



## The Effect of Human Resource Management Practices on Business Performance among Private Companies in Malaysia

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### Abstract

The aim of this study was to identify commonly HRM practices effect on Malaysian private companies' performance. We found support for the four HRM practices are found to be correlated with the business performance based on responses from 153 managers from Selangor based private firms in Malaysia. Regression results showed that training and development, team work, compensation/incentives, HR planning, performance appraisal, and employees security have positive and significant influence on business performance with the exception for compensation/incentives and employees security.

**Keywords:** HRM, Private Companies, Malaysia

### 1. Introduction

Human resources of a company is saying to be one of the important capital is playing such an important role in the operation of an organisation. Pfeffer (1994) argued that human capital has long been held to be a critical resource in most firms. Companies are now trying to add value with their human resources and human resource (HR) department has been set up in order to manage their human capital, where as organisation in last decade, managed their human capital through personnel department which is only a small division of the company. The process of managing the human capital is called human resource management (HRM).

Malaysian organizations have started realising the importance of HRM. Cheah et al. (2003) stated that Malaysian managers realised that HRM had to be effective to bring about organisational stability and harmony. Besides, they also stated that the diversity of the composition of the modern workforce in Malaysia requires more appropriate and imaginative HRM solutions. As several scholars have noted that managing people is more difficult than managing technology and capital (Barney, 1991; Lado & Wilson, 1994), principally, in a country like Malaysia which is a multiracial country, failure in managing human capital and maintaining the harmony within an organisation will create fatal problems to the organisations.

Malaysian government has envisioned as a developed nation by 2020. Government has also recognised that human resource management can play an important role for the said vision. Managing human resources has become critical to the success at all companies, large and small, regardless of industry (Ulrich, 1997). Stavrou-Costea (2005) also argued that the effective human resource management can be the main factor for the success of a firm. Today the most of the

companies believed that without efficient HRM programmes and activities companies would not achieved and sustained effectively (Schuler, 2000). Consequently most of the organisations, domestic companies and multinational companies/corporations (MNCs) in Malaysia nowadays tend to focus more on HRM and also treated HRM as a key of success.

It is important for Malaysian private companies to retain their employees into their organization due to meet their ultimate goal i.e. maximizing profit. Malaysian Employers Fedearation (MEF, 2004, 2005) reported that annual labour turnover in 2003 and 2004 were approximately 17 per cent and 16 per cent respectively. Considering the need for HRM practices, Malaysian SMEs can motivate and retain their talented employees into their organization. Thus, this research is expected to become, in an important part, a meaningful guideline for human resource management practitioners in motivating and retaining their talented and skilled employees in the Malaysian context.

The purpose of this paper is to review the literature findings available other researches in the globe to date, to examine the relationship between HRM practices and performance of the organizations in the medium scale enterprises in Malaysia.

## **2. Literature Review**

Studies show that HRM plays an important role in formulating and implementing organisational strategy. Myloni et al. (2004) found that also HRM can be seen as part of the overall strategy of the firm. The increasingly importance of HRM in strategy has then led the HR managers to be part of the decision makers while formulating and implementing strategy. Rozhan and Zakaria (1996) study of Malaysian firm provides some evidence of HR managers having an involvement in the strategy formulation process.

Most research suggests that HRM is vital in order for an organisation to achieve organisational success (Barney, 1991; Jackson & Schuler, 2000; Pfeffer, 1994). Typically, HRM is considered to be vital in order for an organisation to achieve its success by enabling the organisation to sustain competitive advantage. Literatures on strategic HRM even indicate that HRM practices and systems contribute to the creation of a sustained competitive advantage for the firm (Arthur, 1994; Gerhart & Milkovich, 1992; Huselid, 1995; Macduffie, 1995; Terpstra & Rozall, 1993). As a result, it is important that a firm adopt HRM practices that make use of its employees.

A number of researches have found a positive impact of HRM on organisational performance. For instance, Becker and Gerhart (1996), Becker and Huselid (1998), and Dyer & Reeves (1995) empirical studies found that firms which align their HRM practices with their business strategy will achieve superior outcomes. MacDuffie (1995) studies worldwide auto assembly plants found that some HRM practices are related to productively and quality of the firm. Delery and Doty (1996) found significant relationships between HRM practices and accounting profits among banks. Youndt et al (1996) found that certain combinations of HRM practices are related to operational performance of manufacturing firms. Guthrie (2001) surveyed in New Zealand corporations found that HRM practices are related to turnover and profitability of the corporations.

More recent empirical study on HRM practices (Lee & Lee, 2007) uncovered six underlying HRM practices on business performance, namely training and development, teamwork, compensation/incentives, HR planning, performance appraisal, and employee security help improve firms' business performance including employee's productivity, product quality and firm's flexibility. This study reveals that three items of HRM practices influence business performance: training and development, compensation/incentives, and HR planning. However, some other researches also show that certain HRM practices have significant relationship with operational (employee's productivity and firm's flexibility) and quality performance outcomes (Chang and Chen, 2002; Ahmad and Schroeder, 2003; Kuo, 2004 Sang, 2005). These research evidence shows that effective HRM practices can have positive impact on business performance.

Using data from 197 Taiwanese high-tech firms Chang and Chen (2002) conducted a comprehensive study to evaluate the links between HRM practices and firm performance. This study reveals that HRM practices including training and development, teamwork, benefits, human resource planning, and performance appraisal have significant effect on employee productivity. This study also found benefits and human resource planning have negative relationship with employee turnover.

To generalize the efficacy of seven HRM practices by Pfeffer (1998) Ahmad and Schroeders (2003) found the seven HRM practices such as employment security, selective hiring, use of teams and decentralization, compensation/incentive contingent on performance; extensive training, status difference and sharing information have significant relationship with operational performance. Kuo (2004) adopted 11 HRM practices found that employment security, team working and incentive compensation are regarded as three of the main practices for impacting hospital performance.

Although HRM practices has been consider as one of the influential variables seems to increase business performance, most of the Malaysian private business organization really not practicing HRM into their business (Chew, 2005). It is unclear on how to change the mindset of the Malaysian business organization practicing HRM into their businesses. In order to understand what influence business performance as well we must first find out the HRM practices that are

influencing business performance. Therefore, it is replicated with references to the HRM practices related research in developed countries. In this study six factors have identified and they are training and development, teamwork, compensation/incentives, HR planning, performance appraisal, and employee security.

### 3. Research Model and Hypotheses

After looking at the literatures, this research posits the following hypotheses and statistical research model:

**H1:** There is a significant relationship between the training and development and business performance.

**H2:** There is a significant relationship between teamwork and business performance.

**H3:** There is a significant relationship between compensation/incentives and business performance.

**H4:** There is a significant relationship between HR planning and business performance.

**H5:** There is a significant relationship between performance appraisal and business performance.

**H6:** There is a significant relationship between employee security and business performance.

According to the existing literature the conceptual model in this study is shown in Figure 1.

### 4. Research Methods

#### 4.1 Sample and Data Collection

Data for this study was gathered by primary data collection method through personal administered questionnaire. Due to the cost constraint a convenient sample of 159 private companies were chosen for this research. One trained data collector approached potential respondents in randomly selected private business organization in Selangor in Malaysia. After assisting a respondent in completing a survey, the data collector would then approach the next available person and resume the screening process.

Of the 159 respondents who were agreed to complete the survey. However, 6 were discarded due to uncompleted responses; the final sample was 153 for an effective response rate of 91.45 percent. The response rate is very high due to the fact that the researchers' pursued all respondents personally and motivate respondents to participate the survey. The majority of the respondents were male (57.51 percent), Chinese group was the highest contributors of the total respondents (74.50 percent). Their age ranged from 16 to 50 with mean age of about 41.5 years old. Most of them were undergraduates representing 66.66% of the total sample.

#### 4.2 Measurement Development

Respondents completed personal survey questionnaire that included questions about the basic characteristics of the respondents (gender, age, race) items designed to assess (a) HRM practices, and (b) business performance.

*Business performance:* Business performance was measured using items developed by Lee and Lee (2007) with minor wording changes tailored to the business organization in Malaysia. Six items were rated using a multi-item method was used to increase the accuracy of measurement, and each item was based on a five point Likert scale (1) strongly disagree to (5) strongly agree.

*HRM practices:* Twenty five items measured variables were used to reflect the components of HRM practices. HRM practices including training and development, teamwork, compensation/incentives, HR planning, performance appraisal, and employee security were considered as the independent variables for this research. Similarly like business performance a multi-item method was used to increase the accuracy of measurement, and each item was based on a five point Likert scale (1) strongly disagree to (5) strongly agree.

#### 4.3 Reliability

Table I shows the number of items comprising each scale: the reliability reported by Nunnally (1978) for the scale and Cronbach's alpha for scale reliability obtained for our sample. Reliability from our sample showed a reasonable level of reliability ( $\alpha > 0.70$ ).

#### 4.4 Test for construct validity: factor analysis

A factor analysis was conducted in order to develop factors that help in explaining the role of experience and reference group in online brand trust. As suggested by Hair et al., (1995), seven factors were identified for the factor analysis using the eigen value criteria that suggest extracting factors with an eigenvalue of greater than 1.0. In conducting the factor analysis we followed Hair et al (1995) and Alfansi and Sargeant (2000). The seven factors identified explain 59.21 percent of the total variance. The extraction method used was principal axis factoring with Varimax rotation. This method has been widely accepted as a reliable method of factor analysis (see, Alexander and Colgate, 2000). In our survey, the Kaiser-Meyer-Olkin (KMO) measure of sampling adequacy score (0.86) was well above the recommended 0.5 level (Malhotra, 1999) suggested that the data may be factorable.

In creating these measures of HRM practices, we decided not to drop items loading heavily (.4 or higher). All items were loaded more than .4, however one item of training and development, one item of HR planning loaded together with other items is considered as insignificant and not meaningful as it is of low correlations decided to remove from all further analysis.

### 5. Normality of Data and Multi-collinearity

Two major methods were utilized in order to determine the presence of multicollinearity among independent variables in this study. These methodologies involved calculation of both a Tolerance test and Variance Inflation Factor (VIF) (Kleinbaum et al, 1988). The results of these analyzes are presented in Table IV. As can be seen from this data, i) none of the Tolerance levels is <or equal to .01; and ii) all VIF values are well below 10. Thus, the measures selected for assessing independent variables in this study do not reach levels indicate of multicollinearity. The acceptable Durbin – Watson range is between 1.5 and 2.5. In this analysis Durbin – Watson value of 1.745, which is between the acceptable ranges, show that there were no auto correlation problems in the data used in this research. Thus, the measures selected for assessing independent variables in this study do not reach levels indicate of multicollinearity.

### 6. Results of Hypotheses Tests

This study combined six HRM practices into one regression, to see the overall effect on business performance. The result in the table shows that of the six hypothesized relationships, four are significant ( $p < 0.05$ ) and two are nonsignificant ( $p > 0.05$ ) (see Table IV).

H1 suggest that training and development has a positive impact on business performance. The regression results support this hypothesis ( $t = 2.803$ ,  $p = .006$ ). This findings is consistent with studies indicating that higher the training and development facility provided by the company the performance will be. In other words, training and development program is important factor for business performance of a company (Lee and Lee, 2007).

H2 suggests that team work positively affects business performance. The regression results support this hypothesis ( $t = 2.266$ ,  $p = .025$ ). This finding is consistent with studies by (Lee and Lee, 2007; Ahmad and Schroeders, 2003) found that team work has significant relationship with business performance.

H3 suggests that compensation/incentives have a positive impact on business performance. The regression results show nonsignificant relationship with business performance ( $t = 1.172$ ,  $p = .243$ ). This study is counter to early study by Lee and Lee (2007).

H4 suggests that HR planning has positive and significant relationship with business performance. It is expected since past literature has consistently shown that HR planning has a significant and positive impact on business performance (Lee and Lee, 2007; Chang and Chen, 2002). The regression results support this study ( $t = 3.821$ ,  $p = .001$ ).

The acceptance of H5 (performance appraisal) is in agreement with some past research findings (Lee and Lee, 2007; Sang, 2005; Chang and Chen, 2002). The study result indicating that performance appraisal has positive impact on business performance ( $t = 2.128$ ,  $p = .035$ ). All of the previous studies suggest that performance appraisal significant and positive relationship with business performance.

From the results of the regression of this study found that employees security has no significant relationship with business performance ( $t = -.287$ ,  $p = .774$ ). However, the negative sign on the figure shows that if there is a relationship it will be negative one. This higher the security problem lower the business performance will have in the business. This study is consistent with previous study by Lee and Lee (2007).

### 7. Implications for practice

The study reveals four significant indicators of HRM affecting business performance in the business. Government agencies like MIDA, SMIDEC, and other government agencies should create better awareness of the benefits of HRM practices to encourage higher rate of retention of the employees in the business organisation. It can be done by having seminars or induction sessions to allow companies to evaluate their business performance. In order to receive greater responses towards HRM practices, it is recommended that authority should give certificate as a token and financial support to attend the seminar. They could establish a close link with all business organization and get continuous feedback from them in order to identify the problem areas and take necessary actions to rectify them. Another way to enhance the possibility to use HRM in the companies sectors, government should enforce standardized, consistent and uniform policies in all business sectors, agencies or subsidiaries in practicing HRM policies. Management of private businesses should provide adequate pre-training to their employees on how to practices in business at all levels must be ensured so that the employees should get comfortable with practicing it.

### 8. Conclusion

The research framework for this study relied on the six HRM practices as identified in various past research namely, training and development, team work, compensation/incentives, HR planning, performance appraisal, and employees security. Based on the result of the study, four HRM practices are found to be correlated with the business performance

with the exception for compensation/incentives and employees security. These results indicate that these two factors will not likely to influence the overall business performance in the Malaysian business organisation. In conclusion we can say all six HRM practices help improve firms' business performance including employee's productivity, product quality and firm's flexibility. From this result, it can be concluded that this study has achieved its main objective, which is to, study about the effect of HRM practices towards business performance in the context of private firms in Malaysia. Furthermore, the analysis indicates that in general the HRM practices did have some effect towards business performance even though two of the HRM factors did not show any support.

### 9. Limitations and recommendation

The study is limited in several ways. First, the small number of participants restricts the generalizability of the findings. Second, further analysis is needed on the pre-existing differences between the groups with respect to medium scale and small scale business organizations particularly HRM practices rate, which could impact future usages of HRM into all organisations. Further analysis is also needed to determine the potential moderating effects of ideology of its owner, size and technology usage of the firm.

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Table 1. Reliability Analysis

Variables	Coefficient Alpha
Training and Development	0.737
Team Work	0.809
Compensation/Incentives	0.862
HR planning	0.797
Performance Appraisal	0.724
Employees Security	0.769
Business performance	0.831

Table 2. Test of Collinearity

Variable	Tolerance	VIF
Training and Development	.597	1.675
Team Work	.555	1.802
Compensation/Incentives	.700	1.429
HR planning	.646	1.548
Performance Appraisal	.590	1.695
Employees Security	.613	1.632

Table 3. Regression Results

Independent variables	Parameter estimate	Standard error	t-value	p-value
Constant			2.162	.032
Training and Development**	.218	.329	2.803	.006
Team Work*	.183	.065	2.266	.025
Compensation/Incentives	.084	.072	1.172	.243
HR planning**	.286	.070	3.829	.001
Performance Appraisal*	.167	.073	2.128	.035
Employees Security	-.022	.081	-.287	.774

\*p<0.05; \*\*p<0.01; N=153  
Overall model: F=21.80; p<0.0001; R<sup>2</sup>=0.473; Adjusted R<sup>2</sup>=0.451

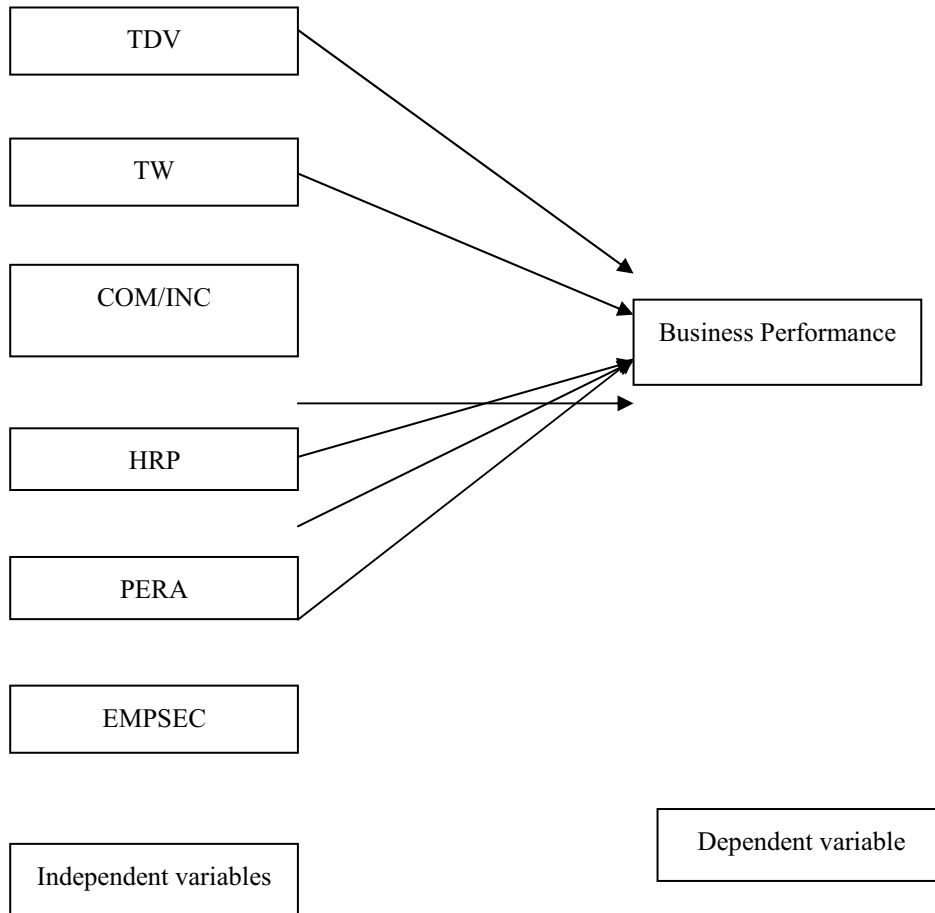


Figure 1. A Schematic diagram of the conceptual framework