

THE HUMAN SIDE OF SMALL AND MEDIUM ENTERPRISES

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ABSTRACT

The limited research conducted on Human Resource Management (HRM) in small and medium enterprises (SMEs) suggests that acquiring, developing, compensating and retaining employees is a major problem. A Queensland-wide study of Human Resource Management Practices in SMEs (with a sample of 431) found a surprisingly high take-up of human resource management practices. The present paper discusses this study, presents the results obtained and reflects on its implications for human resource management in SMEs.

INTRODUCTION

Although small and medium enterprises (SMEs) are important to national economies, human resource management (HRM) practices have received limited emphasis in the small business or SME literature (Purcell 1993). Interest has grown, however. For example:

- Marlow and Patton (1993) found small firms could use an HRM approach;
- Desphande and Golhar (1994), undertook a comparative study of HRM practices in large and small manufacturers in USA;
- Duberley and Walley (1995) found SMEs lacked strategic HRM in SMEs; and

- Bacon, Ackers, Storey and Coates (1996), however, conversely noted many SMEs applied HRM practices.

Further, a number of SME studies examined individual HRM practices, such as training or recruitment and retention of employees (Barber, Wesson, Robertson, and Taylor, 1999; Heneman and Berkley 1999). Many of the studies of employee management practices have been meta analyses of wider surveys. In such an analysis of survey data on selected Canadian industry-region combinations, Weber and Verma (1998) found SMEs are more likely to innovate when pursuing external and functionally flexible strategies. Using the United Kingdom Workplace Industrial Relations Survey of 1990, Bryson and Millward (1998) found differences in employee involvement practices between small and large establishments. Similarly, Rimoldi (1998) used Argentine's 1994 Economic Census data to analyse collective bargaining approaches in small enterprises. Industry studies have also been undertaken (e.g., Galang (1998) examined high performance work practices in chemical, petroleum refining, rubber, leather, metal and machinery manufacturers), as have regional studies (eg. Golzio 1998; Wagar 1998).

Neither the Australian small business nor the Australian HRM literature contains many references to HRM practices in SMEs. Many aspects of industrial relations in Australian small business have been examined (eg. Bray and Kelly 1989; Kitay and Sutcliffe 1989; Callus, Kitay and Sutcliffe 1992; Isaac 1993; Barrett 1995). However, most studies, such as the two Australian Workplace Industrial Relations Surveys in 1990 and 1995, have dealt with SMEs as part of larger research and have been the subject of meta analysis of small firm industrial relations (Barrett 1997; Barrett and Buttigieg 1999). A current longitudinal study of

small business that addressed some aspects of employment management through the introduction of 'business improvement management activities' should provide some useful comparison of data (*A Portrait of Australian Business* 1996).

What is true for human resource practices in larger organisations may not apply to SMEs. Differences in organisational structure and processes between large organisations and SMEs have been found and further research is needed to see how Australian SMEs respond to changing environmental demands.

A small pilot study of 31 SMEs in regional Queensland, Australia found less organisational change in SMEs than in large organisations (Wiesner and McDonald 1996). The study also found that, where organisational change occurs in SMEs, collective bargaining plays almost no part in the change processes (McDonald and Wiesner 1997). This reflects the low take-up of enterprise bargaining by Australian small businesses (Barrett 1995), despite an emphasis in devolving industrial relations to an enterprise level. The pilot study suggests a need for additional information about SMEs' HRM practices, leading the present survey of managers in 432 small and medium Queensland manufacturing enterprises that examined their recruitment methods, selection processes, compensation approaches, training and development strategies and performance appraisal policies. As studies on human resource management and other employee management practices that focus on SMEs are only emerging, the present paper fills some of the gaps in our knowledge of HRM practices in Queensland SMEs.

DEFINING SMES

SMEs may be defined in a number of ways (e.g., Johns, Dunlop and Sheehan 1989; von Potobsky 1992; Storey 1994; Cletcher-Gershenfeld, McHugh and Power 1996; Osteryoung, Pace and Constand 1995) and across countries and industry sectors (Atkins and Lowe 1996). SMEs have been defined through the number of employees, type of ownership, degree of independence, nature of

managerial processes, use of business planning, turnover rates and value of assets (Atkins and Lowe 1996; Bacon, Ackers, Storey, and Coates 1996; Duberly and Walley 1995; Hornsby and Kurato 1990; Joyce, Woods, McNulty, and Corrigan 1990, Osteryoung et al. 1995).

Atkins and Lowe's (1996) found that 34 of 50 studies used employee numbers as the criterion. However, there is no consensus between countries. Within the same country there may also be variations. For example, in America, upper limits as high as 500 and as low as 100 have been used to define a small business (Hornsby and Kuratko 1990; Osteryoung et al. 1995). In Britain, numbers as high as 500 have also been used (Duberly and Walley 1995), although 200 is a more common limit (e.g., Atkins and Lowe 1996; Bacon et al. 1996; Joyce et al. 1990).

There are few Australian studies that focus on SMEs as a discrete classification, although some small business and general surveys have categorised businesses and workplaces according to size (employment numbers). The most widely used Australian definition is the Australian Bureau of Statistics definition that suggests small businesses have fewer than 100 employees in the manufacturing sector and fewer than 20 in retail, wholesale, construction and service sectors (Johns and Storey 1983). This small business classification also requires an enterprise to be independently owned and operated, to be closely controlled by the owner/managers who contribute most if not all of the operating capital and to have principal decision making functions resting with the owner/managers (ABS Cat. No. 1321.0 1990). *A Portrait of Australian Business* (1996) divided small business into 'micro businesses' (businesses other than agriculture employing fewer than 5 people, which is also an ABS definition) and size categories of 1 to 4, 5 to 9, and 10 to 19 employees. Some other large studies, such as national surveys of human resource management practices in 1989 and 1993, defined small business as employing fewer than 100 employees. The next size bracket was 100-249 employees (Collins 1993). These studies looked at facets of organisational change and, given the size classifications,

provide a basis for comparing results with the current survey. Other relevant studies include the 1990 and 1995 Australian Workplace Industrial Relations Surveys (AWIRS 1990 and AWIRS 1995), in which workplaces were categorised as 5 to 19, 20 to 49, 50 to 99, 100 to 199, 200 to 499 and 500 or more (Callus, Morehead, Cully and Buchanan 1991; Morehead, Steele, Alexander, Stephen and Duffin 1997).

When focussing on human resource practices and organisational change, SMEs have been defined as organisations that employ between 20 and 200 employees (Baron 1995). Small businesses employ 100 or fewer employees, (following the ABS definition of small business in manufacturing), while medium sized businesses employ from 101 to 200 employees. A recent longitudinal survey of Australian small business found organisations that employed 21 to 200 employees constituted 6% of all businesses in Australia, but employed 28% of the workforce (*Portrait of Australian Business* 1997). If workplaces are restricted to those with more than 20 employees (as in the Australian Workplace Industrial Relations Survey of 1995), workplaces with between 20 and 199 employees make up 92% of all business and employ 56% of the workforce (Morehead et al. 1997). The number of employees in Australian SMEs has increased in recent years (Hemmings 1991), even during the 1990-91 recession (Bureau of Industry Economics 1994). SMEs with a workforce of 20 or more would be expected to have a management structure, although smaller organisations are likely to have less formal organisational structures and HRM practices (Callus et al. 1991; Olson and Terpstra 1992). While size may be only one of the factors that determine the characteristics of SMEs, the range from 21 to 200 was used in the present study, which is discussed in more detail in the following section.

THE PRESENT STUDY

A questionnaire was distributed to 1215 small and medium sized manufacturers, with follow-up interviews being undertaken with senior managers if respondents indicated a willingness to participate in a further extension of the

project. The survey collected information on Human Resource Management practices, other employee management practices, organisational change and a range of background information about the business and the respondent.

A pilot study was undertaken of SMEs in the Darling Downs region to test content validity. Based on this analysis a revised questionnaire was submitted to several senior academics in the HRM field and to a panel of SME managers for comment. The revised questionnaire was mailed to the 1215 Queensland SMEs on a database of manufacturers held by the Queensland Department of Tourism, Small Business and Industry.

Organisations were encouraged to respond by including a covering letter explaining the purpose of the survey and a reply paid envelope. Follow-up letters, an assurance of confidentiality, and participation in a draw for a one-day, tailor-made workshop for recipients who provided contact details were also used to attract responses. Follow-up telephone calls were made to 50 percent of non-respondents. After allowing for incorrect mail addresses, closed businesses and non-manufacturers, 431 usable questionnaires were returned, providing a 35% response rate.

Descriptive statistics were calculated to present demographic and organisational change results, which are provided as frequency and percentage distributions so trends can be identified (Healy 1991; Moore 1995). Cross-tabulation and the chi-square test were used to examine the relationships between size and various HR practices. The results obtained are discussed in the following section.

THE RESULTS OBTAINED

Sample Characteristics

Seventy six percent of respondents were small firms (100 or fewer employees) and almost all (96%) were more than five years old. Just under half (47%) were family owned and, of these, family members managed 65 percent. Very few were franchises (2%) and just under half (48%) operated in only one location.

The Queensland Department of Small Business and Tourism sample frame was intended as a database of manufacturers. However, using the Australian Bureau of Statistics industry categories, only 54 percent of respondents indicated that they were involved in manufacturing. Nevertheless, the proportion of respondents from the manufacturing sector is higher than in other recent surveys, principally because of its origin.

More than three-quarters (78%) did not employ a human resources specialist but, where a specialist was employed, it was in human resources, rather than in industrial relations or related fields. While over half (52%) had at least one union member, the majority (66%) stated that union members made up less than 10% of its workforce. In only 17% of responses did union members constitute more than 50% of the workforce.

A Profile of HRM Practices in Queensland SMEs

A range of human resource practices (recruitment and selection, training and development, performance appraisal) was included in the survey and a high level of adoption of these practices was found, which is at odds with Sisson's (1993) 'bleak house' scenario that suggested an absence of sound human resource practices. He assumed employees were more likely to be treated in unfair and arbitrary ways in organisations that do not pursue sound human resource practices.

Recruitment and Selection Practices

A number of recruitment practices were examined, as shown in Table 1. Informants were asked to identify the extent to which various recruitment practices had been used in the three

TABLE 1: Recruitment and Selection Practices in Queensland SMEs

Practices	Total % of SMEs	N.	Size	
			Small %	Medium %
Recruitment				
Newspaper	92	418	91	95
Government employment agency	66	354	66	66
Private employment agency*	71	370	65	90*
Referrals by employees	88	371	88	90
Referrals from other sources	76	339	75	80
Walk-ins	67	358	67	66
Radio	1	311	1	1
Selection				
Job analysis	85	1250	85	86
Written job description	96	1376	95	97
Informal selection procedures*	75	1246	82	71
Formal selection procedures *	86	1283	81	91
Application pro-forma *	67	362	64	76
Reference checks	99	405	96	99
Interview panel*	69	385	66	80
One-on-one interviews	96	404	96	95
Psychological testing*	26	370	20	45
Decision-making on selection				
Line managers make decision*	81	397	77	93
Other managers / employees have an input in the selection design*	89	390	86	96
Other employees have an input in the selection decision*	67	386	64	75*

* p<0.05.

years prior to the survey. Recruitment practices were largely conventional, with more than nine out of ten SMEs using newspaper advertisements for recruitment, while radio was not used. Medium and small organisations differed significantly in only one recruitment practice, with medium sized organisations using private employment agencies more.

Less than a third of respondents had job analyses for all positions. However, 86 percent did use job analyses for some positions. While almost all used job descriptions (99%), fewer than a half (45%) wrote such descriptions for all positions. There was a mix of formal and informal selection processes used when appointing employees, with both formal selection procedures (84%) and informal methods (79%) used together. Two thirds used

application forms but less than a quarter used psychological testing. One-on-one selection interviews occurred in almost all responding SMEs, although many used both interview panels and single interviewers. Nearly all followed up some applicants' references, although less than half did so for all applicants. There were significant differences between medium and small organisations in five selection practices. Medium size organisations used formal selection practices in general, application forms, interview panels and psychological tests more than did small organisations. Informal selection practices were used more by small organisations. Line managers made the selection decisions in eight out of ten responding organisations but other managers also had input in most SMEs, as did other employees (67%).

TABLE 2: Training and Development Practices in Queensland SMEs

Practices	Total % of SMEs	N.	Size	
			Small %	Medium %
Training and Development				
Formal training budget *	63	400	57	84
Does your business provide training	99	421		
Informal on-the-job training	98	415	98	99
Technical or vocational training ¹	76	414	75	81
Management and development training ² *	76	408	72	89
Introduced training where none formally existed*	76	403	70	93
Increase in training where previous program existed*	69	391	63	87
New career paths introduced*	74	403	71	83
Informal mentoring	77	398	76	81
Formal mentoring *	38	393	34	52
Computer-aided instruction	63	403	62	68
Who Provides Training?				
Formal in-house training provided by own staff *	83	405	81	92
Formal in-house training provided by external consultants *	73	408	67	84
External training (provided by training body/institution) *	82	410	79	91

* p<0.05.

1 ie., apprenticeships, training of young employees, retraining of older employees, especially due to demand in new technology;

2 ie., leadership, supervisory skills, personal communication, graduate and postgraduate sponsorship;

Training and Development

Almost all respondents (99%) provided training and development. However, only 63 percent had a formal budget allocation for training. Three-quarters had introduced formal training in the three years prior to the survey where previously there had been none, while 69 percent had increased training where such programs had previously existed. Table 2 shows the range of training and development practices that responding SMEs provided. There was a high incidence of apprenticeships, training young employees and re-training older employees, especially due to demands made by new technology. Attention was also paid to training in leadership, supervisory skills and personal communication and graduate and postgraduate sponsorship was provided in some cases.

Significant differences in approaches to training and development were found between small and medium enterprises. Medium size organisations were more likely to:

- have a formal training budget;
- provide management development training;
- have increased training where a programs previously existed;
- have introduced new career paths;
- provide formal mentoring;

- provide formal in-house training conducted by staff and consultants; and
- provide external training undertaken by a training institution.

Performance Appraisal

SMEs used formal and informal performance appraisal (PA) approaches. Formal appraisal was found in more than two-thirds of organisations (71%) and informal appraisal in almost three-quarters (74%). In almost all cases (93%), the line manager appraised employees. Table 3 suggests that the most common aspect of performance appraisal is the setting of objectives and, presumably, evaluating performance against the goals that are set. However, fewer than half used more complex appraisal systems, such as rating scales. Very few employed narrative essay forms. The results suggest there was a heavy reliance on management and supervisor control of appraisal functions.

Formal appraisal systems, rating scales and narrative essays, informal performance appraisal were more common in medium size organisations, while informal and peer appraisals were more common in small organisations. Line managers seemed to be more involved in PA decisions in medium size organisations than they were in small organisations.

TABLE 3: Features of Performance Appraisal Practices in Queensland SMEs

Practices	Total % of SMEs	N.	Size	
			Small %	Medium %
Performance appraisal practices				
Formal performance appraisal system*	71	408	65	89
Management by objectives	75	402	73	81
Rating scale*	47	387	43	60
Narrative essay*	16	382	12	26
Informal performance appraisal	74	390	74	75
Who conducts appraisals?				
Line manager*	93	380	90	99
Employee self-performance appraisals	49	297	44	56
Peer performance appraisals*	46	303	50	34

* p<0.05.

TABLE 4: Compensation Practices in Queensland SMEs

Practices	Total % of SMEs	N.	Size	
			Small %	Medium %
Compensation practices				
Use of job evaluations in setting pay levels	89	431	89	91
Pay levels based on awards classifications*	94	415	93	99
Performance based pay (PBP)	93	402	93	93
Competitive wages	86	380	84	88
Pay based on acquired skills	92	394	92	92
Group/team incentive programs	44	378	41	51
Pay based on seniority	36	377	38	32
Profit sharing/gain sharing schemes	39	384	36	47
Employee share scheme*	17	379	11	33
Individual incentive programs	51	380	49	56
Annual bonus	57	388	55	64
Benefits other than superannuation (eg life insurance, health insurance)*	34	376	29	47
Employees recognized in other ways than take home pay or compensation practices above	98	177	100	95

* p<0.05.

Compensation Practices

As can be seen in Table 4, the survey found that, notwithstanding the recent emphasis on enterprise bargaining, many SMEs relied on awards for pay and classification decisions, whether this was to determine a wage rate or as an underlying basis for the payment of over award rates. Medium size organisations used pay levels based on awards classifications, employee share scheme and benefits other than superannuation (eg life insurance, health insurance) more than their smaller counterparts.

Employment Relations Practices

Employment relations practices were used less often than the various HR practices already discussed. As can be seen in table 5, few respondents had formal regular meetings with union delegates, although this is more common in larger organisations. While half of the respondents employed at least one union member, there was little negotiation with trade unions. Formal meetings with union delegates or shop stewards were rare and informal meetings occurred in only a quarter of organisations. The incidence of formal

agreements with employees does not suggest respondents were consultative as joint employee-management consultative committees and work teams existed in a minority of the SMEs.

Individual contracts occurred in half of the SMEs surveyed. This is a much higher proportion than was reported in *A Portrait of Australian Business* (1996), where 23 percent of businesses with from 20 to 99 employees and 9 percent in organisations of more than 100 employees had individual contracts. A similar inconsistency was found in the incidence of agreement making. This may be owing to the manufacturing base in the present sample. The former distinguishes between registered and unregistered agreements. These have been combined in Table 6. There were also differences between the results of this survey and the 1995 Australian Workplace Industrial Relations Survey. In AWIRS 95, the incidence of written or verbal agreements in Australian SME workplaces was 44 percent for firms with 20 to 49 employees, 54 percent for firms with 50 to 99 employees and 63 percent for firms with 100 to 199 employees (DIR 1996).

TABLE 5: Employment Relations Practices in Queensland SMEs

HR Practices	Total % of SMEs	N.	Size	
			Small %	Medium %
Employment relations practices				
Formal agreements with employees*	61	413	45	22
Formal agreements with unions ¹ *	25	408	83	51
Informal agreement making with unions and/or employees	37	396	64	63
Individual contract with non-managerial employees*	50	402	54	40
Regular formal meetings with union delegate*	12	397	94	70
Informal meetings with union delegate*	25	397	83	52
Establishment of joint consultative committee*	39	408	68	44
Establishing work teams with direct responsibility for setting and achieving targets	48	404	54	46
Establishing other forms of self-management	16	311	85	82

* p<0.05.

¹ 'Unionisation' refers to the estimated presence of at least one union member in the workforce (Callus et al. 1991)

Differences between findings may be attributable to the specific questions asked and the period during which the surveys were conducted. Table 6 refers to arrangements that were in place at the last pay period in June 1995, whereas the present survey was conducted in July and August of 1997 in a period of decline in union density. The present study asked respondents to indicate whether they engaged in any of the practices shown in Table 5. It may be that respondents confused awards and agreements within the enterprise, as no distinction was made between enterprise agreements and other sorts of agreements in the question. McDonald and Wiesner (1997) have suggested that managers' are unclear about what constitutes an agreement, enterprise bargaining and the processes of agreement making. If such

confusion is present, it may extend to the distinction between awards and agreements.

IMPLICATIONS FOR SMES

The ability to compete effectively in a changing environment is a key to survival and growth. This means anticipating, responding and adapting to a changing environment (Bonvillian 1997; Decker and Belohlav 1997; Nadler and Shaw 1995). Nadler and Shaw (1995) argued that organisational capability (defined as the skills, abilities and competencies that are the unique product of the organisational system) is the fundamental source of sustainable advantage. The challenge for management is to develop organisations that can achieve such an

TABLE 6: Agreements and Individual Contracts in Small and Medium Sized Manufacturers

Size of Manufacturer	Enterprise Agreement (registered with industrial tribunal and unregistered) (%)	Award Arrangements (%)	Individual Contracts (%)
20-99	11.9	60.4	22.6
100+	12.9	15.3	9.0

Source: Adapted from Productivity Commission/Department of Industry, Science and Tourism (1997), *A Portrait of Australian Business: Results of the 1995 Business Longitudinal Survey, Small Business Research Program*, AGPS Canberra, Table 3.72.

advantage (Dunphy and Stace 1992; Limerick 1992; Nadler and Shaw 1995).

SMEs face difficulties in planning and responding to a changing environment because of their position in the marketplace. Joyce et al (1990) found the market was a major barrier to change for small firms. Market uncertainty makes it difficult for small firms to plan for growth and change, especially as they rely on the sales of larger organisations or the state of the industry in which they operate (Atkins and Lowe 1996; Jennings and Beaver 1997; Joyce et al. 1990). *A Portrait of Australian Business* (1996) suggested that smaller size firms were less likely to aspire to growth or to introduce new products and services. The impact of a turbulent environment on the viability of SMEs can be seen in the high exit rates reported by *Portrait of Australian Business* (1997), which suggested that a quarter of firms with 10 employees or less planned to close or sell within 3 years. This rate progressively decreased as size increased. In this present survey, 55 firms, representing 3% of the initial sample, were longer operating.

Jennings and Beaver (1997) distinguished between large organisations that strategically pursue competitive advantage through a process of strategic planning and small and medium sized firms' strategic planning, which they characterised as adaptive. The focus in such adaptive organisations is on manipulating limited resources to gain maximum short-term advantage in the face of environmental threats.

The present study suggested a relatively high level of adoption of standard human resource practices. However, collective and consultative processes were generally less common. With 98% of managers reporting that their business had altered its practices to achieve its goals and objectives, it seems many SME managers take a strategic approach to HRM. This is less clearly the case with other change issues.

Fisher and Dowling (1999) reported senior HR managers saw performance appraisal, recruitment, selection and training and development as the most important new HR policies, programs and systems in large

Australian firms. The present findings suggest this is also true for SMEs. The picture presented suggests the SME sector should not be seen as a 'bleak house.' The results suggest SME HR practices are more sophisticated than might have been expected. What is the significance of this finding? The more that is learned from observing SMEs, the fewer underground assumptions will be made. A better understanding of human resource practices may lessen the frustration small business owners experience as the result of HR problems.

With the exception of industrial relations practices, what are some tentative explanations for the relatively positive HR profile in SMEs? Storey (1992) identified increased competition as the main causes of the shift towards HRM in large British firms. Queensland SMEs may have had more specific triggers for adopting good HR practices. One explanation may be the fact that 70% of the managers in the survey held a higher educational qualification than a secondary school certificate. It was evident from our interviews with SME managers that they have little understanding of management theory but that they were familiar with many of its components. Bacon et al (1996) reported similar findings. It is true that large organisations are more likely to have the resources, technical knowledge and skills to implement large-scale HR programs and it is also true that the term 'bleak house' could be used to label some SMEs, but the present results suggest it is inaccurate to assume they were a norm in the SME sector.

Bacon et al (1996) suggested large organisations have much to learn from the informal nature of change in small businesses and the present study supports that view. Where SMEs have implemented good HR practices they may have an advantage over large organisations. For example, their informal organisational structures and relationships may mean forces that traditionally restrain change or maintain stability have less influence. Additionally, their flexibility and small size means changes in practices can be adopted more quickly (Marlow and Patton 1993) than in large organisations, where mechanistic and bureaucratic structures

can slow the implementation of good HR processes (Robins, Waters-Marsh, Cacioppe, and Millett, 1994).

The management process in a small firm is also different as it is characterised by the personal preferences and attitudes of the owner and/or managers. The close interaction of management with operations and employees provides an opportunity for direct leadership and the communication of aspirations, plans and activities. The permeation of a strong culture is facilitated, which can assist in implementing new HR practices and in overcoming a resistance to change. This is in contrast to large firms where the communication of new practices can be problematic (Jennings and Beaver 1997; Johns, Dunlop and Sheehan 1983).

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