

# The Reality of Relationship between the HRM Practices and Organizational Performance (Open the Black Box)

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**Abstract—** This study focuses on the fact of the relationship between Human Resources Management Practices and Organizational Performance which have been the center of attraction for many researches and studies. The effect of human resource management practices positively on employee outcomes and then on organizational performance is the engine of organizations to sustain the competitive advantage, and the management of this worthy resource can lead to success. objectives: The main objective of this study is: 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. To achieve this objective, a quantitative research study was conducted on a sample consisting of 265 Malaysia small businesses working in manufacturing sector. Structural equation modeling with Amos 20 was used as an advanced quantitative measure beside other statistical measures in order to attain the prior objectives. Results: 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 and both human resources management practices and organizational performance. Conclusion: the human resources management could be one of the most significant strategies to achieve the competitive advantage.

**Keywords-** Human Resource Management Practices, Employee Outcomes, Organizational Performance, Small Business.

## I. INTRODUCTION

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. [1] has confirmed the fact that HRM1 practices represent a single path that can be used by businesses to conform attitudes and behaviors 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.

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 involvement1-2-3-4-5.

Study by Huselid [1] 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 businesses6-7. 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.

Thus, the focus of this study is to test the power of HRM Practices in Organizational Performance of small businesses in Malaysia.

## II. THE CAUSAL-CHAIN PERSPECTIVE BETWEEN HRM PRACTICES –EMPLOYEE OUTCOMES- ORGANIZATIONAL PERFORMANCE

To explain the HRM practices influence on employee outcomes and ultimately on organizational performance, social exchange theory suggested that employees' perceptions of how their job influence job satisfaction are related to the common idea about the extent to which the organization concerns with their well-being, therefore, this belief may cause a desire among employees to demonstrate positive attitude and behaviour towards the organization<sup>8</sup>, suggested that the reciprocal action results positive outcomes both for employees (employee engagement, job satisfaction, trust) and organizations (higher productivity, lower-level of absenteeism and turnover).

Kandasamy [9] indicated to the importance of employee outcomes as indicators of employee well-being which influence the organizational performance. The results of their empirical work about employee well-being and the quality of work life in service industry showed that employee well-being significantly affected customer's service satisfaction.

Several scholars indicated to employee well-being as a vital constituent that influence the organizational performance, and HRM practices role is to create and maintain an organizational climate that enforce the employee well-being<sup>10</sup>. In an intensive study, [10] surveyed a large body of research concerning the relationship between HRM practices, employee well-being, and O.P.

Additionally, Van [10] investigated 41 literature studies previously conducted in the period between 1995- 2008, and followed up with another review for empirical research that accomplished in the period between 1995-2010 about the role of employee well-being in the HRM-O.P. relationship<sup>11</sup>. The key findings of these review confirmed that employee well-being mediate the relationship between HRM practices and organizational performance.

In literature concerning the HRM-O.P. relationship, two distinct perspectives about employee outcomes as a mediating variable in this relationship exist.

Mutual- Gains Perspective; It proposes that HRM may positively affect both the employee and the organization. Several models have been developed to examine the positive influence of HRM practices on both E.O. and O.P., in accordance with this strand, or the "Optimistic Perspective" as called by<sup>12-13-14</sup>. noted that HRM practices are often used to elicit and control employee outcomes (attitudes and behaviors) which contribute to O.P.

Depending on social exchange theory, scholars such as<sup>15</sup>. considered HRM practices as indicators of organization's interest of its employees, and when employees perceive that interest, they reciprocate with satisfaction, cooperation,

involvement, and trust. Similarly, [16]. presented, through his conceptual model (AMO) view, that HRM practices increase employee outcomes such as job satisfaction, commitment, trust, and reduces stress levels which hence positively influence the O.P.

Contrary to mutual-gains perspective, conflicting-outcomes perspective or "Pessimistic Perspective" as called by<sup>12-17</sup>. is concluded that, while HRM works for the benefit of the organization, but has been no influence on employee outcomes<sup>12-18-19</sup>

As there is very little known empirical research that examine the influence of HRM on O.P. in small businesses, this research try to gain new insights to HRM practices and its causal relationship with O.P., depending on RBV to discuss the important role of human capital and management in small business.

In literature, another point of view has been lately put forward to explain and examine the causal chain of HRM-performance relationship that is so-called organizational justice theory as it proposed as a means of understanding the HR-performance relationship through employee perceptions and subsequent attitudes and behaviours. [20] advocated this theory as they claimed that it clearly explain how and why people react to a given HRM outcome, process or interpersonal action by addressing perceptions of fairness in their employment relationship<sup>21</sup>.

As long as there is a growing conviction that HRM practices affect O.P. through causing in employee outcomes (attitudes and behaviours) in response to their perceptions of those practices<sup>22</sup>., and, as an agreement has been existed that there is still a scarcity of research concerning the link between HRM and O.P. based on employee reactions to HRM<sup>23-24-25</sup>.

This research attempts to explain the HRM "Black Box" by developing a better comprehension of the mediating behaviours that interpret the relationship between HRM practices, employee outcomes and organizational performance, depending on a full understanding of the previous theories and approaches have been mentioned.

## III. PROBLEM STATEMENT

Today, small businesses are one of the most popular topics in business literature. A wide range of research seeks to find out what is needed to enhance the performance of small business. Among the strategies that could help small businesses to survive and grow are internal factors such as human resource, which may not receive the attention and the care like other factors such as capital, technology, raw materials, and other production inputs.

Many researchers have been made to identify the HRM-company performance relationship over the past decade or so, serious gaps in our knowledge still remain [26].found that although positive relationships have been reported between HRM and performance, the causal ordering of the variables integrated in these relationships was not convincing. Additionally, whilst it was assumed that effectively

implemented HR practices will cause higher performance, it was supported that it is more important to see (How) something is done compared to just (What) has been done. It was further argued that it is important to consider the intervening steps in the HRM- Performance relationship, or to consider the variables mediating the endpoint variables. The issues had been expressed by the model of study:

Try to test the causal relationship between HRM Practices and Organizational Performance.

#### IV. RESEARCH OBJECTIVES

The main focus of this study is tracking the influence of each one, HRM practices on organizational performance of small businesses that might lead to the best way to the success of small businesses. The summary of objectives of study is below:

- To explore how HRM practices as one “bundle” directly affect organizational performance of small businesses.
- To evaluate the indirect relationships between HRM practices and trust in management, cooperation, Intention to turnover, and effort and involvement.
- To develop the indirect relationship between trust in management, cooperation, intention to turnover, and effort and involvement and organizational performance of small businesses.
- To examine the relationship between HRM practices and organizational performance with trust in management, cooperation, intention to turnover, and effort and involvement as a mediation.

#### V. RESEARCH HYPOTHESES

- H1: There is a significant relationship between human resource management practices and organization performance.
- H2: There is a significant relationship between human resource management practices and trust in management.
- H3: There is a significant relationship between human resource management practices and cooperation.
- H4: There is a significant relationship between human resource management practices and intention to turnover.
- H5: There is a significant relationship between human resource management practices and effort and involvement.
- H6: There is a significant relationship between trust in management and organization performance.
- H7: There is a significant relationship between cooperation and organization performance.
- H8: There is a significant relationship between intention to turnover and organization performance.
- H9: There is a significant relationship between effort and involvement and organization performance.

- H10a: Trust in management mediates the relationship between human resource management practices and organization performance.
- H10b: Cooperation mediates the relationship between human resource management practices and organization performance.
- H10c: Intention to turnover mediates the relationship between human resource management practices and organization performance.
- H10d: Effort and involvement mediates the relationship between human resource management practices and organization performance.

#### VI. METHODOLOGY

##### A. Population and Sample

The population of study is the small businesses in manufacturing sector in Malaysia. Account to approximately 15,796. Simple random sampling has been used in this study. It is the method most commonly employed in many practical situations. In this study the sample is 265 small manufacturing businesses in Malaysia, (265 owners/ managers, and 656 employees).

##### B. Data Collection

A questionnaire is the main instrument for data collection, the reasons that made the researcher choose the questionnaire are; (1) Most literature review related with this study used questionnaire to collect the data. (2) Difficult to find free time to meet the respondents through working hours. (3) Alternative instruments considers more expensive.

Most research devoted to test the causality relationship between HRM- Organizational Performance, and use a single source of data, which is called “over- reliance”. Particularly, collecting the data about HRM, employee perceptions, and organizational performance without use multi-source/ multi-rater, is subject to common method variance and rater bias. [27]. referred about researches that depend on a single source of respondents as “highly questioned” in term of reliability and validity.

Thus, to avoid the potential single source bias, data for this study will collected from managers/ owners, and employees of small manufacturing businesses.

##### C. Questionnaire Design

- Modify the Questionnaire and used the most commonly -used terms in Malaysia:
- After design the questions, researcher tried to modify and simplified the questions through used the direct and short questions. Also used the common terms that know from managers/ owners of small businesses.
- Panel of Judges: researcher put forth the variables of study on some of lecturers of Technology Management Faculty/ University Malaysia Pahang and some experts from some University Putra Malaysia and International

Islamic University Malaysia to choose the best questions. Since, the judges test the each item and investigate whether these skills or knowledge measured by this item or not depending on their experience.

- Re-modify the Questionnaire: after defining the questions that present the content of variable, researcher re-modified and arranged the questions.
- Exploratory Factor Analysis (EFA): this step conducted to test the validity of this variable. Researcher tested the EFA on 100 small manufacturing businesses.
- Pilot Study: this step conducted on 20 small businesses to check the reliability of questions.
- Distribute the questionnaires: after all the steps before the researcher distributed the questionnaires on sample of study.

#### D. Statistical Analysis Technique

Structural Equation Modelling (SEM) with Amos 20 has been used to assess the relationships among the variables in the research model represented.

## VII. RESULTS

To determine the best-fit model, three structural models namely direct (model 1), indirect (model 2) and partial mediation model (model 3) were tested for model comparison. The direct model (model 1) examined direct relationships from HRM practice and organizational performance without going through the mediator variable (Trust in Management, Cooperation, Intention to Turnover, and Effort and Involvement). The indirect model (model 2) estimated paths from HRM practice and trust in management, cooperation, intention to turnover, and effort and involvement, and from trust in management, cooperation, intention to turnover and effort and involvement to organizational performance. Meanwhile, the partial mediation model incorporates all identified paths linking to organizational performance.

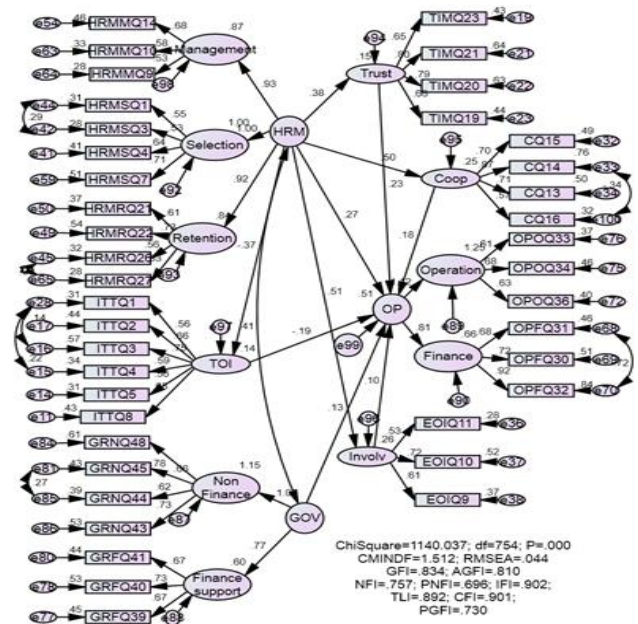


Fig 7: Mediation Model

TABLE 7.1: SUMMARY OF MODEL FIT INDICES FOR DIRECT, INDIRECT AND MEDIATION MODEL

Model	Chi-Square ( $\chi^2$ )	df	$\chi^2/df$	RMSEA	GFI	IFI	TLI	CFI	PGFI
Direct	1328.107	762	1.743	0.053	0.805	0.856	0.843	0.854	0.712
Indirect	1154.796	756	1.528	0.045	0.833	0.899	0.889	0.897	0.730
Mediation	1140.037	754	1.512	0.044	0.834	0.902	0.892	0.901	0.703

TABLE 7.2: GOODNESS-OF-FIT INDICES FOR THE MEASUREMENT MODEL

Best Practices	CMIN/df	Kline (2010)	1 – 5
	RMSEA	Steiger (1990)	< .08
	CFI	Byrne (2010)	> .90

Note: RMSEA = Root Mean Square Error of Approximation, GFI = Goodness-of-fit, AGFI = Adjusted Goodness of Fit Index, NFI = Normed Fit Index, CFI = Comparative-fit index, IFI = incremental fit index, TLI = Tucker-Lewis coefficient Index, PGFI = Parsimony Goodness-of-Fit Index, PNFI = Parsimonious Normed Fit Index

In choosing structural model fit, based on the Model Comparisons in Figure 7.1 and Table 7.1 depending on the best practices approach (Table 7.2), shows the mediation model is most likely to represent a better model fit, since it presents better fit indexes compare to the other models.

## VIII. CONCLUSION

The findings of the study present significant influence relationship between HRM practices and organizational performance, HRM practices and employee outcomes, and employee outcomes and organizational performance, also, the employee outcomes (trust in management, cooperation, intention to turnover, and effort and involvement) mediated between HRM practices and organizational performance. Table 8 demonstrates the conclusion of the results.

TABLE 8: SUMMARY OF THE RESULTS

No.		Findings
H1	Significant relationship between human resource management and organization performance	Significant
H2	Significant relationship between human resource management and trust	Significant
H3	Significant relationship between human resource management and cooperation	Significant
H4	Significant relationship between human resource management and turnover	Significant
H5	Significant relationship between human resource management and effort and involvement	Significant
H6	Significant relationship between trust and organization performance	Significant
H7	Significant relationship between cooperation and organization performance	Significant
H8	Significant relationship between turnover and organization performance	Significant
H9	Significant relationship between effort and involvement and organization performance	Significant
H10a	Trust mediates the relationship between human resource management and organization performance	Partial Mediation
H10b	Cooperation mediates the relationship between human resource management and organization performance	Partial Mediation
H10c	Turnover mediates the relationship between human resource management and organization performance	Partial mediation
H10d	Effort and Involvement mediates the relationship between human resource management and organization performance	Indirect mediation

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