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## Article

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Journal of Risk and Financial Management

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*Suggested Citation:* Mashavira, Nhamo; Guvuriro, Sevias; Chipunza, Crispen (2022) : Driving SMEs' performance in South Africa: Investigating the role of performance appraisal practices and managerial competencies, Journal of Risk and Financial Management, ISSN 1911-8074, MDPI, Basel, Vol. 15, Iss. 7, pp. 1-18,  
<https://doi.org/10.3390/jrfm15070283>

This Version is available at:

<https://hdl.handle.net/10419/274805>

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Article

# Driving SMEs' Performance in South Africa: Investigating the Role of Performance Appraisal Practices and Managerial Competencies

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**Abstract:** Managerial competencies and performance appraisal practices are often ignored when considering the performance of Small-to-Medium Enterprises (SMEs). Yet, these competencies and practices are fundamental for the survival of the SMEs. SMEs are critical for economic growth and job creation in many economies. The current study sought to establish whether managerial competencies and performance appraisal practices correlate with SMEs' performance in South Africa. Firm performance was measured using two variables: innovation and return on investment (ROI). The study adopted a structural equation modelling analytical approach. Interpersonal competencies were found to be a significant factor of managerial competencies, but conceptual and political competencies were not. The study also found that managerial competencies, and not performance appraisal practices, significantly correlated with both innovation and ROI. The study recommends that performance appraisal practices be tailored to suit SMEs in the developing countries context.

**Keywords:** SMEs; managerial competencies; performance appraisal; business performance; South Africa



**Citation:** Mashavira, Nhamo, Sevias Guvuriro, and Crispen Chipunza. 2022. Driving SMEs' Performance in South Africa: Investigating the Role of Performance Appraisal Practices and Managerial Competencies.

*Journal of Risk and Financial Management* 15: 283. <https://doi.org/10.3390/jrfm15070283>

Academic Editors: Abdullah Promise Opute and Khaled Hussainey

Received: 29 March 2022

Accepted: 16 May 2022

Published: 27 June 2022

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## 1. Introduction

Small-to-Medium Enterprises (SMEs) contribute to economic growth, job creation, wealth and income generation and poverty reduction (Manzoor et al. 2021). Increased firm competition and globalisation have raised the importance of firm performance as an organisational topic (Chinomona 2013; Masroor and Muhammad 2019; Yang et al. 2017). Organisational performance, the ability of an organisation to produce results in line with its set targets (O'Regan et al. 2008), is critical for SMEs' survival (Mabhungu and van der Poll 2017). There has been an increase in entrepreneurial research focusing on SMEs' performance (Aleem and Rahman 2018; Kirsten et al. 2015) premised on SMEs' fundamental role in the socio-economic development of economies, particularly employment and economic growth (Ardic et al. 2011). Worldwide, about 90% of private businesses are SMEs and these contribute more than 50% of employment opportunities (World Bank 2021). SMEs in Western Europe, Japan and the United States of America (USA), for instance, generate 55% to 80% of total employment (Katua 2014). Approximately 23 million SMEs in the USA contribute more than 50% to the country's Gross Domestic Product (GDP) (Katua 2014) and these SMEs are pivotal in creating new jobs, improving product quality, increasing competition and driving innovation.

In the African context in countries such as Egypt, Nigeria and Kenya, SMEs have been estimated to contribute over 70% towards employment and 30–40% to GDP. In Ghana, about 92% of businesses are SMEs contributing about 85% towards employment and about 70% to GDP (Frimpong 2013). SMEs in South Africa account for about 91% of the

formal business entities, contributing to about 51% to 57% of the GDP and providing almost 60% of employment opportunities (Cant and Wiid 2013). With an unemployment rate of approximately 34.9% (Statistics South Africa 2021) and high levels of poverty and inequalities (Chatterjee et al. 2021), the performance of SMEs becomes a critical subject for investigation to leverage employment creation, competitiveness and innovation. Bhorat et al. (2018) predicted that SMEs have the potential to advance both inclusive growth and development and to generate 90% of new jobs by 2030, in South Africa.

The South African government, through the Department of Trade and Industry (DTI), the Industrial Development Corporation (IDC), the Small Enterprise Development Agency (SEDA) and the Small Enterprise Finance Agency (SEFA), seeks entrepreneurial ventures sustenance. Nevertheless, SMEs in South Africa continue to record low performance, low growth and high failure rates (Fatoki 2018), and the Family Business Association of Southern Africa (FABASA), the official representative of family businesses in South Africa, continues to report SMEs' low performance.

Performance appraisal has been found to be significant to organisations as, in addition to measuring the quality of human resource management (Aggarwal and Thakur 2013), it catalyses the motivation and creativity of employees (Abouzeid 2018). Tahiri et al. (2021) also identified appraisal of employees' performance (also known as employee evaluation or employee rating) as one of the key issues in the management of human resources. Yet, despite being the most significant development in human resource management, performance management as well as its performance appraisal tools, has not received much empirical recognition amongst entrepreneurial ventures (Wickramasinghe 2016). The few studies, for example, Wijetunge (2014) and Zheng et al. (2009), available on managing employee performance in SMEs in general suggest that SMEs face difficulties in executing performance management. This evidence provides scope for further research on performance appraisal. Having inappropriate or no formal appraisal of employees' performance may limit firm performance. Studies by Ling and Nasuridin (2010) and Narware (2011) respectively reported a positive effect of performance appraisal on administrative innovation and knowledge management, thereby enhancing the industrial environment and the long-term success of SMEs. Kathiravan et al. (2017) reported elements involved in the appraisal process, such as appraisal method, fairness process, fairness outcome, employee participation, goal congruity, feedback on performance and a performance-based approach to be strongly related to effective performance appraisal in SMEs.

Related to employee performance appraisal is the managerial competencies (Sabiou et al. 2019) and these have been considered important for business performance too (Bulog et al. 2017). Moreover, managerial competencies provide a sound basis for meaningful performance management (Bhardwaj and Punia 2013), which, despite being more expansive and strategic than an appraisal, encompass the performance appraisal process. A direct link is therefore said to exist between managerial competencies, value creation and a firm's growth and strategy (Fatoki 2014).

Studies of SMEs in developing countries have attributed the underperformance of SMEs to exogenous factors advertently or inadvertently ignoring endogenous factors such as managerial competencies and employee appraisal practices. Employee appraisals provide critical employee information to the business (Bititci et al. 2015) and this information is useful for promotions, salary administration, layoffs, retention-termination and the identification of individual employee performance gaps to the HR management (Noe et al. 2010). When entrepreneurial ventures neglect managerial competencies and employee appraisal practices, such weak HR management practices can impact on firm performance (Patel and Cardon 2010; Kotey and Slade 2005).

This study sought to examine the influence of performance appraisal and managerial competencies on SMEs' performance in a developing country setting. The study adopts two measures of performance which are ROI and the product and process innovation (hereinafter referred to as innovation). Innovation involves two dynamic outcomes—changes in the particular services/products offered to the clients or customers, and changes in the

mode through which they are created and delivered (Damanpour and Gopalakrishnan 2001). The choice of the aforementioned measures has been influenced by the Balanced Scorecard, developed by Kaplan and Norton (1992)—a well-known model for balancing financial (ROI) and nonfinancial measurements of performance (in this case innovation). According to the model, adding nonfinancial measures of performance to the traditional financial measures helps to provide a more holistic view of the actual performance achieved (Mashovic 2018). Analytically, the study adopts structural equation modelling to establish if there are significant correlates between (i) performance appraisal practices, managerial competencies and ROI, and (ii) performance appraisal practices, managerial competencies and innovation. The analytical approach employed here allows for the extraction of information from a range of measurements for each of the latent variables in the model. The adoption of subjective socio-emotional financial measures (ROI and innovation), as measures of firm performance, improves critical decision-making that is not only based on traditional measures.

The rest of the paper is structured as follows. Section 2 provides hypotheses development. This is followed by the research methodology in Section 3 and the results in Section 4. Sections 5 and 6 provide the discussion and conclusions, respectively.

## 2. Hypotheses Development

### 2.1. Performance Management and Performance Appraisal

Performance management, like other human resource management innovations, is an American import whose origins are controversial. The evaluation of performance can be traced back to the sixth day of God's creation process: "God saw all that he had made, and it was very good" (Genesis 1:31, NIV). Some literature (Smith and Goddard 2002; Andersen et al. 2006) pointed out that performance management has no mutually agreed definition and can mean different things to different people. An extensive literature review by Ates et al. (2013) posited performance management as a process that starts with strategy development which requires the development of vision, mission and values and the definition of business goals and objectives at corporate and individual or team levels. The process is an iterative closed-loop, aimed at managing and improving individual and corporate performance through continuous adaptation to the changing operating environment (Ates et al. 2013). For SMEs, such strategy formulation enhances performance (Majama and Magang 2017; Donkor et al. 2018), and so too are environmental factors (Nwachukwu et al. 2017).

Performance appraisal and performance management involve the evaluation of employees and are interchangeably used (McMahon 2013). However, it can be argued that performance management is more expansive than performance appraisal, as the former tends to be linked with developments in areas such as coaching, competency-based appraisal, 360-degree feedback, performance pay and (of late) employee engagement (McMahon 2013) and so performance appraisal, therefore, becomes relevant to the SMEs. Torrington et al. (2014) identified the following as characteristics of performance management systems. First, performance management systems have a top-down link between business objectives and individual objectives (performance appraisal, however, may not have objectives, or the objectives may not explicitly be linked to business objectives). Second, the sole purpose of performance appraisal is to measure performance, which is but one component of performance management. Lastly, performance management is line-manager owned and driven, rather than being owned by the human resource function, as typically is the case with performance appraisal. Thus, SMEs require sound performance appraisal practices in place to realise growth.

### 2.2. Performance Appraisal Methods

There are four common performance appraisal methods. The 360-degree feedback is one of the four commonly documented performance appraisal methods used by SMEs (Chen 2011), and it involves evaluation input from many levels within the enterprise,

as well as from external sources. This technique uses ratings from several people (such as superiors and their counterparts from other departments, customers or clients and consultants), and is useful because of the wider range of performance-related feedback that it offers compared to traditional evaluation techniques (Mckenna and Beech 2013). Based on multiple source evaluations, a manager will provide feedback to the appraisee, help them to understand their strengths or shortcomings, and provide suggestions on performance improvement. A 360-degree performance review provides objective feedback and assists in identifying perception gaps (the participants' view of their performance in contrast to the views of others) (Lewis et al. 2021). This review also provides opportunities for self-assessment, allowing for self-reflection. For SMEs, 360-degree feedback helps validate the objectivity of feedback the employee receives since the supervisor includes a range of viewpoints (Dashew 2007).

The second common performance appraisal method, the key process indication, is a tool for performance evaluation that analyses key parameters of a process's input and output through proper data taking and an analysis algorithm to provide a quantitative measure for assessing the performance appraisal (Chen 2011). This method breaks the main line of business into key performance areas and analyses the key areas before coming up with the key performance indication. Key process indication decomposes the company's long-term goals into detailed and specific objectives that can be implemented. The tool helps the managers to understand the main tasks of their divisions and to set up performance appraisal criteria based on those main tasks (Chen 2011). Exploring performance appraisal in SMEs thus becomes an interesting undertaking for such firms' performance and growth.

The Balanced Scorecard (Kaplan and Norton 1992; Chen 2011) is the third appraisal method and is mostly used by better-resourced enterprises. The Balanced Scorecard is a stakeholder's perspective focused on performance management issues and operates on the assumption that for an organisation to be successful, it must satisfy the requirements of key stakeholders: investors, customers and employees (Mckenna and Beech 2013). When fully implemented, it aligns everyone within an organisation so that all employees understand how and what they can do to support the strategy (Rompho 2011). It can be used to make compensation decisions and provide feedback to management regarding the feasibility of the strategy.

The Balanced Scorecard suggests that an organisation's performance can be viewed from four main perspectives: financial, customer, internal business process and learning and growth (Rompho 2011). The four perspectives are aligned to the enterprise's strategy and create a holistic model of its strategy, thereby allowing all employees to see how they can contribute to the success of the business. The use of the Balanced Scorecard in SMEs is significantly different from that in large organisations in that the duration of each step is much shorter in smaller organisations (Rompho 2011). However, little is known regarding Balanced Scorecard effectiveness in SMEs.

The fourth appraisal method, the Management by Objectives (MBO) (Chen 2011), sometimes called management by results or results management and a work planning and review programme (Byars and Rue 2011), stresses the link between individual performance and departmental performance. The method advances the notion that subordinates should play an active role in the appraisal process to achieve a degree of commitment to the achievement of targets (Mckenna and Beech 2013). Several requirements must be met if an MBO system is to be successful. Among them is that the objectives should be quantifiable and measurable; objectives should be challenging, yet achievable, and objectives should also be expressed in writing and in clear, concise, unambiguous language (Byars and Rue 2011). However, Yongping's (2013) study on the MBO system reported that the appraisals of corporate executives contain a large number of qualitative assessment indicators that lack objectivity and are, hence, difficult to measure. Further research on the effectiveness of performance appraisal in SMEs using this method is thus called for.

### 2.3. Managerial Competencies

Chandler and Jansen (1992) posited that to be effective, a manager must be competent in interpersonal, conceptual and political competencies. Interpersonal competencies (also known as people skills, i.e., soft, human or generic skills) comprise the ability and knowledge to work with people (Sidek and Mohamad 2014). They are alternatively labelled in literature as core skills, life skills, employability skills, transferable skills, generic capabilities, generic attributes, workplace competencies, or key competencies (Vučetić 2018; Young and Chapman 2010). These competencies include individual characteristics, such as motivation, communication skills, problem-solving, or conflict resolution skills, that allow one to cope with less programmed jobs and more generic job conditions (Gawrycka et al. 2020). Interpersonal competencies benefit small enterprises in that they allow for planning, coordination and trust (Robbins and Hunsaker 2006); capacitate proprietors to understand their employees and to appreciate what motivates them (Bateman and Snell 2009); and assist proprietors to be more contemplative and self-directed (Hager et al. 2002).

Conceptual competencies involve the mental capacity to organise all an enterprise's interests and activities, the tenacity to think out of the box through engaging new thought patterns, challenging the status quo, and allowing deviations from standard operating procedures (Chandler and Jansen 1992). Managerial conceptual competencies help in planning strategically for enterprises. These competencies allow managers to evaluate circumstances and recommend alternative courses of action. Good managerial conceptual skills are critical for top management, who mostly engage in strategic planning. They also help managerial professionals envision concepts, analyse potential challenges and design creative solution.

Pertaining to political competencies, Pfeffer (1981) was amongst the first pioneers to coin the term political skill within academic literature. Pfeffer (1981) holds that political skill is needed if organisations are to be successful. Political competence is the ability to appreciate situations within or beyond one's control; the capacity to determine the time needed to take action and the capability to observe who can repel one's agenda and whom to have on one's side (Bacharach 2006). It involves one's ability to augment their position, form a power base, establish requisite connections and maintain meaningful networks with individuals or organisations that control key resources and have critical skills and abilities (Bacharach 2006; Zarook et al. 2013). SMEs with higher-level political networks report significantly higher reinvestment rates (Zarook et al. 2013).

### 2.4. Performance Appraisal, Managerial Competencies and SME Performance

Studies linking performance appraisal, managerial competencies and SMEs performance are limited. The current study sought to close such a gap in the literature. This section reviewed the few studies on this subject matter. Studies available on performance management in SMEs (Zheng et al. 2009; Chen 2011; Wijetunge 2014) suggest that SMEs face difficulties in the practice of performance management. Yet, White (2008) and Biron et al. (2011) argued that performance management systems in SMEs can result in greater financial performance, increased employee productivity and more motivated employees. The important role of firm performance and performance management in SMEs' development and growth was also demonstrated in studies by Zindiye et al. (2012) in Zimbabwe and Umer (2012) in Pakistan. However, a recent study by Mashavira (2020) on the perceived impact of performance appraisal on the performance of SMEs in Zimbabwe established a very weak and statistically insignificant relationship between performance appraisal and firm performance as measured by ROI and innovation.

Managerial competencies have also been regarded as important in determining the performance of SMEs (Sidek and Mohamad 2014; Temtime and Pansiri 2006; Kyobe et al. 2015) showed that managerial competencies among SMEs owners/managers were among the factors that caused the failure of most of these enterprises. Similarly, Tarwirei's (2015) study on the impact of managerial competencies on SMEs' performance in South Africa found that better performance by the enterprises was linked to the business and technical

competencies of managers and that their ability to outperform competitors and increase productivity depended on the managers' interpersonal competencies.

Research linking performance appraisal practices and managerial competencies, or business performance focuses on large firms and there is limited research on this linkage for SMEs in the developing countries in Africa (Abraham et al. 2001; Pekkola et al. 2016; Aleem and Rahman 2018). The under-exploration of these relationships in a country such as South Africa, where the percentage of SMEs that fail in their fifth year is as high as 50% to 95%, and where about 75% of all new small enterprises fail to become established firms (Neneh and van Zyl 2012), calls for attention. There is an argument that conclusions emanating from developed countries may not be valid for emerging markets that are characterised by institutional voids (Luo and Chung 2012). A number of studies (De Massis et al. 2015; Chirico and Bau 2014) were done in developed countries with different contextual realities from those obtained in South Africa, where levels of managerial competencies and even the conceptualisation of SMEs differ significantly. In view of this, the current study is one of the pioneers to shed light on the nexus between managerial competencies, performance appraisal and the performance of SMEs in an African country. Consequently, we hypothesised that the implementation of performance appraisal practices and appropriate managerial competencies (interpersonal, conceptual and political) correlates positively with innovation among SMEs (Hypothesis 1). Because the current study adopts a hybrid approach to measuring the performance of SMEs that includes innovation and ROI, the second hypothesis was that the implementation of performance appraisal practices and appropriate managerial competencies by SMEs correlates positively with ROI (Hypothesis 2).

### 3. Research Methodology

#### 3.1. Research Design and Approach

The study employed a structured direct survey design that involved the administration of structured questionnaires with closed-ended items (Malhotra et al. 2017). The survey method has the advantage that structured questionnaires are easily administered, and the data acquisition is consistent because the responses are limited to given responses (Malhotra et al. 2017). With closed-ended items, interaction with respondents is minimal and coding and analysis of data, and interpretation of results is simplified. Adopting controlled measurement which produces hard and reliable data afforded by quantitative research (Bryman and Bell 2015), is appropriate for this study since it allowed the use of statistical generalisation to relate findings to a larger population of SMEs (Wahyuni 2012).

#### 3.2. Research Participants and Sampling Procedure

The study adopted convenience sampling given the lack of knowledge on the actual population size or lack of sampling frame (Creswell 2012). The sample had 105 participants. Research participants were drawn from Gauteng province, South Africa's main economic hub. Five zones were identified using the Gauteng Education Department Districts List (2017) and these were Ekurhuleni, Gauteng, Johannesburg, Sedibeng and Tshwane. Given the geographical spacing of the sampling units, two trained field workers and a research company (Research IQ, Marketing Research Consulting and Training) assisted with the distribution of the questionnaires. The use of trained field workers and a professional company was meant to reduce errors in data collection. Questionnaires were delivered to respondents to be collected later.

#### 3.3. Research Instrument

The study used a structured questionnaire, and this instrument has the merit of being easily standardised, being cost effective and requiring little training of field workers (Bless et al. 2013). Closed-ended items on the structured questionnaire allowed for pre-coding of data for statistical analysis. Numerical values were assigned to Likert scale-type questions, restricted and dichotomous questions. The items allowed for measurement of performance appraisal practices, managerial competencies, ROI and innovation. Data on performance

appraisal methods used by owners/managers were as discussed in [Chen \(2011\)](#) and [Mckenna and Beech \(2013\)](#). Respondents indicated the extent to which they agreed with the statements assessing performance appraisal methods on a Likert scale, ranging from 1 (Not at all) to 5 (To a large extent). On items dealing with both managerial competencies and SME performance measures (innovation and ROI), participants showed their level of agreement, on a Likert scale, ranging from 1 (strongly disagree) to 5 (strongly agree).

### 3.4. Analytical Techniques

Descriptive statistics for the key socio-demographic characteristics of the respondents and SMEs characteristics were first computed. This was followed by Cronbach's alphas for the latent variables under consideration. Parameters for Confirmatory Factor Analysis for the measurement items of the latent variables were also calculated to assess the relevance of the items. Finally, the structural equation models, where ROI and innovation as separate endogenous outcomes, were employed to assess the influence of performance appraisal practices and managerial competencies on SME performance.

### 3.5. Validity and Reliability

To ensure content validity such that the measuring instrument provided adequate coverage of the investigative questions guiding the study ([Cooper and Schindler 2014](#)), questions were given to HR experts and experts in the SME field to be examined for bias, sequence and clarity. In addition, criteria for measuring the different constructs in the questionnaire were defined and scored in terms of literature. To correct for common method bias, more preventative procedural strategies were employed. These included a good research information coversheet, promising feedback to participants and improved scale item clarity, ([Hair et al. 2015](#)). We also used 7-point scales, 5-point scales and sometimes altered the anchors ([Griffiths et al. 2019](#)). Piloting was carried out on 40 SMEs excluded in the final study. Piloting was essential to remove possible flaws in the instrument ([Dikko 2016](#)). In terms of internal reliability, assessing the extent to which a measurement was devoid of random or unstable error ([Cooper and Schindler 2014](#)), the study employed Cronbach's alpha which is easily integrated into computer software when quantitatively analysing data ([Bryman and Bell 2015](#)).

### 3.6. Ethical Considerations

The Ethics Committee in the Faculty of Management, Central University of Technology in Free State (reference number 15/10/2015) approved the study and informed consent was obtained from all the respondents. Respondents were provided with the information leaflet about the study. To ensure the anonymity and confidentiality of respondents, no information that identified individuals participating in the study was collected.

## 4. Results

### 4.1. Firm Characteristics and Respondents' Socio-Demographics

The summary of the respondents' characteristics (Table 1) shows that seven in every ten respondents were males: almost four in every ten of these respondents were owners of the business in consideration and likewise, almost four in every ten were managers in the business. Sixty-one percent of the enterprises were non-family owned (NFOSME) and the remaining 39% were family-owned (FOSME). As expected for SMEs, about two-thirds of the enterprises did not have a designated Human Resources (HR) Department such that the Owner who doubles up as the manager (76%) or ordinary manager (10%) handled HR affairs. In some instances (8%), the accountants handled HR affairs. About 45% of the respondents were not related to the owner of the business, while about 42% were the owners of the business. Only 11% of the respondents were related to the owners of the business. In terms of the education level of the respondents, a substantial number had either secondary schooling (38%) or a diploma (45%). With respect to race, black Africans (56%) and Whites (25%) dominated the sample. In these SMEs, on average, four employees were related, SMEs had an average of



40 employees, had operated for an average of 14 years and the respondents' average age was 40 and they had been with the enterprise for an average of nine years.

**Table 1.** Respondent's socio-demographics and firm's characteristics.

Socio-Demographics/Characteristics		%	Sample (n)		
Gender	Male	70.48	105		
	Female	29.52			
	Total	100.00			
Position in company	Owner	39.05	105		
	Company Manager	39.05			
	HR Manager	6.67			
	Owner-manager	5.71			
	Other	9.52			
Total	100.00				
Ownership	FOSME	38.83	103		
	NFOSME	61.17			
	Total	100.00			
Firm has HR department	Yes	33.65	104		
	No	66.35			
	Total	100.00			
Relationship to owner	Owner	42.72	103		
	Family member	11.65			
	Not related to owner	45.63			
	Total	100.00			
Who handles HR issues	Owner-manager	76.06	71		
	Manager	9.86			
	Personal Assistant	2.82			
	Accountant	8.45			
	Outsourcing	2.82			
Total	100.00				
Education	Primary	0.96	104		
	Secondary	37.50			
	Diploma	45.19			
	Degree	13.46			
	Honours/Masters	1.92			
	Other	0.96			
Total	100.00				
Race	Black African	56.19	105		
	White	24.76			
	Coloured	4.76			
	Indian	12.38			
	Other	1.90			
Total	100.00				
Characteristics	Mean	Standard Deviation	Minimum	Maximum	Sample (n)
Related employees	4.26	5.86	1	36	39
No. employees	40.80	48.88	5	200	105
Operating period (years)	13.55	12.83	1	90	103
Respondent's age	40.06	13.12	1	98	99
Years in company	8.77	8.13	1	52	102

#### 4.2. Measurements Reliability

To assess the relevance of the items for each latent variable, factor analysis was carried out to assess the factor loadings. Cronbach alphas were computed and as is shown in Table 2, all the variables had satisfactory alpha values (greater than the minimum 0.70). Parameters assessing the appropriateness of Confirmatory factor analysis are also reported in Table 2. For almost all the latent variables, two or more parameters satisfied the requirements suggesting that the models that used the measurement items for latent variables appropriately. Thus, the structural models employed the performance appraisal practices variable, two performance measures (Innovation and ROI) and three components of managerial competencies (i.e., interpersonal, conceptual and political competencies).

**Table 2.** Cronbach alphas and Confirmatory Factor Analysis parameters.

Latent Variable	Alpha Value	Confirmatory Factor Analysis Parameters		
		Chi2 ( <i>p</i> -Value)	Root Mean Square Error of Approximation	Comparative Fit Index
Performance appraisal practices (Pap)	0.80	1.50 (0.47)	0.00	1.00
Innovation (Inn)	0.88	26.61 (0.00)	0.28	0.95
Return on Investment (ROI)	0.90	4.62 (0.10)	0.11	1.00
Interpersonal competence (Ic)	0.86	16.29 (0.13)	0.07	0.98
Conceptual competence (Cc)	0.92	281.34 (0.00)	0.10	0.87
Political competence (Pc)	0.80	19.46 (0.11)	0.07	0.97

Note: Alpha minimum value standard was 0.70; recommended Confirmatory Factor Analysis parameters: insignificant Chi2, recommended Root mean square error in approximation was 0.08, cut off value for comparative fit index was 0.90 or 0.95.

#### 4.3. Innovation, Performance Appraisal Practices and Managerial Competencies

The identified items for each of the latent variables were highly significant (Table 3). Performance appraisal practices had four items. The items summarizing performance appraisal practices were the use of a grading system, employing cost-benefit analysis to keep employees, use of written records of critical incidents of favourable and unfavourable employee work actions and the ranking of employees. The four items significantly correlated with the performance appraisal practices variable in the structural model.

Innovation had six items that were summarised by the designing of new products in two consecutive years, initiating unique improvements to product features in two consecutive years and improving production processes in two consecutive years. All the six items were fundamental in measuring innovation in the SMEs and were statistically significant ( $p < 0.001$ ).

**Table 3.** Influence of managerial competencies and performance appraisal on firm innovation.

Structural	Coefficient
<b>Firm performance—Innovation (Inn):</b>	
Managerial competencies (Mc)	0.99 ***
Performance appraisal practices (Pap)	0.09
<b>Managerial competencies (Mc):</b>	
Interpersonal competence (Ic)	0.72 ***
Conceptual competence (Cc)	−0.26
Political competence (Pc)	0.29
<b>Measurement for Performance appraisal practices (Pap):</b>	
Using a grading system when rating employees (gs)	0.76 ***
A cost and benefit analysis of keeping the employee (cb)	0.82 ***
Using a written record of critical incidents of favourable and highly unfavourable employee work actions (wr)	0.48 ***
Placing all employees from a group in rank order of overall performance (pe)	0.63 ***
<b>Measurement for Innovation (Inn):</b>	
Our firm designed new products in 2015 (in15)	0.65 ***
Our firm designed new products in 2016 (in16)	0.86 ***
Owner/managers initiated unique improvements to product features in 2015 (pf15)	0.61 ***
Owner/managers initiated unique improvements to product features in 2016 (pf16)	0.84 ***
Our firm improved its production processes in 2015 (pp15)	0.76 ***
Our firm improved its production processes in 2016 (pp16)	0.83 ***
<b>Measurement for Interpersonal competencies (Ic):</b>	
I communicate in a supportive way when employees share their problems with me (ic1)	0.81 ***
I motivate and energise others to do a better job (ic2)	0.68 ***
I make sure that employees at the business are provided with opportunities for personal development (ic3)	0.71 ***
I insist on intense hard work and high productivity from my subordinates (ic4)	0.64 ***
I make sure that sufficient attention is given to interpersonal relationships (ic5)	0.81 ***
I clarify to employees what is expected of them (ic6)	0.52 ***
I listen openly and attentively to others who give me ideas, even if I disagree (ic7)	0.68 ***
<b>Measurement for conceptual competencies (Cc):</b>	
I build cohesive, committed groups of people (cc1)	0.64 ***
I give employees, regular feedback about how they're doing (cc2)	0.67 ***
I articulate a clear vision of what can be accomplished in the future (cc3)	0.78 ***
I ensure that regular assessments occur at the business (cc4)	0.78 ***
I facilitate effective information sharing and problem-solving in the business (cc5)	0.72 ***
I keep close track of how units are performing (cc6)	0.76 ***
I establish ambitious goals that challenge employees to achieve performance levels above the standard (cc7)	0.66 ***
I regularly come up with new, creative ideas regarding processes and products for the business (cc8)	0.53 ***
I am always working to improve the processes we use to achieve our desired output (cc9)	0.64 ***
I push others to achieve world-class competitive performance in products (cc10)	0.50 ***
I try my best to be ethical in my business conduct (cc11)	0.53 ***
I make sure that we assess how well we are meeting our customers' expectations (cc12)	0.46 ***
I create a climate where employees want to achieve higher levels of performance than the competition (cc13)	0.55 ***
I facilitate a climate of continuous improvement at the business (cc14)	0.58 ***
I make certain that all employees are clear about our policies, values and objective (cc15)	0.49 ***
I routinely share information across functional boundaries at the business to facilitate coordination (cc16)	0.64 ***
I initiate cross-functional teams or task forces that focus on important issues (cc17)	0.75 ***
I have developed a clear strategy for helping the business successfully accomplish my vision of the future (cc18)	0.79 ***
I create an environment where creativity is rewarded (cc19)	0.65 ***
<b>Measurement for political competencies (Pc):</b>	
I involve customers in our evaluations (pc1)	0.65 ***
I delegate some tasks but still closely monitor their execution (pc2)	0.69 ***
I coordinate regularly with managers in other units at the business (pc3)	0.59 ***
I always monitor and adapt to the regulatory, political and economic environments (pc4)	0.39 ***
I am good at establishing the right connections with stakeholders like suppliers, financiers, politicians and customers (pc5)	0.76 ***
I have consistent and frequent personal contact with my external customers (pc6)	0.32 ***
I create an environment where involvement and participation in decisions are encouraged (pc7)	0.65 ***
I attend to corporate social responsibility concerns (pc8)	0.58 ***

Notes: Structural Equation Modelling; Estimation method was maximum likelihood; No. of observations = 95; The results and significance shown here are for the standardised solution; Iterative (100) applied to force concavity; \*\*\*  $p < 0.001$ .

All the seven items for interpersonal competencies were statistically significant. For the SMEs in the study, the owners/managers' interpersonal competencies were measured by supportive communication, ways of motivating, provision of personal development,

insisting on intense hard work, supporting interpersonal relations, clarifying what is expected of employees and listening to all staff members.

Conceptual competence was measured using a wide range of items and Table 3 shows that all were statistically significant ( $p < 0.001$ ). It comprised cohesiveness, regular feedback, vision articulation, regular assessment, information sharing, tracking different units' performance, establishing ambitious goals, new and creative ideas, pushing for world-class competitive performance and ethical conduct. In addition, the measures included meeting customer expectations, a conducive climate for higher performance and continuous improvement, clear policies, information sharing across function boundaries, facilitating cross-functional teams, clear strategy and creativity rewarding.

The third component of managerial competencies was political competence. This comprises eight items, and all were statistically significant. Thus, a sound political competence was measured by allowing customer evaluations, task delegation, clear coordination with other units, adaptation to the political-economic environment, right connections with stakeholders, personal contact with external customers, encouraging the involvement of all in decision making, and attending to corporate social responsibility.

Interpersonal competence, conceptual competence and political competence were hypothesised to explain managerial competencies in SMEs. Only the Interpersonal competencies emerged as statistically significant ( $p < 0.001$ ). In turn, managerial competencies and performance appraisal practices were assessed to check on their influence on firm performance in form of innovation. Managerial performance influenced firm performance and was statistically significant ( $p < 0.001$ ). However, performance appraisal practices did not matter in explaining firm performance as measured by innovation. Figure A1 provides the Conceptual model for the results presented in Table 3.

#### 4.4. ROI, Performance Appraisal Practices and Managerial Competencies

The study also employs ROI as another measure of firm performance and Table 4 provides the results of that analysis. As with Table 3, the latent variables (managerial competencies and performance appraisal) were used in the analysis.

**Table 4.** Influence of managerial competencies and performance appraisal practices on firm's ROI.

Structural	Coefficient
<b>Firm performance—Return on Investment (ROI):</b>	
Managerial competence (Mc)	0.64 ***
Performance appraisal practices (Pap)	0.03
<b>Managerial competencies (Mc):</b>	
Interpersonal competence (Ic)	0.84 ***
Conceptual competence (Cc)	0.12
Political competence (Pc)	−0.17
<b>Measurement for Performance appraisal practices (Pap):</b>	
Using a grading system when rating employees (gs)	0.77 ***
A cost and benefit analysis of keeping the employee (cb)	0.82 ***
Using a written record of critical incidents of favourable and highly unfavourable employee work actions (wr)	0.49 ***
Placing all employees from a group in rank order of overall performance (pe)	0.63 ***
<b>Measurement for ROI:</b>	
The firm posted net profits in 2015 (np15)	0.69 ***
The firm posted net profits in 2016 (np16)	0.56 ***
The firm's income outweighed expenditure in 2015 (ie15)	0.89 ***
This firm's income outweighed expenditure in 2016 (ie16)	0.86 ***
This firm's overall returns exceeded overall costs in 2015 (rc15)	0.91 ***
This firm's overall returns exceeded overall costs in 2016 (rc16)	0.88 ***

Table 4. Cont.

Structural	Coefficient
<b>Measurement for Interpersonal competence (Ic):</b>	
I communicate in a supportive way when employees share their problems with me (ic1)	0.80 ***
I motivate and energise others to do a better job (ic2)	0.72 ***
I make sure that employees at the business are provided with opportunities for personal development (ic3)	0.70 ***
I insist on intense hard work and high productivity from my subordinates (ic4)	0.64 ***
I make sure that sufficient attention is given to interpersonal relationships (ic5)	0.79 ***
I clarify to employees what is expected of them (ic6)	0.51 ***
I listen openly and attentively to others who give me ideas, even if I disagree (ic7)	0.68 ***
<b>Measurement for conceptual competence (Cc):</b>	
I build cohesive, committed groups of people (cc1)	0.65 ***
I give employees, regular feedback about how they're doing (cc2)	0.67 ***
I articulate a clear vision of what can be accomplished in the future (cc3)	0.76 ***
I ensure that regular assessments occur at the business (cc4)	0.76 ***
I facilitate effective information sharing and problem solving in the business (cc5)	0.72 ***
I keep close track of how units are performing (cc6)	0.75 ***
I establish ambitious goals that challenge employees to achieve performance levels above the standard (cc7)	0.65 ***
I regularly come up with new, creative ideas regarding processes and products for the business (cc8)	0.50 ***
I am always working to improve the processes we use to achieve our desired output (cc9)	0.62 ***
I push others to achieve world-class competitive performance in products (cc10)	0.47 ***
I try my best to be ethical in my business conduct (cc11)	0.56 ***
I make sure that we assess how well we are meeting our customers' expectations (cc12)	0.45 ***
I create a climate where employees want to achieve higher levels of performance than the competition (cc13)	0.55 ***
I facilitate a climate of continuous improvement at the business (cc14)	0.58 ***
I make certain that all employees are clear about our policies, values and objectives (cc15)	0.48 ***
I routinely share information across functional boundaries at the business to facilitate coordination (cc16)	0.62 ***
I initiate cross-functional teams or task forces that focus on important issues (cc17)	0.73 ***
I have developed a clear strategy for helping the business successfully accomplish my vision of the future (cc18)	0.77 ***
I create an environment where creativity is rewarded (cc19)	0.65 ***
<b>Measurement for political competence (Pc):</b>	
I involve customers in our evaluations (pc1)	0.64 ***
I delegate some tasks but still closely monitor their execution (pc2)	0.67 ***
I coordinate regularly with managers in other units at the business (pc3)	0.59 ***
I always monitor and adapt to the regulatory, political and economic environment (pc4)	0.38 ***
I am good at establishing the right connections with stakeholders like suppliers, financiers, politicians and customers (pc5)	0.76 ***
I have consistent and frequent personal contact with my external customers (pc6)	0.34 ***
I create an environment where involvement and participation in decisions are encouraged (pc7)	0.66 ***
I attend to corporate social responsibility concerns (pc8)	0.59 ***

Notes: Structural Equation Modelling; Estimation method was maximum likelihood; No. of observations = 94; The results and significance shown here are for the standardised solution; Iterative (100) applied to force concavity; \*\*\*  $p < 0.001$ .

Table 4 clearly shows that the items for performance appraisal practices, components of managerial competencies and ROI were all significant ( $p < 0.001$ ). However, when assessing the significance of interpersonal, conceptual and political competencies as factors explaining managerial competencies, only the interpersonal competence was significant. In turn, managerial competencies statistically and significantly ( $p < 0.001$ ) explained the ROI of the enterprises.

### 5. Discussion

While managerial competencies, as a latent variable, correlated significantly with both innovation and ROI (outcome variables), performance appraisal practices did not show any significant correlation with the variables. The insignificant performance appraisal practices finding in the current study differed from similar studies by [Aleem and Rahman \(2018\)](#), [Jamsari et al. \(2017\)](#) and [Nongmaithem and Kassa \(2016\)](#). These studies reported a positive association between performance appraisal practices and an enterprise's perceived business

performance. The fact that performance appraisal practices used by South African SMEs did not show any significant correlation with the two outcome variables could be attributed to overreliance on informal appraisal methods, which because of lack of documentation, may lead to a lack of accountability among employees. The other possible explanation is that some performance appraisal practices initially meant for large corporations were adopted by SMEs wholly; yet their contextual realities differed from the bigger companies. Cognisant of the fact that organisational settings between large companies and SMEs differ, and that these enterprises are not smaller versions of large firms, SMEs need support and cultivation to implement appropriate appraisal methods (Pekkola et al. 2016).

Regarding managerial competencies, it was the interpersonal competencies that explained managerial competencies in the current study. Yet, Ikupolati et al. (2017) established that conceptual competencies made entrepreneurs become more goal-driven and boosted their self-confidence. In addition, Katz (2009) observed that appreciating relationships (as afforded by conceptual skills) among a business's parts enabled entrepreneurs to act in ways that advance the overall welfare of the business. Similarly, having connections in the right places (afforded by political competencies) determines an entrepreneur's access to capital, business permits, raw materials and the prices for such (Hoffman and Lange 2016), yet the current study reported interpersonal competence as the only significant component in explaining managerial competencies.

The current study has five key limitations. First, SMEs suffer from poor record-keeping and informal operation leading to responses informed by individual memory as opposite to documented facts. Innovative methods of assessing performance appraisal practices, managerial competencies and the performance of SMEs that can address such challenges can be considered in the future. Second, data for the current study were collected cross-sectionally, although longitudinal data could also measure the variables under consideration and produce more nuanced results. Third, conceptualisations of SMEs differ from country to country and from industry to industry such that viewing SMEs as a homogenous lot is problematic. Abouzeedan (2011) emphasised the importance of a firm's age, size, location and business sector when categorising SMEs. Studies of this nature, when carried out at a larger scale, could allow for sub-group analysis of SMEs based on the age, size, location and business sector factors. Fourth, research participants were drawn from the Gauteng province, yet national studies could produce more robust results. Finally, it is worth noting that other methods of appraising employee performance, such as the assessment centre method, essay evaluation and paired comparison, among others, have lately been recommended for start-ups and small businesses (Roychoudhuri 2018). Future studies could consider the above-mentioned methods.

## 6. Conclusions

The study established that whereas managerial competencies correlated significantly with both innovation and ROI as measures of firm performance, performance appraisal practices did not show such correlation. The significance of managerial competencies was driven by the interpersonal competencies only and not by the other two competencies. Thus, people skills, including individual attributes such as personality traits, motivation and attitudes were instrumental among owners/managers in South African SMEs. South African SMEs failed to leverage their performance on the performance appraisal practices in use.

**Author Contributions:** Conceptualization, N.M., S.G. and C.C.; Formal analysis, S.G.; Funding acquisition, S.G. and C.C.; Investigation, N.M. and C.C.; Methodology, N.M. and S.G.; Project administration, N.M.; Supervision, C.C.; Writing—original draft, N.M.; Writing—review & editing, S.G. and C.C. All authors have read and agreed to the published version of the manuscript.

**Funding:** The Central University of Technology, South Africa funded data collection, and both the Central University of Technology, South Africa and the University of the Free State, South Africa funded the article processing charges.

**Institutional Review Board Statement:** The study was conducted according to the guidelines of the Declaration of Helsinki and approved by the Central University of Technology’s (Bloemfontein) Faculty of Management Ethics Committee (Approval No: 15/10/2015).

**Informed Consent Statement:** Informed consent was obtained from all subjects in the study.

**Data Availability Statement:** Data are available and can be obtained from the authors upon request.

**Acknowledgments:** The researchers would like to thank the two research assistants—former HR students at Great Zimbabwe University, Zimbabwe, who assisted in data collection. A research company (Research IQ, Marketing Research Consulting and Training) also assisted in the distribution of questionnaires.

**Conflicts of Interest:** The authors declare no conflict of interest.

Appendix A

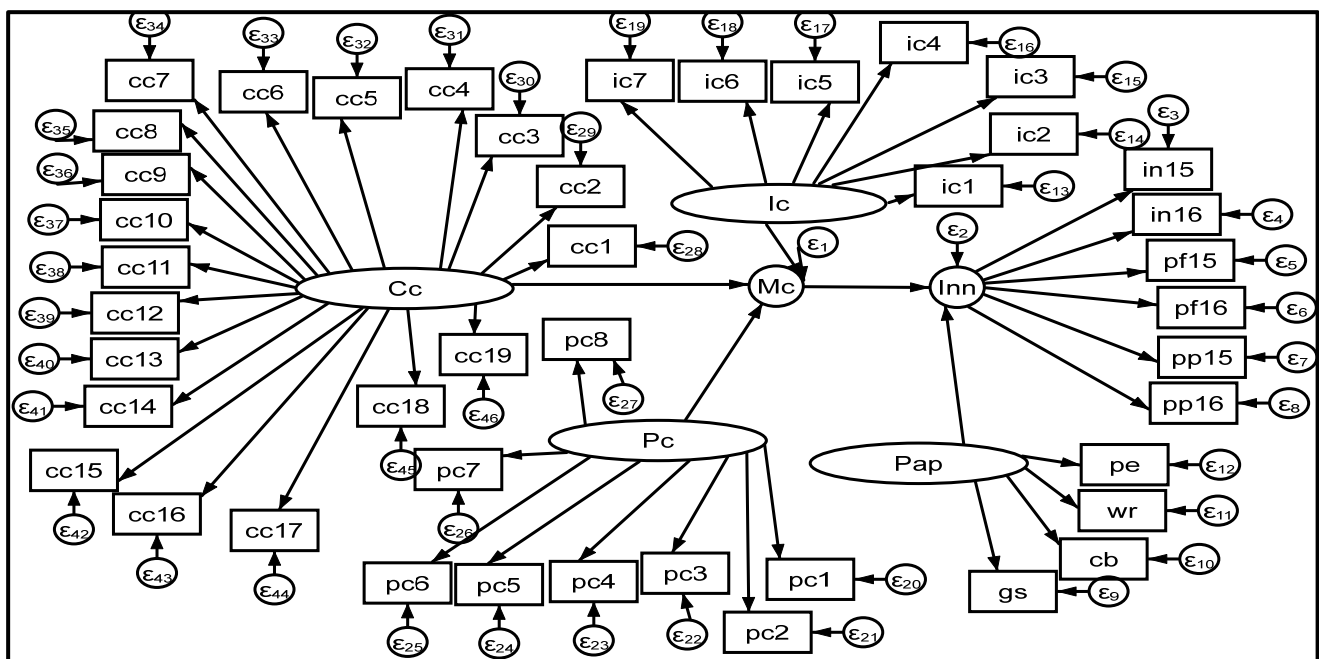
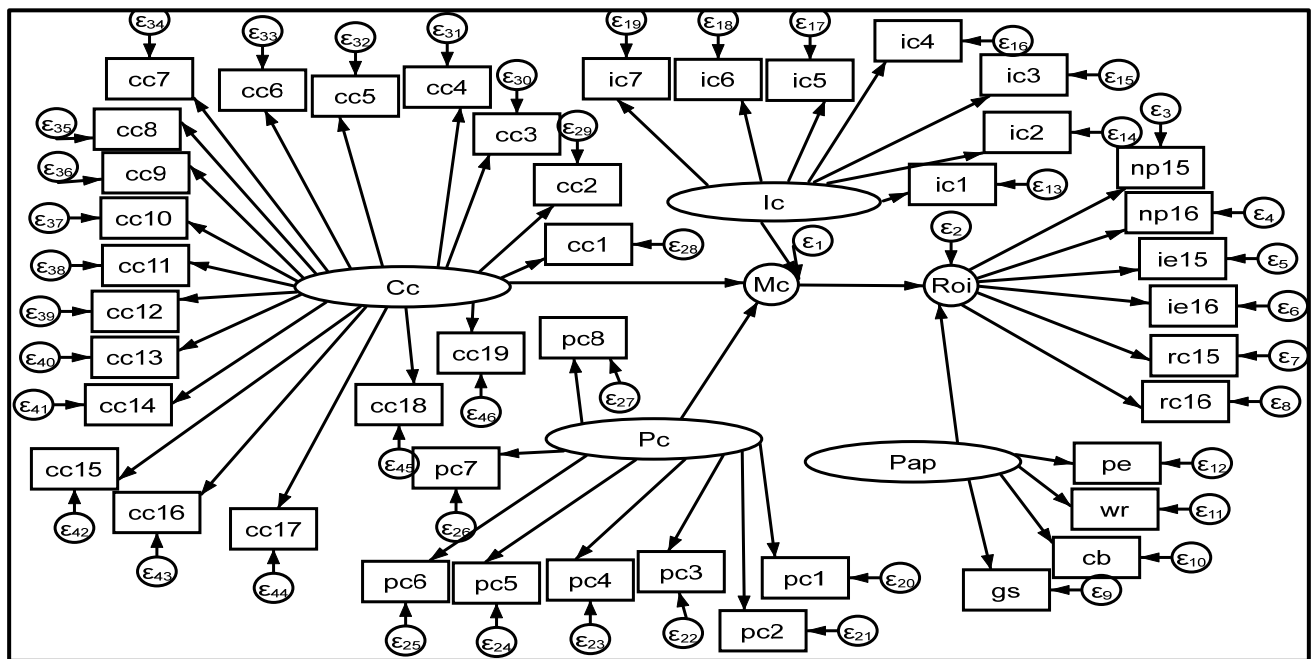


Figure A1. Structural Equation Model (SEM) conceptual framework for innovation as a measure of performance. Note: Definitions of the variable acronyms are provided in Table 3 in the text.



**Figure A2.** Structural Equation Model (SEM) conceptual framework for return on investment as a measure of performance. Note: Definitions of the variable acronyms are provided in Table 4 in the text.

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