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## The importance of human resources management for small businesses in South Africa

### Abstract

The majority of SMEs fail in the first five years of operation (Cant and Ligthelm, 2003). Human resource management (HRM) has been identified as a crucial key success factor for SMEs in today's world. This research study investigates small business owners' perception of the importance of HRM. The objective of this paper is to determine the perceived importance of human resources (HR) among South African SMEs and the management of it. A questionnaire was constructed and judgement sampling was used to gather the responses of 88 small business owners. The research revealed that the majority of SMEs have HR practices of some sort in place, as well as areas to improve on HR practices. The challenge now is to further increase the adoption of HR management and practices among small businesses in South Africa to ensure their success, as they play a vital role in the South African economy.

**Keywords:** South African SMEs, developing countries, human resource functions, human resources management, HR, HRM.

**JEL Classification:** M19.

### Introduction

During the developing stages, SMEs tend to be more vulnerable as they encounter many difficulties due to the lack of resources, namely financial and human capital resources. SMEs play a crucial role in developing countries such as South Africa, as the country faces significant unemployment and income distribution challenges (Cant & Wiid, 2013). Approximately 91 per cent of formal business entities in South Africa are SMEs, contributing between 51-57 per cent of GDP and 60 per cent of employment (Kongolo, 2010). However, it is estimated that up to 63 per cent of South African SMEs do not make it past the second year of trading (Robert, 2010). Initially, the majority of SMEs focus on the financial and marketing aspects of their business. However, at a later stage, HR becomes a concern (Dunn, Short & Liang, 2008). Mazzarol (2003) highlights that, as SMEs grow and the number of staff members increases, they are required to learn how to develop and implement HRM. Many owners and/or managers of SMEs are forced to handle, among other functions, HR activities that they are usually poorly equipped to do (Mazzarol, 2003).

The main objective of HR is to create and maintain an efficient workforce that is able to meet the organization's needs (Mayhew, 2014). Effective HRM can be a competitive advantage for SMEs, because experienced and motivated employees are seen as valuable resources, which have a significant influence on the overall performance of a business

(Klaas, 2003; Mayhew, 2014; Ray, 2014). Businesses with successful HRM practices are likely to have lower absenteeism and employee turnover rates and better skills development and retention (Asadii, 2012). Due to the characteristics of SMEs, employees are also usually required to perform activities in various business functions. Therefore, HRM plays a crucial role in ensuring that the right employees are hired to meet those demands and that there is relevant support structures available to ensure work productivity.

Research on HRM is generic and predominantly focused on large organizations (Dunn et al., 2008). Little research has been conducted on SMEs and more specifically in developing countries such as South Africa. The findings of HRM for large organization or in developed countries cannot be generalized for SMEs in developing countries, as they each face different barriers specific to them (Kapurubandara & Lawson, 2006). Therefore, the aim of this study was to investigate the SMEs' perception on the importance of HRM. In the subsequent section of the study, the objectives and research methodology used in the study are provided, followed by a review of the available literature. The study concludes with a discussion of the research findings and recommendations and concluding remarks are made.

### 1. Literature review

**1.1. SMEs in South Africa.** The National Small Business Amendment Act of South Africa, 2004 defines an SME as "any separate business entity, including co-operative enterprises and non-governmental organizations, managed by one owner or more and is predominantly carried on in any sector or subsector of the economy, which can be defined as a micro-, a very small, a small

or a medium enterprise depending on the number of employees, total annual turnover and total gross asset value” (Government Gazette of the Republic of South Africa, 2004). South African SMEs are broadly classified as organizations that have between 1-200 employees, that make a total annual turnover of less than R50 million and possibly own assets up to the value of R18 million (Mahembe, 2011).

**1.2. SMEs and HR.** SMEs’ productivity and likelihood of survival may increase if they adopt HRM practices (Bacon & Hoque, 2005). Carlson, Upton & Seaman (2006) state that managing employees effectively has a positive effect on organizational performance. However, there is a lack of interest with regard to HRM in SMEs (Anderson, 2003). Managers/owners of SMEs often view HR practices as costly, bureaucratic and time consuming (Anderson, 2003). Therefore, many SMEs are informal in terms of HR practices and are less likely to practice HRM compared to larger organizations (Bacon & Hoque, 2005). Dunn et al. (2008) state that the following functions of HR management are important. These will now be discussed.

- ♦ *Hiring and firing of employees.* Hull (2013) states that one of the most crucial and challenging decisions faced by managers/owners is hiring employees. Hiring the ‘right’ employees is good for business, as they are likely to attract more customers and to be more productive (Nichols, 2006; Truck, 2014). Shamis (2014) points out that hiring great employees is fundamental to the success of any business, as hiring employees who cannot meet the demands of the business or do not fit the business culture, is a huge cost to the organization (Hull, 2013). Mazzarol (2003) states that one of the main problems experienced by SMEs is finding and retaining high quality employees.
- ♦ *Analyzing and classifying work tasks.* Another important role of HR is to analyze and classify work tasks. Managers/owners should do this before hiring employees to ensure that they know exactly what is needed or expected from an employee (Hull, 2013). Nakhata (2008) states that work tasks need to contribute to a desired goal or output that meets the business’s needs and long-term goals. Adler (2013) emphasizes that clarifying expectations upfront and clearly indicating the performance requirements of a job is good management practice. When employees do not have a clear purpose, they tend to lack enthusiasm and are less likely to become involved or take on new responsibilities (Govindarajulu & Daily, 2004).
- ♦ *Motivating employees.* Nohria, Groyberg & Lee (2008) state that one of the most challenging tasks of a manager/owner is to motivate employees to always do their best. The reason being that people are different and there is no one-size-fits-all approach to motivating them (Lazenby, 2008). Motivating employees is linked to other aspects of HR management, namely creating a culture that promotes teamwork and collaboration, designing jobs that are meaningful and interesting, providing those that excel with promotion opportunities, implementing transparent and fair resource allocation processes and having an effective reward system which is linked to performance evaluations (Nohria et al., 2008).
- ♦ *Training and development.* SMEs are generally hesitant to provide funds for employee training and development (Mazzarol, 2003). Not only is training and development expensive, but it also incurs loss of work, because employees are attending the training sessions (Frost, 2014). However, Sarvadi (2005) states that training and development should be viewed as an investment and not an expense, because it is essential and not optional for the success of the business. In order to retain the high quality employees that the owners/managers have hired, it is fundamental to have training and development, because it helps to build loyalty (Lipman, 2013). Furthermore, training and development may result in improved job performance, acquisition of new skills and self-efficacy or self-management skills of employees (Aguinis & Kraiger, 2009). An organization as a whole may also experience improved overall performance, increased quality and quantity of output and enhanced reputation (Aguinis & Kraiger, 2009).
- ♦ *Performance evaluations.* Performance evaluations are the formal process of monitoring employees in order to improve performance and productivity (Shahzad, Bashir & Ramay, 2008). Rynes, Gerhart & Parks (2005) suggest that performance evaluations improve performance in two ways: through constructive feedback on individual performance and through administrative decisions linked to rewards and punishments aimed at motivation. Therefore, the purpose of performance evaluations is to provide employees with information that enables them to perform better and give them an incentive to use that information (Rynes et al., 2005). Managers/owners need to conduct performance evaluations to ensure that employees are performing as expected (Hamlett, 2014).

- ◆ *Compensation and benefit plans.* Compensation and benefit plans consist of monetary and non-monetary components such as pay scales, reward programs and benefit packages, which allow an organization to compete for high quality employees (Lister, 2014; Johnson, 2014). Johnson (2014) states that compensation and benefit plans affect recruitment and retention rates, as well as employee satisfaction. Furthermore, Carlson et al. (2006) state that the design of compensation and benefits used by an SME is critical to its success. However, it should be designed in a manner that is fair to ensure employee satisfaction (Li, 2011).
- ◆ *Personnel policies and procedures.* Moore (2014) defines policies as guidelines which regulate employee actions and procedures as customary methods of handling activities. According to White (2014), HR policies and procedures consist of employment and work policies, work schedules, performance evaluation guidelines and employee remuneration and benefit plans. Policies and procedures act as a guide for all employees on how they should conduct themselves (Amico, 2014).

**1.3. Factors influencing HRM adoption.** Low HRM adoption rate is a concern, as there is growing evidence that HRM not only increases employee welfare and performance, but also improves the organization's overall performance (Dunn et al., 2008). Urbano and Yordanova (2008) add that HRM improves the long-term competitiveness of SMEs by developing and utilizing employees and encouraging them to pursue the interest of the organization. There are internal and external influences on the adoption of HRM in SMEs (Bacon & Hoque, 2005).

According to Bacon & Hoque (2005), internal influences include:

- ◆ *Workforce skill mix and employee dependency.* SMEs that hire more low-skilled employees are less likely to adopt HRM.
- ◆ *Professional management training.* SMEs that lack employees with specialized knowledge of HR practises are less likely to adopt HRM.

On the other hand, Bason and Hoque (2005) state that external influences include:

- ◆ *Corporate governance and proprietary control.* SMEs that are part of large multi-site groups and not family-owned businesses are more likely to adopt HRM.
- ◆ *The wider business community.* SMEs that attend seminars or are part of associations that provide business advice are more likely to adopt HRM.

- ◆ *Relationship between SMEs and larger customers.* SMEs that work with larger customers are more likely to adopt HRM.
- ◆ *Trade unions.* SMEs that are involved with trade unions are more likely to adopt HRM.

On the other hand, according to Urbano and Yordanova (2008), previous studies indicate that the following factors influence the adoption of HR management:

- ◆ *Size of an organization and the presence of an HR department.* Larger SMEs with more employees are more likely to have an HR department and adopt HRM.
- ◆ *Type of organization and its strategy and planning.* SMEs with business plans, pursuing growth strategies and non-family businesses are more likely adopt HRM.
- ◆ *Type of industry the organization is in.* SMEs that are in exporting, franchising or working with larger organizations are more likely to adopt HRM.
- ◆ *Decision-making style of the organization.* SMEs that have progressive decision-making ideologies are more likely to adopt HRM.
- ◆ *Macro-environmental factors.* SMEs that are more attuned to the market and economic conditions and legal regulations are more likely to adopt HRM.
- ◆ *Availability of resources.* SMEs with more resources available are more likely to adopt HRM.

It is evident that there are various factors influencing the adoption of HRM practices in SMEs. In South Africa: the "Rainbow Nation", the increasing diversity among the workforce with its different demands that need to be addressed emphasizes the necessity of having HRM in place (Anderson, 2003). Diversity requires collaboration between people of varying competence levels, cultures and ages (Anderson, 2003).

## 2. Research objectives

This study aims to determine whether SMEs recognize the importance of human resources management (HRM) in their businesses. The study further aims to determine which specific areas of HRM are important to South African SMEs; which specific areas of HRM South African SMEs need assistance with and how South African SMEs manage their human resources.

## 3. Methodology and findings

The research followed a quantitative analysis of the research question to establish the perceived

importance of HR among South African SMEs. To address this problem adequately, the research methodology was based on the primary data collected from South African SMEs. To achieve a low level of error, judgement sampling method was used and a total of 88 usable responses were received.

The questionnaire consisted of a set of questions that relates to demographical information. It was found that most of the respondents were female (58.6%) with more than half older than 40 (56.9%). A large portion of the respondents were owners of their businesses (79.0%), some of which were also managers of their businesses. The SME sector that these businesses operated in consisted mainly of construction (20.0%), business services (10.0%), manufacturing (10.0%) and retail (7.1%). A large proportion of the respondents' businesses have existed for less than five years (60.8%), while one quarter of the respondents' businesses have existed for six to ten years (25.7%). Almost half of the respondents (41.8%) reported that their annual turnover was less than R100 000.

The second set of questions investigated the perceived importance of specific HR areas and how HR is managed. The main constructs of this study are specific HR areas and perceptions of HRM which were measured through Likert-type scales. The basic Likert scale consisted of five scale points

with labels ranging from strongly disagree to strongly agree. The data were quantified and analyzed by examining the frequency of occurrences and the importance of the problem. A frequency distribution was used once all the data had been accumulated. The research findings pertaining to HR aspects are discussed below.

#### 4. Research findings

Descriptive statistics are used to describe:

- ◆ Which specific areas of HRM are important to South African SMEs.
- ◆ Which specific areas of HRM do South African SMEs need assistance with.
- ◆ The perception of how South African SMEs manage HR.

##### 4.1. Descriptive analysis on which specific areas of HRM are important to South African SMEs.

The participants were asked to select their level of agreement or disagreement with the importance of seven listed HR management tasks. The levels of agreement were combined for Strongly Agree and Agree and for Strongly Disagree and Disagree to a three-point scale due to an inadequate sample size. Most of the respondents (55.7% and more) strongly agree or agree that all of the listed HR management tasks are important for a business.

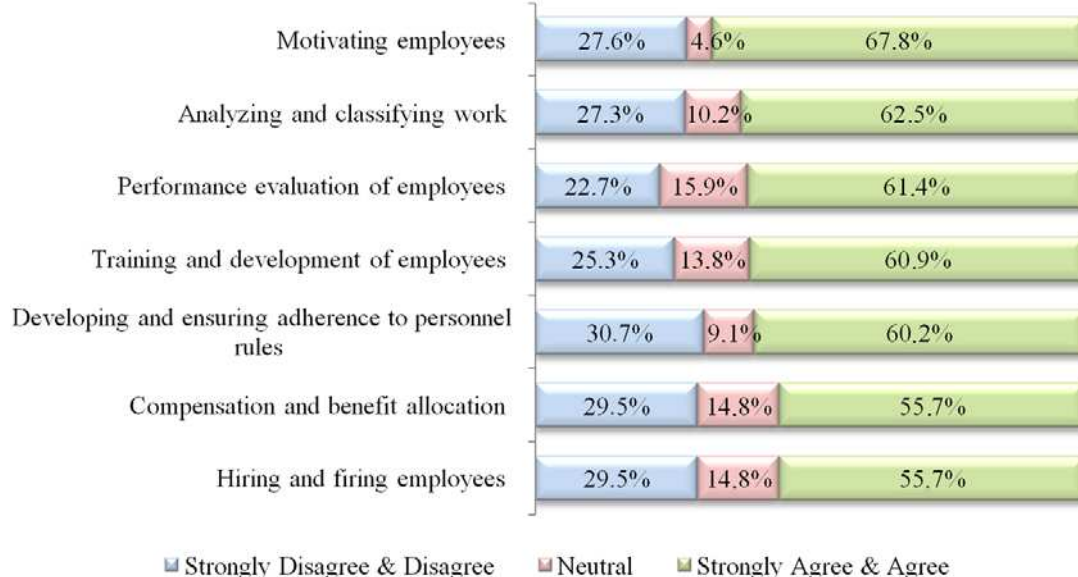


Fig. 1. Levels of agreement with the importance of HR management tasks

**4.2. Descriptive analysis on which specific areas of HRM do South African SMEs need assistance with.** The participants were asked to select the listed HR tasks which they need assistance with. Seven different tasks were listed and the percentage of respondents who selected each task was calculated (Figure 2).

All of the listed HR tasks were selected to indicate

that the respondents needed help with those tasks. The top four tasks identified for help by more than half of the respondents are:

1. Training and development of employees.
2. Analyzing and classifying work.
3. Motivating employees.
4. Performance evaluation of employees.



Fig. 2. Percentage of respondents who indicated that they needed help with selected HR tasks

**4.3. Descriptive analysis on the perception of how South African SMEs manage HR.** The participants were asked to select the level of agreement or disagreement with the nine statements which describe

perceptions of how HR is being managed. The levels of agreement were combined for Strongly Agree and Agree and for Strongly Disagree and Disagree to a three-point scale due to an inadequate sample size.

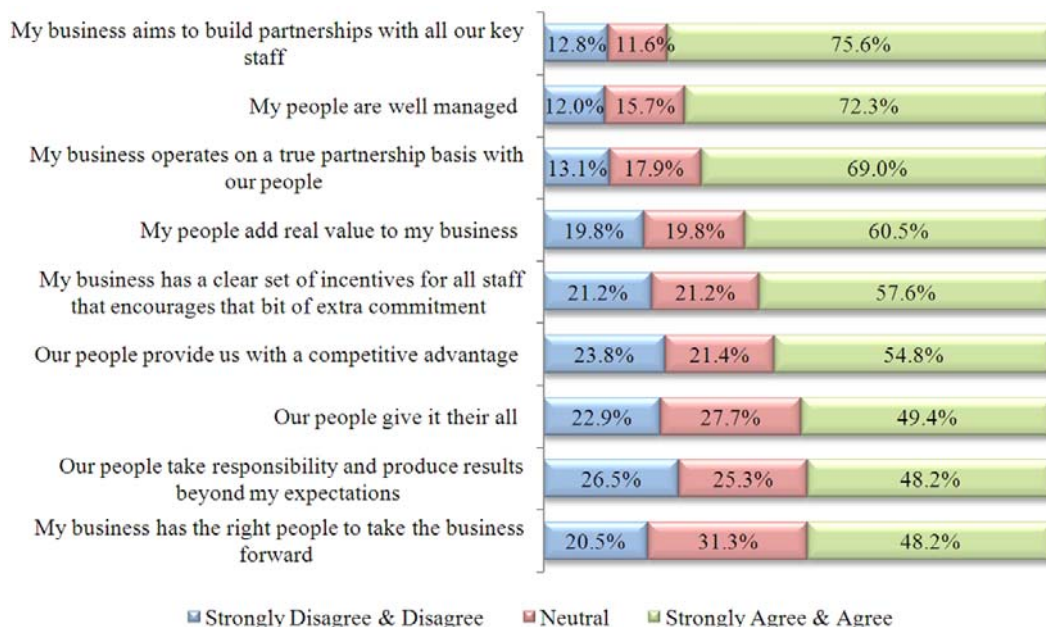


Fig. 3. Levels of agreement with how HR is being managed

Far more respondents strongly agree or agree with all of the statements on how HR is being managed than those who Strongly Disagree or Disagree. Most of the respondents (55.7% and more) strongly agree or agree that all of the listed HR management tasks are important for a business.

From Figure 3, it can be seen that more than 50.0% of the respondents strongly agree or agree with the following statements:

- ◆ My business aims to build partnerships with all our key staff.
- ◆ My people are well managed.
- ◆ My business operates on a true partnership basis with our people.
- ◆ My people add real value to my business.
- ◆ My business has a clear set of incentives for all staff that encourages that bit of extra commitment.

- ◆ Our people provide us with a competitive advantage.

Just below 50.0% of the respondents strongly agree or agree with the following HR management statements:

- ◆ Our people give it their all.
- ◆ My business has the right people to take the business forward.
- ◆ Our people take responsibility and produce results beyond my expectations.

### Conclusion

HR plays a crucial role in the performance of any organization and it is fundamental to understand how to manage HR (Kishore, Majumdar & Kiran, 2012). However, due to the size and lack of resources of SMEs, many do not have formal HR departments or professionals, which results in difficulty recruiting



and retaining employees (Bhatti, Syed, Shah & Shaikh, 2012). However, it is important for SMEs to assume the role of HRM, as it will not only improve productivity and the quality of work life for employees, but also comply with laws and regulations, enhance workforce flexibility and gain a competitive advantage (Bhatti et al., 2012). Since the beginning of the 21<sup>st</sup> century, there has been a shift in what is considered as the competitive advantage for SMEs. Important factors such as technology, finances and the production process have decreased in significance, whereas other factors such as employees and their intellectual capital, skills, creativity and information have gained more importance. It is for these reasons that HRM has gained more importance in ensuring the success of SMEs compared to the past period (Ceranić & Popović, 2009). In order to ensure effective HRM, specific HR functions discussed earlier need to be addressed (Bhatti et al., 2012).

The main aim of this study was to determine whether SMEs recognize the importance of HR management specifically with regard to which specific areas of HRM are important, which specific areas of HRM do SMEs need assistance with and the perception of how SMEs manage HR.

The study revealed that most of the respondents strongly agree or agree that HR management tasks such as analyzing and classifying work; hiring and firing employees; motivating employees; training and development of employees; performance evaluation of

employees; compensation and benefit allocation; developing and ensuring adherence to personnel rules are important for a business and that they need help with these HR tasks. The majority of the respondents indicated that their HR is in place.

It is evident from the study that motivation can be problematic within a small business, as the majority (67.8%) of the respondents had rated it as important and (55.8%) had indicated that they need assistance/help to motivate their staff. Almost half (49.4%) of the respondents indicated that their staff members give it all, meaning that staff members are motivated to do their best. Staff members who are not motivated can be the result of poor recruitment and selection processes; poor job description and job evaluation; performance evaluations, remuneration practises, staff training and development, etcetera. It is, therefore, recommended that short learning programs that focus on human resource management in small businesses be developed and that small business owners enrol for these short learning programs.

Given the small sample size that was used ( $n = 88$ ), the results only give a general indication of human resources management (HRM) practices in South African SMEs. Therefore, the variables identified cannot be generalized as being representative of all South African SMEs. Further research in this area is, therefore, recommended.

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