

THE INFLUENCE OF HUMAN RESOURCES MANAGEMENT  
PRACTICES AND GOVERNMENTAL SUPPORT ON  
ORGANIZATIONAL PERFORMANCE IN SMALL  
MANUFACTURING BUSINESSES IN MALAYSIA

YUSRA YASEEN LAZIM

Thesis submitted in fulfillment of the requirements  
for the award of the degree of  
Doctor of Philosophy in Technology Management

Faculty of Industrial Management  
UNIVERSITI MALAYSIA PAHANG

March 2015

## **ABSTRACT**

This study focuses on four knowledge fields (Human Resources Management, Employee Outcomes, Governmental Support, and Organizational Performance) which have been the center and attraction for many researches and studies. The growing awareness of the crucial role of human capital as the engine of organizations to sustain the competitive advantage, and the management of this worthy resource can lead to success. Pursuant to these facts, human resource management and governmental support are two of the most significant factors that considered having decisive influence on the organizational performance of small businesses. The main objectives of this study are: First, to assess the effect of human resources management practices on the organizational performance of small businesses through examining the causal order of the main variables (Human Resources Management, Employee Outcomes, and Organizational Performance) in an attempt to unfold the so-called “Black Box” to clarify the ambiguous relationship between human resources management practices and organizational performance; Second, to assess the vital contribution of governmental support to the organizational performance of small businesses. To achieve these objectives, a quantitative research study was conducted on a sample consist of 265 small businesses working in manufacturing sector/ Malaysia. Structural Equation Modelling with Amos 20 was used as an advanced quantitative measure beside other statistical measures in order to attain the prior objectives. The main findings of the study were; the existence of a significant relationship between human resources management practices as one “bundle” and organizational performance, and significant relationships between the component of employee outcomes (Trust in management, Cooperation, Intention to turnover, and Effort and involvement) and both human resources management practices and organizational performance. Also, there is a positive relationship between governmental support and organizational performance of small businesses.

## ABSTRAK

Kajian ini memberi tumpuan kepada empat bidang pengetahuan (Pengurusan Sumber Manusia, Hasil Pekerja, Sokongan Kerajaan, dan Prestasi Organisasi) yang telah menjadi pusat dan tarikan untuk banyak penyelidikan dan kajian. Kesedaran yang semakin meningkat terhadap peranan penting modal insan sebagai enjin organisasi untuk mengekalkan kelebihan daya saing, dan pengurusan sumber yang amat bernilai ini boleh membawa kepada kejayaan. Selaras dengan fakta-fakta ini, pengurusan sumber manusia dan sokongan kerajaan adalah dua faktor paling penting yang dianggap mempunyai pengaruh yang kuat ke atas prestasi organisasi perniagaan kecil. Objektif utama kajian ini adalah: Pertama, untuk menilai kesan amalan pengurusan sumber manusia ke atas prestasi organisasi perniagaan kecil melalui kajian sebab dan akibat bagi pembolehubah utama (Pengurusan Sumber Manusia, Hasil Pekerja, dan Prestasi Organisasi) dalam usaha untuk membuka apa yang dikenali sebagai "Kotak Hitam" untuk menjelaskan hubungan kabur di antara amalan pengurusan sumber manusia dan prestasi organisasi; Kedua, untuk menilai sumbangan penting sokongan kerajaan terhadap prestasi organisasi perniagaan kecil. Untuk mencapai objektif ini, satu kajian penyelidikan kuantitatif telah dijalankan ke atas sampel yang terdiri daripada 265 perniagaan kecil yang bekerja dalam sektor pembuatan / Malaysia. Persamaan Permodelan Struktur dengan Amos 20 telah digunakan sebagai kaedah ukuran kuantitatif selain lain-lain kaedah statistik bagi mencapai objektif kajian. Penemuan utama kajian ini ialah; kewujudan hubungan yang signifikan di antara amalan pengurusan sumber manusia sebagai salah satu "ikatan" dan prestasi organisasi, dan hubungan yang signifikan antara komponen hasil pekerja (amanah dalam pengurusan, kerjasama, niat untuk berhenti, dan usaha dan penglibatan) dan kedua-dua pengurusan sumber manusia amalan dan prestasi organisasi. Selain itu, terdapat hubungan yang positif antara sokongan kerajaan dan prestasi organisasi perniagaan kecil.

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## LIST OF ABBREVIATIONS

C	Cooperation
EI	Involvement
E.O	Employee Outcome
EO	Effort and Involvement
EU	<i>European Union</i>
GDP	Gross Domestic Product
GR/ Gov.	Governmental Support
GRF	Financial Governmental Support
GRN	Nonfinancial Governmental Support
HRD	Human Resources Development
HRM	Human Resources Management
HRMM	HRM (Management Practices)
HRMR	HRM (Retention & Motivation Practices)
HRMS	HRM (Selection Practices)
IFC	<i>International Finance Corporation</i>
ITT	Intention to Turnover
MECD	Ministry of Entrepreneur and Cooperative Development
NSDC	National SME Development Council
OECD	Organization for Economic Co-operation and Development
O.P	Organizational Performance
OPF	Organizational Performance (Financial)
OPO	Organizational Performance (Operational)
SMIDEC	Small and Medium Industries Development Corporation
TIM	Trust in Management

UNIDO

United Nations Industrial Development Organization

# **CHAPTER 1**

## **INTRODUCTION**

### **1.1 INTRODUCTION**

All economic point of views have shown consensus about the growing importance of small business, whether in the industrially developed countries or developing countries. Several statistics indicate that these businesses represent more than 90% of the total number of the enterprises in developing countries (Hashim, and Abdullah, 2000).

In Malaysia, The importance of small businesses rises through its active contribution in generating income and value-added. In 2003, small businesses achieved a net income of RM 405 billion and RM 154 billion value added (UNDP, 2007). The latest statistics indicate that SMEs contribute 99.2% of the total business establishments, and contribute about 32% of GDP and 59% of total employment (SME Annual Report, 2010/11).

Currently, small businesses are facing many challenges and problems due to rapid environmental changes represented by the diversity of the labour market, development of information systems, globalization, and the constant change in product demands. These hasty changes are confronted by the inability of most of these businesses to keep up with

these changes as well as utilizing them in their favour, due to the weakness of available resources for small businesses such as (necessary funding, advanced information system and active human resource).

To success, small businesses must have the ability to improve performance by creating products and new work strategies, reducing costs, improving quality and productivity through using available resources and facilities such as the human resources by focusing on the ways and means that can help improve the ability of the workforce (Luthans and Sommers, 2005).

Many researchers have interested in HRM of small businesses because of its decisive influence on creating and increasing knowledge, motivation, trust, involvement and commitment, which is reflected in turn as a source of sustainable competitive advantage. Huselid (1995) has confirmed the fact that HRM practices represent a single path that can be used by businesses to conform attitudes and behaviours of their employees in order to serve the desired goals through the creation of conditions that make their employees on a high degree of engagement and thus making all efforts to achieve the organizational objectives.

Studies mostly concentrated on HRM and its impact over organizational performance in large firms (Delancy and Huselid, 1996; Huselid, 1995; Paul and Anantharaman, 2003 and Dean Hartog and Verburg, 2004). However, few studies have looked at the influence of HRM practices over organizational performance in small businesses (Collins et al., 2004, 2005 and Tiwari, 2012).

The importance of HRM practices lies in their power to influence the organizational performance not directly but through the positive influence on the employees' performance known as (employee outcomes). Many studies have been conducted to examine the relationship between HRM practices and employee outcomes which tend to have influence on the organizational performance, but a few of those studies were dedicated to small businesses. The studies were devoted to examining the relationship between HRM practices and one variable of the employee outcomes such as trust, commitment, engagement and involvement (Collins et al., 2005; Huselid, 1995; Becker and Huselid, 1998; Wright and Snell, 1998 and Guest, 2000).

Study by Collins et al. (2005) in Cornell University/ New York along with Gevity institution is regarded as a pioneer study that highlighted the importance of human resources in small businesses, and on the effective strategies followed by HRM in these businesses and their impact on the employee outcomes and then on the organizational performance. Based on Cornell University study, the main objective of this study is to examine the relationship between HRM practices and organizational performance of small businesses through the mediator variables; Trust in management, cooperation, Intention to turnover, and effort and involvement (employee outcomes).

In spite of the growing importance of small businesses in the economies of most countries in the world, these businesses suffer many difficulties that limit their capabilities to succeed and withstand the challenges faced and which sometimes lead many to fail and withdraw from the market. These problems are seen in the difficulties of obtaining the necessary funding, legal restrictions and bureaucratic procedures and lack of managerial qualifications, and the difficulty to take advantage of opportunities for innovation due to lack of the necessary skills to turn creative ideas into commercial products that bring profit back to the businesses (Vinnell and Hamilton, 1999 and Cosh and Hughes, 2003). Most countries (developed, transitional, and developing countries) undertook to put forward various programs and policies to support small businesses in order to improve their ability to grow and step up their performance in innovation, promoting managerial skills, and to adopt the best practices to improve the efficiency of their human resources.

Malaysia has achieved many national development goals and nearly all of the Millennium Development Goals (MDGs), for example the MDGs target to reduce the proportion of the population living below the poverty line by 50% between 1990 and 2015 was achieved in 1999, when the poverty rate fell from 16.5% in 1990 to 7.5%. By 2006 the poverty rate was just 5%. The growth and development of small businesses in Malaysia have contributed significantly in creating employment and thus in reducing the poverty rate (Malaysia SME Business Directory, 2010). The full realization of the importance of small businesses may incite the government to set up several institutions, incubation centres and banks allocated to these businesses, such as NSDC, SMIDEC, MECD, HRD portal.

Malaysia has given priority to small businesses and developed policies that meet the development needs. Strategies of the Eighth Malaysia Plan (2001-2005) have focused on the



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Studies mostly concentrated on HRM and its impact over organizational performance in large firms (Delancy and Huselid, 1996; Huselid, 1995; Paul and Anantharaman, 2003 and Dean Hartog and Verburg, 2004). However, few studies have looked at the influence of HRM practices over organizational performance in small businesses (Collins et al., 2004, 2005 and Tiwari, 2012).

The importance of HRM practices lies in their power to influence the organizational performance not directly but through the positive influence on the employees' performance known as (employee outcomes). Many studies have been conducted to examine the relationship between HRM practices and employee outcomes which tend to have influence on the organizational performance, but a few of those studies were dedicated to small businesses. The studies were devoted to examining the relationship between HRM practices and one variable of the employee outcomes such as trust, commitment, engagement and involvement (Collins et al., 2005; Huselid, 1995; Becker and Huselid, 1998; Wright and Snell, 1998 and Guest, 2000).

Study by Collins et al. (2005) in Cornell University/ New York along with Gevity institution is regarded as a pioneer study that highlighted the importance of human resources in small businesses, and on the effective strategies followed by HRM in these businesses and their impact on the employee outcomes and then on the organizational performance. Based on Cornell University study, the main objective of this study is to examine the relationship between HRM practices and organizational performance of small businesses through the mediator variables; Trust in management, cooperation, Intention to turnover, and effort and involvement (employee outcomes).

In spite of the growing importance of small businesses in the economies of most countries in the world, these businesses suffer many difficulties that limit their capabilities to succeed and withstand the challenges faced and which sometimes lead many to fail and withdraw from the market. These problems are seen in the difficulties of obtaining the necessary funding, legal restrictions and bureaucratic procedures and lack of managerial qualifications, and the difficulty to take advantage of opportunities for innovation due to lack of the necessary skills to turn creative ideas into commercial products that bring profit back to the businesses (Vinnell and Hamilton, 1999 and Cosh and Hughes, 2003). Most countries (developed, transitional, and developing countries) undertook to put forward various programs and policies to support small businesses in order to improve their ability to grow and step up their performance in innovation, promoting managerial skills, and to adopt the best practices to improve the efficiency of their human resources.

Malaysia has achieved many national development goals and nearly all of the Millennium Development Goals (MDGs), for example the MDGs target to reduce the proportion of the population living below the poverty line by 50% between 1990 and 2015 was achieved in 1999, when the poverty rate fell from 16.5% in 1990 to 7.5%. By 2006 the poverty rate was just 5%. The growth and development of small businesses in Malaysia have contributed significantly in creating employment and thus in reducing the poverty rate (Malaysia SME Business Directory, 2010). The full realization of the importance of small businesses may incite the government to set up several institutions, incubation centres and banks allocated to these businesses, such as NSDC, SMIDEC, MECD, HRD portal.

Malaysia has given priority to small businesses and developed policies that meet the development needs. Strategies of the Eighth Malaysia Plan (2001-2005) have focused on the

## **CHAPTER 3**

### **METHODOLOGY**

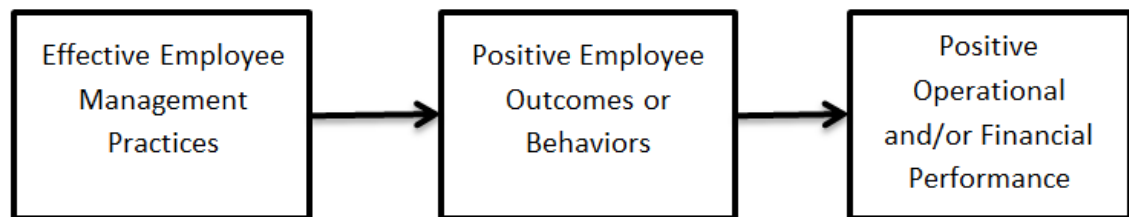
#### **3.1 INTRODUCTION**

This chapter describes the overall research methodology used to solve research problem. The model of study, measurement of variables, and hypotheses used in this study will be presented. Also illustrate the target population, the sample of study, the instrument used to collect the data, and questionnaire design. Finally, demonstrate of the statistical analysis technique utilized in this study.

#### **3.2 MODEL OF THE STUDY**

Numerous studies and researches that concern with the importance of small businesses and the methods of attention and sponsorship of small businesses have been conducted in the different countries of the world, due to the fact that small businesses from the foundation stone in the process of economic and social advancement. This study consists of two parts; the first part is devoted to examining the causal order of the relationship between HRM practices and organizational performance by illuminating the indirect influence of the mediating variables that is so-called employee outcomes. The second part of the study is dedicated to highlight the vital role of governmental support for small businesses,

through testing the direct relationship between governmental support and organizational performance. The model of this study had been adapted from the earliest model developed by Cornell University/ New York and Gevity institution (see figure 3.1). The model had been examined on a sample of small businesses in USA in 2005. In 2007 the model had been tested on a sample of small businesses by the researcher in Iraq.



**Figure 3.1:** Basic Model of Cornell University

Source: Collins et al. (2005)

As there is no consensus about a standard set of HRM practices in the HRM literature, three groups of practices has been identified as one bundle that may affect firstly on employee outcomes, then indirectly effect on organizational performance. So in this study, three different HRM practices (sub- bundles of HRM practices) would be examined to clarify their effects on organizational performance. These sub- bundle of HRM practices are: selection practices, management practices, and retention and motivation practices.

Many previous researches examined the relationship between either the whole system of HRM practices and organizational performance or selected individual HRM practices and organizational performance. Becker and Huselid (1998) indicated that it is more suitable to study the influence of HRM practices on organizational performance simultaneously in one model, because examining the effect of each element in isolation from the rest HRM practices is not controlled. This study follows the same approach and examined a bundle of HRM practices with quite understanding that each individual of HRM practice would have a different effect on organizational performance, but jointly would influence organizational performance.

This study examines how HRM practices affect organizational performance. We do trace the causal order relationship between HRM practices and organizational performance, by inserting employee outcomes as mediating variables; with considering that HRM practices can enhance these outcomes (Guest, 1997; Becker et al., 1997; Delery and Shaw, 2001 and Edwards and Wright, 2001).

The general framework of mediating models indicates to an indirect relationship through employee outcomes, between HRM practices and organizational performance. Nevertheless, many direct relationships may be observed between individual HRM practices and organizational performance (Schuler and Jackson, 1999 and Harel and Tzafrir, 1999). But these relationships may not be simultaneously present, and even the possibility of the absence of these direct relationships; some practices positively enhance organizational performance through the intervening process.

The success of any organization (including small business) depends on number of factors. The special characteristics which small businesses have and the difficulties that hinder their progress make them in dire need of governmental support. In Malaysia, the government with its strong belief of the vital role of small businesses adopted many supporting programmes for backing up small business sector.

The review of literature related with governmental support revealed that there is a scarcity of empirical researches devoted to tracing the influence of governmental support on the organizational performance of small businesses. So, to clarify the extent of the utilization of small businesses for the governmental support, the sub-model of this study concerned to demonstrate the relationship between governmental support and organizational performance. The general conceptual model for this study is as follow: