

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 Eight Malaysia Plan (2001-2005) have focused on the