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THE INFLUENCE OF STRATEGIC HR PRACTICES ON ORGANIZATIONAL PERFORMANCE IN MICRO COMPANIES

Emil Knezović¹

ABSTRACT

The research in human resource management (HRM) field has evolved in past couple decades. By observing human resources (HR) as one of the most important assets in the business, it is obvious that it represents a key to business success or failure. By reviewing the literature, one cannot neglect that there is one serious gap in HRM research which relates to micro companies. This study aims to reduce that gap by examining 107 micro companies in relation to strategic HR practices and organizational performance. Results show that there is no enough evidence to support positive and significant relationship between strategic HR practices and organizational performance in micro companies.

Keywords: strategic human resource management; organizational performance; small and medium enterprises, micro companies, Federation of Bosnia and Herzegovina

1. INTRODUCTION

The importance of small and medium enterprises (SMEs) to the economy is highly supported by the statistics across the globe (Savlovski & Robu, 2011). According to these two authors, the role of SMEs in modern economy can be explained by two perspectives. The first one is the company's perspective which states that many big companies were actually developed from SMEs and that most of competitors are expected to come from this sector in the near future. On the other hand, there is an individual's perspective which states that SMEs represent the first source of a job. Under normal conditions and proper support, SMEs are real power in generating adequate-income jobs (Berry, 2002).

Speaking about the perspectives, Zaman and Vilcenau (1999) adds one more which states that most of innovations and creations in the business come particularly from this sector. The overall national income is highly dependent on the performance of SMEs, thus their role and importance in economic development have risen recently. Taking into consideration its dominancy in terms of number of enterprises and number of employees, it is obvious that SMEs have direct impact on both employment and economic growth (Aceleanu, Trasca, & Serban, 2014). When it comes to developing countries, sector such as the one of SMEs has been highly prioritized regarding the fight with unemployment (Amra, Hlatshwayo, & McMilan, 2013). According to Subhan, Mehmood, and Sattar (2013), the increase in economic activities within a country is caused by SMEs' growth which on the other hand is highly related to improvements in the process of innovation. There is not many works published on the topic of SMEs and the Bosnian economy. One of the main reasons is unavailability of data on SMEs in the country. However, there are some works that should be mentioned here. Mainly, the researchers were focused on the limitations imposed by the law and other regulations on this sector. In 2001, Hasic (2001) used several variables such as trade and monetary policy, regulations, the flow of capital and the policy of foreign investments, banking, taxes, government interventions, prices and payment control, ownership rights and the black market to present the obstacles with which SMEs in Bosnia and Herzegovina have to deal. In his later research, Hasic (2006) analyzes the strengths and possibilities of SMEs to adapt and deal with future challenges related to participation in the process of globalization. As a result, he stated that SMEs and conditions related to

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them, in Bosnia and Herzegovina, are among the worst out of all economic components of the countries. In 2009, Bosnia and Herzegovina was in its initial stage of entrepreneurship and development of the SMEs sector. Unfortunately, there were no clear objectives and strategies by which SMEs should have impacted the economy and lead the country out of the crisis in that time (Dzafic et al, 2011).

Companies' success and growth are linked to their ability to achieve a competitive advantage over their rivals through distinctive competencies. Obtaining a good competitive position is a challenge for businesses today. The competitive advantage in modern business is highly dependent on human resources (HR) and therefore there is a huge need for companies to create cohesive and effective strategic human resource management (HRM) system. According to Waiganjo, Mukulu, and Kahiri (2012) strategic HRM represents a new pattern for management of Human Resources (HR) in organizations. Poor management is identified as one of the main reasons that lead to the failure of small and medium enterprises. According to Ijose (2010), in order to be recognized as valuable partners, SMEs have to focus themselves on their human resources in terms HR capabilities, adding a value in the value chain, be adopted to the types of industries needed and be understood by management. The question of HR, as sources of competitive advantage in small and medium enterprises, was highlighted by Wright, McMahan, and MacWilliams (1994) where they emphasized the importance for SMEs to identify whether their human resources are creating the competitive advantage in terms of four elements: value, rareness, inimitability and non-substitutability.

The fact that strategic HRM is important in SMEs can be found in the relevant literature. In support of this, Beaver and Hutchings (2005) found out that "SMEs which take a strategic approach to training and development of their human resources will profit not only from a competitive position in their marketplace but that they will also be well placed in order to adjust to changing and often uncertain external influences on the business environment presented to organizations in the 21st century"

(p. 592). Human resources in small companies can be observed from two perspectives. One is described by Singh and Vohra (2005) who state that the main problems of managers in small businesses are "attracting talent, motivating employees, and retaining key employees" (p. 57). Another perspective has been described by Tansky and Heneman (2003) who state that human resources as a source of competitive advantage were mostly analyzed in the setting of big companies in previous period. The focus on SMEs has been a recent trend (Umer, 2012). However, one substantial part of this sector has been neglected in the previous research that was developed around size and age as eliminatory criteria (Cardon & Stevens, 2004). The support for the neglecting of micro companies can be found in the statement made about SMEs which says that there is "homogeneity among smaller firms, e.g., they are informally organized, with correspondingly informal HRM practices" (De Kok & Uhlaner, 2001).

Taking everything into consideration, this study explores the usage of strategic HRM in micro companies. Further it aims to test the relationship between strategic HR practices and organizational performance in micro companies.

2. LITERATURE REVIEW

2.1 Definition and importance of micro companies

The first thing that we can observe is the term that was highly used in the literature. SMEs stand for small and medium companies. It is also true that some definitions contrast these two types to less than 50 and 250 such as in the case of the national Law of Bosnia and Herzegovina (Ministry of Development and Entrepreneurship, 2012).

However, some of the recent studies supported the inclusion of micro companies as separate group in the classification of SMEs. Leegwater and Shaw (2008) dedicated one report to the sector that they called micro, small, and medium enterprises (MSMEs). The similar report was done in Egypt by Creative Associates International (2014). Since these three groups

of companies are the engine of economy (Wilde, 2011), it is important to contrast among them.

The definition of SMEs varies from country to country, but several criteria used in this classification are highly accepted, such as: number of workers, annual turnover, total

assets, and the degree of independence of company (European Commission, 2015). Guided by these criteria, the Law on the Promotion of Small Business Development of the Federation of Bosnia and Herzegovina proposed the classification of SMEs as shown in Table 1.

Table 1. Federation of Bosnia and Herzegovina Criteria for SMEs (Ministry of Development and Entrepreneurship, 2012)

Company categories	Assets (mill. Of €)	Revenue (mill. Of €)	Employees
Micro	0.20	0.20	1-9
Small	2.00	2.00	10-49
Medium	15.00	20.00	50-250

Small businesses have important role in World's development. Small businesses represent large force that contributes to three areas of development: economic, social, and employment (Savlovschi & Robu, 2011). Edminston (2007) supported the importance of smaller businesses where he stated that "economic development experts are abandoning traditional approaches to economic development that rely on recruiting large enterprises with tax breaks, financial incentives, and other inducements" (p. 73). Further, it is important to mention that trend is changing and that during the recent years SMEs started to lose their competitive ground while observing the micro companies' growth. The importance of micro companies is even more noticeable when we observe their share in developing countries. According to Li and Rama (2013), these types of companies represent 80% of manufacturing companies in South and Central America and 90% of manufacturing companies in developing Asian countries, such as: China, Korea, Indonesia, and Taiwan highly contributing to employment in these countries.

2.2 Strategic Human Resource Management

The focus on human resources, as the area where companies may gain their competitive advantage, has increased in the last decade. Today, it is undoubted that productivity, globalization, competitiveness and changes cannot be achieved without the accurate and comprehensive understanding of human resources. Human beings are no longer a marginal organizational resource, but rather

a significant source of the new value (Dzubur, 2003).

The main strength of the organization is people and that is why it is so important for organizations to choose the right people and to manage them in the best possible way. For companies, it is important to observe their human resources as individuals with their own needs, wants, desires and ways of motivation. Organizations should think out of the box in order to exploit the information they have and to direct their people toward the organizational goals (Dzubur, 2003). According to Sladovljević, Sisara, and Boban (2007), human capital plays an important role in the implementation of business strategy. In this context, they identify the external strategy as a means of competition and internal strategy as a way of developing, engaging, directing, motivating and controlling the internal resources.

According to Siber (1999), the modern management of human resources has four meanings which are scientific discipline, managerial function, special operations function and specific philosophy of management. Armstrong (2006, p. 3) defines Human Resource Management as a "strategic and coherent approach to the management of the organization's most valued assets – the people working there who individually and collectively contribute to the achievement of its objectives". Desler (2012) describes this managerial function as the process of acquiring, training, appraising and compensating employees. Besides that, it is out of the crucial importance to manage their

labor relations, health and safety and fairness concerns. Therefore, organizations constantly invest in education, employ quality staff, evaluate performance and improve workforce in order to maintain and increase the value of their intellectual capital. They emphasized the importance of it and acknowledge that it is the factor that is hardly replaceable and almost impossible to copy since each human capital is customized for the purposes of the organization. Today companies are competing in the market on the basis of human capital (Sladovljević, Sisara & Boban, 2007).

In order to be able to respond to constant changes in the environment, it is crucial for HR managers to take a strategic approach to their job by aligning their strategies with the organizational one. This is a relatively new phenomenon that is related to a transformation in HRM field (Caliskan, 2010). Bratton (2003, p.37), defines strategic human resource management (SHRM) as “the process of linking the human resource function with the strategic objectives of the organization in order to improve performance”. According to Fottler (2010), SHRM is a comprehensive process that deals with acquiring, developing, and maintain a qualified workforce. In simple words, HRM represents and operative function, while SHRM is the strategic one. Companies are aware of human resources as the most important asset of organization (Barney, 1991), and therefore they acknowledge that by implementing effective policies and practices they are going to improve their organizational performance. Numerous studies support a positive relationship between strategic HR practices and organizational performance at different levels (Arthur, 1994; MacDuffie, 1995; Huselid, 1995; Delery & Doty, 1996; Guest, Michie, Sheenan, & Conway, 2003; Akhtar, Ding, & Ge, 2008; Ngo, Lau, & Foley, 2008; Mitchell, Obeidat, & Bray, 2013).

2.3 Strategic human resource management in micro companies

The focus of HRM research was primarily on big companies. The trend shifted in 21st century and more importance was given to the sector of small and medium enterprises due to their importance in national economies. However, researchers (Chang & Huang, 2005; Katou, 2011; Khan & Khan, 2012; Moidenkutty, Al-Lamki, & Murthy, 2010; Sels et al. 2003) were warning that one

important part of this sector, which is micro companies, was avoided in HRM research.

Even though human capital was perceived as one of critical factors to business success in new and small companies the research in this field is comparatively new (Cardon & Stevens, 2004). Taking this into consideration, several researchers explored the usage of HRM in micro companies. On the one hand, Kahando, Ng'ang's, & Kyalo (2014) argued that informal and unwritten practices characterize HRM in micro companies while, on the other hand, Hashim and Ismail (2011) found existence of formal strategic HR practices in micro companies. However, both works showed the positive and significant relationship between strategic HR practices and some aspects of organizational performance. Comparing the two types of companies (small and micro), Parilla (2013) concluded that small business tend to have more formal management practices than micro companies. This perception has been highly accepted in many areas of research when it comes to small sized businesses. In a comparative study conducted in Australia, that has smaller criteria for companies in terms of employees (<20), Barrett and Mayson (2007) showed that small companies with growth oriented strategy are using formal strategic HR practices more than those with non-growing aspiration. Mattare, Shan, and Monahan (2013) found that sales influenced several strategic HR practices. However, they did not examine reverse causality in their study that was conducted in the State of Maryland. In their study, Vettriselvan, Sathya, and Balakrishnan (2014) emphasized the key role of human effort in reaching the organizational goals even in small sized companies. Rauch and Frese (2000) showed that several strategic HR practices such as training, employee participation, goal communication, and support for personal initiative were the positive influencers on performance of small companies and that strategic HR practices were more effective in the presence of higher human capital. Grigore (2008) found that HRM intensity had positive influence on several dimensions of performance in small companies.

Taking everything into consideration, the following hypothesis has been made:

H1: There is a positive and significant relationship between strategic HR practices and organizational performance in micro companies.

3. METHODOLOGY

This study aims to test the theory of relationship and influence of universal set of HRM practices on organizational performance in micro companies by using universal approach. According to Gooderham, Pary, and Ringdal (2008), this approach is defined as a model where there are pre-determined HR practices that are expected to work in organizations no matter the contingency factors employed. Due to the lack of such research in micro companies, the primary data was collected through cross sectional survey method where questionnaires were sent to companies in the Federation of Bosnia and Herzegovina. For the purpose of this study, the non-probability convenient sampling method has been used since there no public database of micro companies was available at that time.

The questionnaire was created by adapting two questionnaires. The part for strategic HR practices was adapted from Delery and Doty (1996) work, while the part for business performance was adapted from Dyer and Reeves (1995) work. Questions related to the set of HR practices were

based on a 7-point Likert Scale. The set was measured by several HR practices, namely: career development, training, performance appraisal, job security, employee participation, job descriptions, and profit sharing. On the other hand, business performance question were based on 5-point Likert scale and it was measured from three dimensions: financial outcomes, organizational outcomes, and HRM outcomes. In order to control for some effects, several control variables were used such as: size, age, and market competition.

The collected data was analyzed in two stages. The first stage was based on some preliminary statistics such as reliability, descriptive statistics, and correlation while the second stage was used to test hypothesis through hierarchical regression.

4. RESULTS

The results section starts with Table 2 that shows characteristics of respondents consisted of 107 micro companies in the Federation of Bosnia and Herzegovina.

Table 2. Profile of Respondents

Category	Frequency	Percent
Years of operation		
3-5	7	6.5
6-10	74	69.2
Over 10	26	24.3
Industry		
Manufacturing	9	8.4
Service	74	69.2
Trade	22	20.6
Other	2	1.9
Founder manager	85	79.4
Gender of manager		
Male	85	79.4
Female	22	20.6
Education of manager		
High school	34	31.8
Bachelor	42	39.3
Master	28	26.2
Ph.D.	3	2.8
HR staff employed	8	7.5

Note. $N = 107$.

From the table above, we may see that most of the companies are in the business for more than five years. This means that they have already passed the critical years after their initial establishment. The dominant sector in this particular sample is the service sector. This comes as the result that micro companies are more “soft” oriented companies and due to their limitations in terms of employees and finance, they are more suited to work in service or trade industry. When it

comes to owners of companies, there are several interesting facts that come to the focus, such as: the most of companies are managed by their initial founders, there is a gender disparity, and managers tend to be high educated. Finally, as it could be expected, only few companies have formally employed staff for HR matters.

Tables 3 and 4 show the reliability coefficient for variables used in this research.

Table 3. Reliability Scale for Strategic HR Practices

Variables	Cronbach's alpha	Number of items
Career Development	.68	3
Training	.86	4
Performance appraisal	.89	2
Job security	.65	3
Employee participation	.75	4
Job description	.60	4
Profit sharing	/	1
Total	.88	21

Note. $N = 107$.

Table 4. Reliability Scale for Organizational Performance

Variables	Cronbach's alpha	Number of items
Financial outcome	.92	3
Organizational outcome	.76	4
HRM outcome	.84	4

Note. $N = 107$

A reliability test shows moderate to high reliability of measures. Even if the common threshold for the values is 0.7, in some case the lower values can also be accepted, especially in exploratory research (Hair et al., 2006). Further,

the original authors of the set (Delery & Doty, 1996) reported the Cronbach's alpha above 0.6. Descriptive results and correlation coefficients among the variables are presented in Table 5.

Table 5. Descriptive Statistics and Correlation Matrix

	M	SD	1	2	3	4	5	6	7	8	9	10
1 Financial outcomes	3.2	1.0	-									
2 Organizational outcomes	4.0	0.7	.57**	-								
3 HRM outcomes	4.0	0.8	.53**	.73**	-							
4 Career development	4.8	1.3	.20*	.27**	.34**	-						
5 Training	5.0	1.5	.19	.28**	.29**	.58**	-					
6 Performance appraisal	5.5	1.5	-.11	.07	.14	.47**	.45**	-				
7 Job security	5.1	1.4	.24**	.10	.20*	.33**	.19*	.30**	1.00			
8 Employee participation	5.7	1.0	.04	.05	.01	.35**	.38**	.30**	.39**	-		
9 Job descriptions	5.4	1.1	.17	.16	.15	.43**	.32**	.28**	.32**	.53**	-	
10 Profit sharing	4.2	2.2	.14	.16	.11	.35**	.36**	.29**	.05	.13	.28**	-

Note. $N = 107$. * $p < .05$; ** $p < .01$

The table 5 shows two important things: descriptive statistics on strategic HR practices and business performance and the correlation among them. Regarding the descriptive statistics, we may observe that all strategic HR practices obtained relatively high mean scores (greater than 50%). Looking individually, the highest score was for employee participation (5.7) while the lowest was for profit sharing (4.2). On the other hand, when it comes to business performance indicators we may observe that organizational outcomes and HRM outcomes had mean score ($M=4.0$) higher than financial outcomes (3.2).

By observing the correlation matrix we may see that when it comes to strategic HR practices correlation coefficients are mostly statistically significant except in the case of profit sharing

that has insignificant correlation with job security and employee participation. The correlation is moderate in five cases and weak in the rest. On the other hand, the correlation among business performance indicators is statistically significant. When it comes to financial outcomes, the correlation, in both cases, was moderate. The strong correlation is present between organizational outcomes and HRM outcomes.

In addition, the individual correlation between strategic HR practices and indicators of business performance is weak and statistically significant only in some cases of career development which gives some support for the main hypothesis. To test the main hypothesis, the author used hierarchical regression. The results of it are shown in Table 6.

Table 6. Hierarchical Regression

Independent/Dependent	Financial outcomes		Organizational outcomes		HRM outcomes	
	β	ΔR^2	β	ΔR^2	β	ΔR^2
Control variables		.16*		.17**		.15*
Strategic HR practices		.15**		.08		.14*
Career development	.07		.08		.18*	
Training	.14		.10		.10	
Performance appraisal	-.23**		-.05		-.05	
Job security	.18*		.01		.06	
Employee participation	-.10		-.07		-.14	
Job descriptions	.08		.05		.04	
Profit sharing	.03		.00		-.02	
Full model		.31**		.25*		.29**

Note. $N = 107$. * $p < .05$; ** $p < .01$

In the presence of control variables (age, size, founder as manager, industry, and market competition), a set of the best strategic HR practices was entered simultaneously and showed mixed results. Strategic HR practices explained additional 15% of the variance in financial outcomes ($\Delta F=3.08$, $\Delta R^2=.15$, $p<.01$). The overall model was also statistically significant. However, the individual relationship between performance appraisal and financial outcomes was negative. In this case, there was no support for Hypothesis 1-1. Further, the presence of strategic HR practices was statistically insignificant in the case of organizational outcomes. Therefore, the

Hypothesis 1-2 was not supported. On the other hand, strategic HR practices explained 14% of variance in HRM outcomes ($\Delta F=2.5$, $\Delta R^2=.14$, $p<.05$) which gave us support for Hypothesis 1-3.

5. CONCLUSION

This study has identified that there is a need for HRM research in micro companies due to their contribution to the economy. In modern business, one of the most important assets is human capital and therefore the gap that is created by neglecting micro companies has opened some questions.

However, due to the growing importance of this type of companies, several recent publications called for or tested the possibility of inclusion of micro companies in HRM research (Baron, 2003; Vettriselvan, Sathya, & Balakrishnan, 2014).

The hypothesis tested in this research was regarding universal application of strategic HR practices in micro companies and its influence on organizational performance. The results obtained (See Table 6) showed that there is not enough evidence to support the inclusion of micro companies in HRM research which is in agreement with most of studies conducted in smaller companies.

The study faced several limitations. First, there is no public database on micro companies in the area where the research took place. The database that was available was out of date resulting with companies being out of business. Because of that, the convenience sampling method was applied which limited the possibility of generalization of results. Cross sectional survey represents another limitation since it collects the data at one point of time. The sample of the study is relatively small but this was another consequence of unavailability of public database. Finally, a multi industry approach limits this research study to more concrete discussion that includes specific industry characteristics.

This study sets ground for one important question for further research. The set of strategic HR practices used in this research were originally created for companies with larger number of employees. One of the possible reasons why the application of this particular set did not show supporting evidence could be due to specificity and characteristics of micro companies (Barber, Wesson, Roberson, & Taylor, 1999; Van De Woestyne, Dewettinck, & Van Bruystegem, 2010). If a particular set works in large or even in small and medium enterprises it does not mean that it will work in micro companies. Due to their different nature, the special attention should be given to the development of appropriate set of strategic HR practices that could influence organizational performance in micro companies. Longitudinal approach is also a possibility in future and it is also desirable due to specific characteristics of micro companies and avoidance of possible reverse causality.

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