

## **Impact of HRM on Organizational Performance of SME Sector in Pakistan**

*Aqeel Ahmad*

*UCP Business School, University of Central Punjab, Lahore (Pakistan)*

*Muhammad Tayyab*

*MS (Management) Scholar, Department of Business Administration, Leads Business School, Lahore Leads University, Lahore (Pakistan)*

### **Abstract**

*The purpose of this study is to investigate the impact of HRM Practices on perceived organizational performance in the small and medium enterprise (SME) sector of Pakistan. In this study Recruitment & Selection, Training & Development and Reward & Compensation are used to measure the perceived organizational performance. This research is quantitative in nature and questionnaire covers three items of HRM practices including Recruitment & Selection, Training & Development and Reward & Compensation which are used to check its impact on perceived organizational performance in SME sector of Pakistan. The results of this study are based on 342 respondents of different manufacturing, trading and services organizations from SMEs located in different areas of Lahore, the most important and busiest city of Pakistan. Descriptive, correlation and regression tests were used and results were obtained. These results show that there is significant and positive correlation between the said HRM practices and the perceived organizational performance of SME sector of Pakistan. The regression results show that there is significant and positive impact of the said HRM practices on perceived organizational performance. So, this study concludes that the said HRM practices can improve the effectiveness and efficiency of SME sector by implementing them in this sector of Pakistan.*

**Keywords:** Recruitment & Selection, Training & Development, Compensation & Reward, Perceived Organizational Performance, SME Sector of Pakistan.

### **Introduction**

The current era is the era of technology in which rapid changes are occurring in all fields of life including the industrial, agricultural, transportation, services, and other sectors. In any organizational structure there is need to integrate the resources of the organization with the help of organizational performance in positive and effective way. The mechanism of the Human Resource Management makes a clear understanding about the utilization of organizational resources in effective and efficient way. HRM is the process of managing human talent to achieve objective of an organization (Haslinda, 2009). When good HR practices are adopted in the organization, it can promote the level of knowledge, and expertise of the current and prospective employees of the organization, and it also strengthen the motivation level of employees and decrease avoidance and retain capable employees while push nonperformer to leave the organization, and improve performance of the employees and organization (Huselid, 1995). SME sector constitutes approximately 90% of the business sector and it covers 77% employment of the industrial sector as well as the contribution of SME sector in GDP of Pakistan is about 40% (SMEDA Pakistan, 2010). According to the Economic Survey of Pakistan there are almost 3.2 Million SMEs which are operating there business in Pakistan. The contribution of SME sector of Pakistan in national manufacturing exports is 24%, and it is providing employment to more than 21 Million people of Pakistan

(SMEDA Pakistan, 2010). The managers in SME are not much aware to manage their financial matter which results in underutilization of business resources (Salman, A. and Ehsan-ul-Haque, 2003). Furthermore it is learned that proper framework is not available to choose from in such specific contextual, and cultural setting of the organization (Rauf, M.A., M.J.V. Riemsdijk and J.K. Looise, 2010). In the light of above mentioned arguments it is declared that there is lack of implementation of HRM practices on the organizations of SME sector of Pakistan, and little effective research is conducted till now to explore the significant role of HRM practices on the organizational performance of SME sector of Pakistan. Therefore, it is needed to conduct a research to explore the impacts of Human Resource Management (HRM) practices on the performance of the organizations of SME sector of Pakistan.

### **Research Objectives**

- 1:** To check if the Recruitment & Selection practices leads to high performance of the organization in SME sector of Pakistan.
- 2:** To check if Training & Development practices contribute the high performance of the organizations in SME sector of Pakistan.
- 3:** To check that Reward and Compensation practices improve the organizational performance in SME sector of Pakistan.

### **Literature Review**

**Perceived Organizational Performance:** There are various definitions of the organizational performance to understand its concept. As it is defined by Campbell's (1999) that performance is a behavior or action which is related to achieving the goals of an organization that can be scaled and measured in any economic term. The Organizational Performance is one of the most important dependent variable which is used in different organizational studies at very broad level, and simultaneously, it is also one of the complex and under estimated constructs (Rogers and Wright, 1998) It is found that the perceived organizational performance is sometime positively associated with the objective & goals of the organization (Dollinger & Golden, 1992). Performance of the organization can be defined as it is a set of determinants (financial and non-financial) which are used to obtain the information on the level of attainment of the objectives and outcomes of the business (Lebans & Euske 2006 after Kaplan & Norton, 1993).

**Human Resource Management Practices:** The concept of human resource management has become much familiar all over the world because of its significant role to manage the resources of the organization and brought the fruitful results in organizational performance. Human Resource Management (HRM) is sometimes defined as the process or system of inspiring, promoting and maintaining a talented and skilled workforce within the organization to maintain the organizational mission, achieve objectives of the firm, and construct the strategies for a longer period of time. (Kok, Thurik & Uhlaner: 2003). The HRM practices are also defined as HRM is a process which consist of recruitment & selection, skills development, performance appraisal activities, development of HR policies as well as the maintenance of HR records within the organization (Kotey& Slade: 2005).

**Recruitment and Selection:** Recruitment and Selection process is an important Human Resource Practice which participates to a large extent on the performance of employees and organization. Wright and Boswell (2002b) investigated the impacts of recruitment and

staffing, skills development system, reward for performance, and in this case participation on performance measures are also included in organizational commitment of the business. The process of effective recruitment process will enable the employees of the organization to become more significant sources of innovative ideas in the innovation process of the organization (Chen & Huang, 2009).

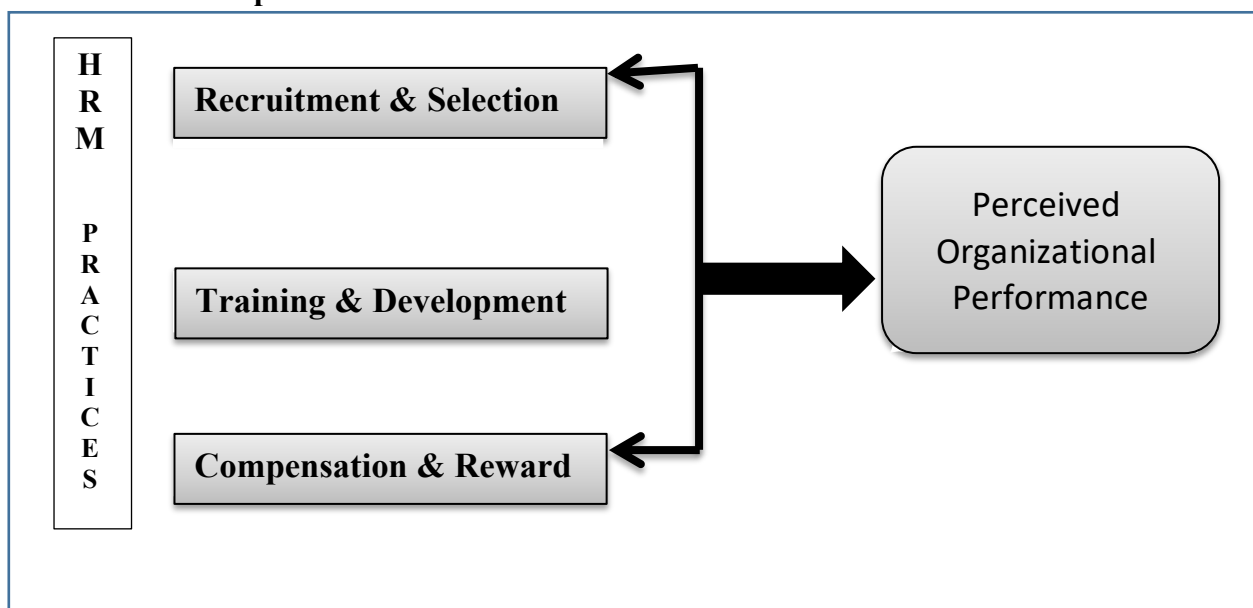
**Training and Development:** Training and development is another Human Resource Management Practice which plays an important role in the success of an organization. Most of the empirical studies represent the positive association between innovation and performance of the organization (Weerawardena, O’Cass, and Julian, 2006). The process that involved in improving skills, knowledge and other expertise with positive attitude in order to developing the efficiency and effectiveness on a specific job is known as Training and Development (Fajana, S.I. 2002). In the same way it was described by Mabey and Ramirez (2005) that fluctuation in organizational performance can be understand very easily if company size and development in managerial skills is taken into account for this purpose.

**Reward and Compensation:** Malhotra, Budhwar, Prowse (2007) explained that "work rewards" are the advantages, individual receive from their working environment and are considered determinants of occupation duty. Firms can affect the motivation level of employees by adopting several ways. A compensation system which is maintained on the basis of performance could be helpful to employees for attaining the specific goals and objectives of the firm. Compensation system enables an individual to achieve the goals of an organization with more efficiency and effectiveness, and it is also helpful to encourages innovation in the organization (Chen & Huang, 2009).

**The SME Sector of Pakistan:** According to SMEDA Pakistan, SME is defined as the enterprise with employees up to 250, having paid up capital 25 million, and annual sales are 250 million .SME sector of Pakistan plays vital role and have potential to grow in near future. In Pakistan Human Resource Management in SME sector seem to be in a developing or initial phase. Many of the organizations have named their personnel and administration departments as human resource departments, while consistently involved in reactive human resource management practices (Yasmin, 2008).

## Research Methodology

### Research/Conceptual Framework



Source: (Shamas Y. 2013)

### Research Hypotheses

**H1:** Recruitment and selection practices have positive and significant impact on perceived organizational performance.

**H2:** Training and development practices have positive & significant impact on perceived organizational performance.

**H3:** Compensation & reward practices have positive & significant impact on perceived organizational performance.

The target population of this study is the SME sector of Pakistan, in which various manufacturing, trading and service sector organizations are included. The study population of this study is consisting of Top Management, Line Management and supervisors of SMEs which are allocated in the area of Lahore. The units of analysis of the study are the individuals of the organizations in SME sector of Pakistan which are Top Managers, Line Managers, and Supervisors. The researcher collected data for this study by using the convenient sampling technique. The researcher visited many of the organizations which fall in category of Small and Medium Enterprises (SME) sector of Pakistan and distributed questionnaires. As Quantitative research has been conducted in this study. Therefore, descriptive and inferential statistical methods have been used in this study.

### Data Analysis And Results

As this is a descriptive study, and Mugenda (2003), argues that descriptive data is usually collected through questionnaires, interviews or by personal observation and an important instrument for data collection is a questionnaire. For this research primary data has been collected using convenient sampling through questionnaire from the Top Managers, Line managers and Supervisors of different Organizations that fall in category of Small and Medium Enterprises (SME). The questionnaire is adapted from the previous researchers Khan et al, (2012) and Al-Qarioti (2015) through appropriate modification to align with the Pakistani context. As sample size was 385 in this study. Therefore, total 425 questionnaires

were distributed to the individuals of the different organizations and, after a week, the researcher visited them again and collected the filled questionnaires back from which 342 questionnaires were completely and accurately filled rest of them were partially. The response rate for this study was 80.47%, and each item of IVs and DV was measured through 5 point Likert Scale.

Table 1: *Demographic*

	Details	Frequency		Details	Frequency
Designation	Top Manager	70	<b>Age</b>	Less than 30 years	80
	Line Manager	137		30 to 40 years	167
	Supervisor	135		More than 40 years	95
Experience	Less than 1 year	77	<b>Sex</b>	Male	234
	1 to 5 years	206		Female	108
	More than 5 years	59			
Nature	Manufacturing	148	Trading		103
	Services	91			

Table 1 shows that there were 70 top level Managers, 137 Line managers and 135 Supervisors including 234 males and 108 females of the age ranging from less than 30 to more than 40 years of old, among them 77 had experience less than one year, 206 had experience between one to five years and 59 had experience more than 5 years. It can be seen that 148 respondents belong to manufacturing, 103 to trading and 91 to services organizations out of 342 organizations

Table 2: *Correlation*

<b>Variables</b>	Recruitment & Selection	Training & Development	Compensation & Reward	Organizational Performance
Recruitment & Selection	<b>1</b>			
Training & Development	.837**	<b>1</b>		
Compensation & Reward	.631**	.605**	<b>1</b>	
Organizational Performance	.900**	.854**	.671**	<b>1</b>

\*\* . Correlation is significant at the 0.01 level (2-tailed).

Correlation Analysis has been performed by the researcher in this study to check the association of the variables which have been used in this study. Correlation analysis shows level of association of the Dependent Variable and Independent variables and it also shows that whether the variables are positively correlated or negatively correlated. The above table shows the results of Pearson correlation measure among observed variables statistically. The correlations between variables are positive and significant support the research objectives and research questions of this research study. The highest level of correlation is between Recruitment & Selection and organizational performance that is .900\*\* showing the Recruitment & Selection and Organizational performance are strongly correlated to each other

and similarly the lowest correlation exists between Compensation & Reward and Training & Development that is .605 \*\* shows moderate positive relation at the level of 0.01. The other results of correlation test are given in the table which represents the level of association among the variables of the study.

Table 3: *Regression Analysis*

Sr.#	Variables	Beta Value	R Square value	F value	P Value	Hypothesis
1	<b>Recruitment &amp; Selection</b>	1.222	0.809	1442.933	0.000	H1 (Accept)
2	<b>Training &amp; Development</b>	0.936	0.729	913.995	0.000	H2 (Accept)
3	<b>Compensation &amp; Reward</b>	0.840	0.449	278.747	0.000	H3 (Accept)

The above table 3 describes the regression results for the variable Organizational performance and Recruitment and Selection. Here Recruitment and Selection is independent variable and Organizational performance is dependent variable. As it can be seen from the table 3 that value of R square is **0.809** it means that in our model Recruitment and Selection is explaining 80.9 percent variability in Organizational performance. The value of F is **1442.933** with P value **0.000**, that is significant as confirmed from the value of P that is <0.05 at 95 % confidence level. So model is good. Similarly, the results table 3 confirms a significant impact on Organizational performance due to Recruitment and Selection. Here the value of beta is **1.222** that is positive and it shows one unit change in Recruitment and Selection brings 1.222 unit of change in Organizational performance. Delaney and Huselid (1995) also found the positive and significant associations between Recruitment & Selection systems and Organizational Performance. It is also observed in case of Training & Development that value of R square is **0.729**, it explains that in this model Training and development is explaining 72.9 percent variability in Organizational performance. The value of F is **913.995** with P value **0.000**, that is significant statistically as confirmed from the value of P that is <0.05 at 95 % confidence level. The results of regression in last table confirm a significant impact on Organizational performance due to Training and development. Here the value of beta is **0.936** that is positive and it shows one unit change in Training and development brings 0.936 unit of change in Organizational performance. When we investigate the past researches we found that Harel and Tzafrir (1999) examined the impact of Human Resource Management practices on Israeli companies and they found that training practices perform a significant role on organizational performance. Similarly it can be seen in case of compensation & reward that value of R square is **0.451** it describes that Compensation and Reward is explaining 45 percent variability in Organizational performance. The value of F is **278.747** with P value **0.000** that is significant statistically as confirmed from the value of P that is <0.05 at 95 % confidence level. Similarly, the results of regression in last table confirm a significant impact on Organizational performance due to Compensation and Reward. Here the value of beta is **.840** that is positive and it shows one unit change in Compensation and Reward brings .840 unit of change in Organizational performance. In the same way a substantial body of work

argues that best compensation and reward system has a significant and positive impact on performance of the organization (Oladipo 2011).

### **Conclusion**

This study was conducted to explain the impact of the Human Resource Management practices on the organizational performance in SME sector of Pakistan. The study was quantitative, and researcher was interested to collect the primary data through questionnaire from different organizations which fall in the category of the Small and Medium Enterprises (SME) sector of the Pakistan. This questionnaire was comprised of items for four variables, named Organizational Performance, Recruitment & Selection, Training & development and Compensation & Reward. The Organizational performance was the dependent variable, whereas remaining three variables were independent variables. Total 425 questionnaires were distributed to the individuals of the SME sector of Pakistan which includes of Top Managers, Line Managers and Supervisors. The Value of the Cronbach's alpha was 0.920, and it shows the data was reliable. The results of the correlation analysis show that there was strong association among the variables of the study. The result of the Regression analysis shows that when we check the impact of the Recruitment and Selection on perceived organizational performance, it was observed that Recruitment & Selection has positive impact on the organizational performance. This support the first hypothesis that, Recruitment & Selection has a positive impact on the Organizational Performance, So, **H1** is accepted. When we check the impact of Training & Development on the Organizational Performance, we found the positive and significant impact of the Training & Development on the Organizational Performance. This supports the second hypothesis that Training & Development has positive impact on the performance of the organization. So, **H2** is also accepted. Finally when we examine the impact of the compensation & reward on the organizational performance through Regression analysis, it was understood from the results that Compensation & Reward has positive and significant impact on the Organizational Performance. In the light of this result **H3** is accepted that, Compensation & Reward has a positive impact on the performance of the organization. So it can be concluded in the light of all above results and arguments that HRM practices have positive & significant impact on the organizational performance in the SME sector of Pakistan.

### **Managerial Implications**

The findings of the present study are expected to enrich HR professionals' understanding about improving the performance of organizations in SME sector of Pakistan. The outcome of this study also gives some helpful guidelines to the present and future HR professionals in the SME sector of Pakistan to achieve success in their profession and get to fruitful outcomes for their organizations. The findings of the study also provide guidelines to the managers to empirically prove that the HRM practices (Recruitment & Selection, Training & Development and Compensation & Reward) have positive effect in improving the performance of organizations of SME sector of Pakistan. So, HR managers need to operationalize these HRM practices in their organizations if they want to enhance the performance of their organizations. These all HRM practices are very common in the developed countries now days, and if the HR professional of developing countries like

Pakistan adopt these practices in their organizations the output level of the organization in all economic terms can be enhanced easily.

#### **Theoretical Implications for the study**

The finding of the present study has contributed to the body of knowledge by bringing in new insights on the factors that may contribute to enhance the performance of organizations of SME sector of Pakistan. Further, the study has indicated that certain factors contribute more to the performance of SMEs than others. The study contribution is adding and examining the relationship and impact of HRM practices on organizational performance. Furthermore, the study thus adds to the existing body of knowledge by testing the applicability of these HRM practices in a new context and a new set of environmental frameworks and can be referred to as theory verification research with additional benefits of theory development and refinement. This study is also very helpful to disclose the facts of the SMS sector of Pakistan that how policies can be settled to improve the performance of the organizations in SME sector of the Pakistan.

#### **Limitations of the study and Future Research Directions**

While making the discussion on the limitations of the study, it would be stated that this study was conducted to test the impact of HRM practices on the organizational performance in SME sector of Pakistan. In Pakistani context where Human Resource Management (HRM) is at its initial stages it needs to be improved for the maximization of its effectiveness. In Pakistan the competency level of HR professionals, literacy rate of employees and working conditions within the organization do not match with the developed countries. So, the results may vary in different context, as there is huge gap between the HRM effectiveness level in developing country and in developed country. This study will only be helpful to understand the impact HRM practices on the organizational performance having similar cultural, political, historical and economical background. Furthermore, the study is conducted in SME sector of the Pakistan; same can be tested and analyzed in other sectors of Pakistan as well as other countries of the world. This study explores new horizons for the future researchers to found the other significant HRM practices and to test the impact of those practices on organizational performance in other sectors of economy, whether those HRM practices are significant or not for the organization.

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