. 21-23), it is a huge effect. In other words, the
findings of regression showed positive association, moreover hiring, training, performance appraisal and compensation does impact non-financial performance of SMEs.

Table 3.0.
Means, Standard Deviations and Intercorrelations Non-Financial Performance of SME’s and Predictor Variables

<table>
<thead>
<tr>
<th>Variables</th>
<th>M</th>
<th>SD</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-financial performance of SME</td>
<td>3.8412</td>
<td>.53370</td>
<td>.423**</td>
<td>.413**</td>
<td>.467**</td>
<td>.287**</td>
</tr>
<tr>
<td>Predictor variable</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Hiring</td>
<td>3.89</td>
<td>0.816</td>
<td>-</td>
<td>.446</td>
<td>.426</td>
<td>.364</td>
</tr>
<tr>
<td>2. Training</td>
<td>3.82</td>
<td>0.790</td>
<td>.446</td>
<td>-</td>
<td>.557</td>
<td>.485</td>
</tr>
<tr>
<td>3. Performance Appraisal</td>
<td>3.80</td>
<td>0.815</td>
<td>.426</td>
<td>.557</td>
<td>-</td>
<td>.508</td>
</tr>
<tr>
<td>4. Compensation</td>
<td>3.69</td>
<td>0.928</td>
<td>.364</td>
<td>.485</td>
<td>.508</td>
<td>-</td>
</tr>
</tbody>
</table>

*p<.05, **p<0.01

Table 3.1.
Simultaneous Multiple Regression Analysis Summary

<table>
<thead>
<tr>
<th>Variables</th>
<th>B</th>
<th>SEB</th>
<th>Beta</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hiring</td>
<td>0.211</td>
<td>0.042</td>
<td>0.225</td>
</tr>
<tr>
<td>Training</td>
<td>0.178</td>
<td>0.043</td>
<td>0.207</td>
</tr>
<tr>
<td>Performance Appraisal</td>
<td>0.206</td>
<td>0.044</td>
<td>0.236</td>
</tr>
<tr>
<td>Compensation</td>
<td>0.093</td>
<td>0.034</td>
<td>0.130</td>
</tr>
<tr>
<td>Constant</td>
<td>1.263</td>
<td>0.167</td>
<td></td>
</tr>
</tbody>
</table>

Multiple Regression Equation for Non-Monetary/Non-Financial Performance of SME’s

\[ Y = C + \beta X_1 + \beta X_2 + \beta X_3 + \ldots + \beta X_n \]

\[ Y = \text{Dependent Variable: Non-Monetary/Non-Financial Performance.} \]
\[ C = \text{Constant value.} \]
\[ \beta = \text{Unstandardized coefficient.} \]
\[ X = \text{Measurement of predictor variable (hiring=X_1, training=X_2, performance assessment=X_3 and recompense=X_4).} \]

The above chart/table, derived following equation:

\[ Y = 1.263 + (0.211X_1) + 0.178X_2 + 0.206X_3 + 0.093X_4 \]

The above equation model can be inferred as increase of single units of hiring (X_1 = 0.211) will add 0.211 units of non-monetary performance (Y), for training (X_2 = 0.178), for performance appraisal (X_3 = 0.206) and for compensation (X_4 = 0.093), increase of every one unit will raise (0.211, 0.178,
0.206, 0.093) units of dependent variable i.e. non-monetary/non-financial performance.

Conclusion

The study’s significance is that it is the first type of research taking place on SME’s with respect to size, sector and type in Karachi. The present research considerably tested the influence of HR practices on SME’s perceived performance with respect to listed SME’s working within Karachi. Still, the study start on as of fundamental perceptions applicable to the research for instance kinds and importance of SME’s and HRM. The present study checked the practices of HRM namely training, hiring, compensation plus performance evaluation and its influence over SME’s perceived performance.

A positive and strong relationship is found among the HR practices and SME’s perceived performance. The result also reveals that training and performance appraisal got positive plus most noteworthy association among performance of SMEs.

The outcomes are aligned through earlier studies findings and supports the studies conducted by many researchers like (e.g., Jamsari et al., 2017; Nongmaith et al., 2016; Ugheoke, Isa, & Noor, 2015; Amin et al. 2014; Zhai, Liu & Fellows, 2013; Zakaria et al. 2011; Khan & Khan, 2012; Paul & Anantharam, 2003; Delaney & Huselid, 1996). They were of the opinion that when employees get a fair performance feedback and organizations invest in training, both result in better and increased organizational performance. The drawbacks ought to be kept in mind that only registered SMEs were aimed for this study.

Recommendations

1. HRM in SME’s should offer some incentive such as training, compensation, recognition, freedom, appreciations, promotion and job security in order to motivate and satisfy the employees for improving organizational performance.
2. The HR managers or owners should meet quarterly with each departmental heads to praise, recognize and appreciate workers for their good performance or target achievement. This will keep them motivated. While specific achievements by workers should be discussed and their names should be displayed on the departmental walls.
3. SMEDA and policy makers as well as stakeholders should ensure that SME’s HR should build up a successful enterprise by regularly planning along with evaluating their recompense as well as system of assessment performance.
References


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Hypothesized model for CFA factorial validity analysis

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Simultaneous Multiple Regression Analysis Summary

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Gaskination’s StatWiki

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