

# Are Human Resource Departments Really Important?

## An Empirical Study on Malaysian Small and Medium Enterprises (SMEs) in the Service Sector

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### Abstract

The intention of this study is to examine the significant differences in terms of employees' job satisfaction and firms' performance for Malaysian SMEs that has their own Human Resource (HR) department against organisations who doesn't have their own HR department. Besides that, this study provides more insight towards Malaysia's Human Resource Management practices based on 43 SMEs in the service sector.

### Findings

The finding of the study reveals that there are significant differences between organisations with HR department and organisations without HR department in terms of employees' training and development, performance appraisal, employee relations and communication and also in terms of employees' job satisfaction.

**Methodology:** SPSS, Sample 43, Self-administered questionnaire.

**Keywords:** Human Resource practices, SMEs, Services sector, Malaysia

### 1. Introduction

SMEs play an important role in all economies in the world by contributing 80 percent of global economic growth (Jutla, et al., 2002). The importance of SMEs in developing a nation must not be taken lightly and be underestimated (Ragesh et al., 2010; Noor Hazlina & Seet, 2009). The contribution of SMEs on the various Asian nations' Gross Domestic Product (GDP) is significant as shown in the Table 1 as follows:

[Insert Table 1]

As indicated in Table 1, more than 90% of the business establishments (except Singapore) are mainly SMEs. These SMEs provide job opportunities for more than 40% of their workforce. Furthermore, SMEs from countries such as Japan and China contribute more than 50% towards their nations' GDP. Thus, these significant GDP indicators reflect the importance of SMEs towards nation building. Hence, many countries are taking steps and initiatives to ensure their nations' SMEs survival, sustainability and competitiveness by providing various support schemes such as branding and marketing, advisory services, subsidised lending and also building human capability (International Monetary Fund, 2009). To build human capability in an organisation, good and sound human resource practices must be implemented to ensure that human resources are well taken care of. Sound

implementation of human resources policies and practices such as recruiting, screening, training, rewarding and appraising have strong relationship towards organisations' performance hence making Human Resources as one of the sources of competitive advantage. (Ordonez de Pablos & Lytras, 2008; Collins, 2007; Chew & Basu, 2005; Khandekar & Sharma, 2005).

Human Resource Management (HRM) can be defined as policies and practices involved in carrying out human resource aspect of management (Dessler, 2007), that influence employees' behaviour, attitudes and performance (De Cieri et al., 2008). Organisations that realise the importance of Human Resources as an asset rather than as a commodity would always find ways to create a working environment that is conducive, safe, and able to fulfill work life balance to their employees in the recent years. However, some organisations outsourced their HR functions or the organisation's administration department handles all matters regarding HR functions, on the pretext of increasing efficiency or reducing cost. Hence it would be interesting to determine whether the HR department contributes towards the employees' job satisfaction and organisations' performance.

However, studies on HR practices in Malaysian organisations are quite limited. Besides that, these studies do not encompass all HRM aspects and the current available evidence is not sufficient (Hassan, 2010). The adoption and development of HRM in Malaysian corporate sector has been slow as compared with multinational companies (MNCs) operating in Malaysia (Chiah-Law et al., 2003). This statement is ascertained by Rowley and Abdul Rahman (2007). Rowley and Abdul Rahman (2007) in their study compared the adoption of HR practices of a Malaysian Organisation with a MNC operating in Malaysia. The study reported that locally owned Malaysian organisations do not place a great importance on HR practices as compared with MNCs. Furthermore, Rowley and Abdul Rahman mentioned that locally owned Malaysian organisations' top management have low commitment towards the importance of HR practices. According to Othman et al., (2001) on their study on SME manufacturing organizations reported performance gap exists between the expectation of top management towards the HRM functions with the actual implementation of the HRM functions in their organisations.

This lead to the research issues of this study. Firstly, this research aims to examine the extent of adoption of HR practices in Malaysian SMEs in the service sector. Besides that this study also aims to determine whether the HR department contributes towards the employees' job satisfaction and organisations' performance.

This paper is divided into 5 parts. Firstly a brief overview of the current Human Resource scenario in Malaysia will be discussed. This brief introduction will provide a general idea on demographics and profile of the current workforce in Malaysia. Secondly, the methodology used for this study will be presented. Thirdly the analysis of the findings and discussion will be presented. Lastly limitation and recommendation for future research will also be presented.

## 2. Current Human Resource Scenario in Malaysia

[Insert Table 2]

As at 2009, 11,585,000 out of the 27 million people in Malaysia are employed. Unemployment rate had increased slightly from 3.3% to 3.9% in 2009 as a result of the world economic crisis, and it is forecasted that it the employment rate will maintained at 3.9% in 2010. In 2009, GDP of Malaysia suffered from a deficit of 3% as a result of worldwide economic collapse, however, it is forecasted that by 2010, with the global economic recovery on the way, Malaysia's forecasted economic growth would be back on track with GDP growth of 2-3%.

The importance of Human Resource had been acknowledged by Malaysian government, where in 1991, the Malaysian government has included Human Resource Development in the 6<sup>th</sup> Malaysian Plan. Besides that, Malaysian Government has also introduced several other incentives for private sector to develop their human resources. These include establishing industrial training institutes to develop employees for job entry level, setting up Human Resource Development Fund in 1993 that are based on a levy/grant system that provides training costs subsidies for employers who have paid the levy, which had been set at 1 percent of the employees' monthly wages for manufacturing firms (MIDA, 2009).

In relations to benefits and compensation, organisations in Malaysia are moving towards performance based system. As shown by a survey conducted by Malaysia Employer Federation. In the survey, 86.3% of the 233 organisations surveyed stated that their organisations linked salaries of their executives to performance (MEF, 2007).

## 3. Methodology

The sample consisted of Malaysian SMEs in the service sector. Malaysian SMEs is can be as organisations with not more than 50 employees. The SME definitions for manufacturing and agriculture sector were also shown in Table 3 below:

[Insert Table 3]

Organisations were chosen from the retail and wholesale, information technology, consultancy, real estate, transport and communication, and healthcare industries. These industries were chosen based on the sampling frame from The Official Business Directory of SMI Association Malaysia 2007. Convenience sampling was used to select the element in the population frame. The Business Directory of SMI Association provides email addresses and addresses of the SMEs. Questionnaires were sent via email and post. HR Managers or top management representatives for organisations without a HR Department were requested to fill in a questionnaire that describes the current HR practices in their organisations. Besides that, respondents were requested to provide their own perceptions of their organisations' performance and job satisfaction level. The response rate for this study is 21.5% where a total of 200 questionnaires are distributed, and only a total of 43 questionnaires were received.

### 3.1 Measurement Items.

The measurement items used this questionnaire were adopted as shown in the following Table 4:

[Insert Table 4]

Table 5 below shows that all of the major variables in this study recorded Cronbach Alpha value of more than 0.7. This indicates that there is a strong internal consistency among the items that make up the scales (Nunnally, 1978). Hence, no items are deleted for the purpose of this study.

[Insert Table 5]

## 4. Findings

Table 3 summarizes the demographic profile of the respondents. 51% of the 43 SMEs surveyed stated that they have a HR department in their organisation while the remaining 48.8% stated otherwise. Male respondent constitute 34.9% where the female respondent was 62.8%. The remaining percentages were concluded as missing data. The majority of the respondents holds a degree (48.8%) and possesses more than 3 years of working experience in HR department or HR related areas.

[Insert Table 6]

Variable 1 until variable 7 in Table 7 represents the extent of current HR practices that are being implemented in their organisation. Table 7 suggests that most organisations in Malaysia adopt HR practices in moderation. As for job satisfaction, the results revealed that generally, the respondents are neutral in this matter. In relation to organisation performance, respondents mean value shows that they feel that their organisation performances are about the same as compared with the industry's average.

[Insert Table 7]

This study intends to distinguish adoption of HR practices among organisations with HR department and those without HR department. Based on the figures reported in Table 8, there are significant differences in Human Resource Practices in terms of training and development, performance appraisal, employee relations and communication and employees' job satisfaction. This reflects that SMEs with their own in-house HR department implement the above mentioned human practices more frequently than with SMEs without an in-house HR department. Besides that, employees attached to organisations which have their own HR department indicate higher job satisfaction. However in terms of organisation performance shows no significant difference exists between organisations with HR department and organisation without HR department.

[Insert Table 8]

## 5. Discussion

This research has three main objectives. Firstly, this research intends to investigate whether any significant differences exist between SMEs with a HR department and those without in terms of implementing HR practices in their organisation. Based on the findings of this study organisations with their own HR department have shown a greater degree of implementation in areas of training and development, performance appraisal, and employee relations and communication. These differences exist because SMEs with HR department are generally larger in size; hence more training are given to cater for different training needs for each department. Consequently, performance appraisals are conducted more often to determine the effectiveness of the training. Besides that, larger SMEs need to ensure message and instructions between management and employees are being conveyed effectively hence, more emphasis are placed in the area of employee relation and communication as compared with smaller SMEs without HR department.

The second objective of this research is to determine whether HR department contributes towards employees' job satisfaction. Based on the findings of this research, SMEs' employees with HR department reported a higher level of job satisfaction. This finding is in accordance with research done by Barney and Wright (1998) where these two researchers in their study on the role of Human Resources in gaining competitive advantage supports the idea that HR practices are important determinants of employee satisfaction. The same conclusion has been ascertained by Harel and Tzafrir (1999) in their research. They found that training is able to improve skills and abilities that are relevant to employees' tasks. As a result, employees' satisfaction with their jobs and workplace will increase.

Finally, this research is also aimed at investigating whether significant differences exist between SMEs with HR department and SMEs without HR department in terms of organisation performance. In this study, there is no significant difference between the two groups. This may be due to the timing where the survey was being conducted in 2009, where the world were affected by the economic crisis hence, affecting the performance of the SMEs being surveyed.

This research would like to suggest that it would be better if organisations with their own in-house HR department will definitely have an impact on employees' satisfaction. Satisfied employees tend to display a strong negative correlation with turnover; hence it is crucial to implement the right human resource policies and practices as mentioned by Mosadeghrad et al., (2008). Besides that, critical areas such as training and development are important to ensure that employees learn how to perform better in their job function. SMEs without a HR department do not seem to engage in training and development of their employees as much as SMEs with a HR department. Hence, this lack of training and development may, impede the growth and survival of the organisation.

HR is an asset and lifeline to organisations, and must be given top priority to increase organisation competitiveness. Effective implementation of HR practices in organisations is a key source of competitive advantage and has been shown to have a positive relationship to organisation performance as confirmed by researchers such as Ordenez de Pablos & Lytras 2008; Chew & Basu, 2005; Khandekar & Sharma, 2005.

## 6. Limitation of Study

The findings of this study must be taken with some caution because this study has limitations. Firstly, this study limits itself to the Malaysian SMEs, hence, the findings and conclusions drawn from this research are representative of the Malaysian SMEs only. In addition, the study would also recommend further research to include other moderating variables such as legal and regulatory environment and industry characteristics. Besides that, this study would like recommend larger sample of organisations for future studies. Lastly, a cross-national comparison of HR practices would also provide a greater insight on the importance of HR practices towards the well-being and sustainability of organisations.

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Table 1. International SME Development and Growth

Country	Measures used in the definitions of SMEs	% of total establishment	% of total workforce	% of SME contribution to GDP
<b>Malaysia (2005)</b>	Employment and sales	99.2	56.4	32.0
<b>Japan (2004)</b>	Employment and assets	99.7	71.0	55.3
<b>Chinese Taipei (2004)</b>	Employment, sales capital	98.0	76.9	40.0
<b>Korea (2003)</b>	Employment and assets	99.8	86.5	49.4
<b>Thailand (2002)</b>	Employment and fixed assets	99.6	69.0	38.9
<b>Singapore (2004)</b>	Employment and fixed assets	45.0	45.0	25.0
<b>Germany (2003)</b>	Employment and sales	99.7	79.0	49.0
<b>China (2004)</b>	Employment, sales and assets	99.0	75.0	56.0
<b>Philippines (2003)</b>	Employment and assets	99.6	70.0	32.0

Source: Malaysia SME Annual Report 2007.

Table 2. Current Human Resource Scenario in Malaysia

	2008	2009 <sup>e</sup>	2010 <sup>f</sup>
<b>Population (million)</b>	27.73	28.31	28.88
<b>Labour Force ('000)</b>	11,967.5	12,061.1	12,216.8
<b>Employment ('000)</b>	11,576.5	11,585.0	NA
<b>Unemployment Rate</b>	3.3%	3.9%	3.9%
<b>GDP Growth (constant 2000 prices)</b>	4.6%	-3.0%	2.0% - 3.0%
<b>Per Capita Income (RM)</b>	25,784	24,055	24,661
e = estimate			
f = forecast			

Source: Malaysian Employers Federation

Table 3. Definition of SME

Size	Manufacturing (including agro-based) and manufacturing related services	Primary Agriculture	Services Sector (including Information Communication Technology sector)
Micro	Less than 5 employees	Less than 5 employees	Less than 5 employees
Small	Between 5-50 employees	Between 5-19 employees	Between 5-19 employees
Medium	Between 51-150 employees	Between 20-50 employees	Between 20-50 employees

Source: Malaysian SME Annual Report (2008)

Table 4. Measurement Construct

Constructs	Number of items	Constructs Sources	Likert Scale
Human Resource Practices - Human resource planning - Staffing - Job/Work Design - Training and Development - Performance Appraisal - Compensation - Employee Relations - Career Planning - Health and safety	64	Geringer et al., 2002	1=Not at all, 5=To a very great extend
Job Satisfaction	7	Geringer et al., 2002	1=strongly disagree, 5=strongly agree
Organisational performance	13	Delaney & Huselid, 1996; Hackman & Oldham, 1974; Geringer et. al, 2002 Khandwalla, 1977;	1=much lower, 5=Much Higher

Table 5. Reliability Coefficients for major variables

Variable	Number of items	Cronbach Alpha
Human Resource Planning	8	0.87
Staffing	7	0.80
Training & Development	9	0.95
Performance Appraisal	8	0.78
Compensation	5	0.70
Employee Relations and Communication	8	0.77
Health and Safety	6	0.95
Organisation Performance	13	0.90
Job Satisfaction	7	0.85

Table 6. Profile of respondents

	Frequency	%
<b>Human Resource Department</b>		
Yes	22	51.2
No	21	48.8
<b>Gender</b>		
Male	15	34.9
Female	27	62.8
<b>Level of Education</b>		
Certificate	9	20.9
Diploma	5	11.6
First Degree	21	48.8
Masters Degree	4	9.3
Phd	2	4.7
Professional Certificate	2	4.7
<b>Years of involvement in HR functions</b>		
Less than 1 year	1	2.3
1-3 years	10	23.3
4-6 years	7	16.3
7-9 years	10	23.3
10-12 years	7	16.3
13-15 years	2	4.7
More than 15 years	2	4.7

Table 7. Descriptive for major variables

HR Practices	Mean	Standard Deviation
Human Resource Planning	3.07	0.82
Staffing	3.00	0.77
Job Work Design	3.00	0.79
Training & Development	2.85	1.00
Performance Appraisal	3.26	1.01
Compensation	3.03	0.76
Employee Relations and Communication	3.24	0.82
Health and Safety	3.14	1.02
Job Satisfaction	3.40	0.60
*Organisation Performance	3.34	0.54

Table 8. Mean Differences between organisations with HR department and without HR department

Variable	Mean		t-value
	With HR Department	Without HR Department	
Human Resource Planning	3.24	2.89	1.44
Staffing	3.01	2.88	0.90
Job Work Design	3.06	2.84	0.91
Training & Development	3.14	2.55	2.03*
Performance Appraisal	3.69	2.81	3.06*
Compensation	3.01	2.97	0.513
Employee Relations and Communication	3.48	2.97	2.10*
Health and Safety	3.23	3.03	0.62
Job Satisfaction	3.60	3.12	0.71*
Organisation Performance	3.43	3.24	1.15

\*p&lt;0.05