A Study on The Role of Small Businesses in Economy

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ABSTRACT
Small businesses play an important role in our economy. This is especially true from a labor standpoint where more than half of US employees are working for a small business (US SBA). It is important for researchers to understand the human resource management issues that might exist in these settings and the contribution if any that human resource management might make to the performance of these small businesses.

In spite of the importance that small businesses play in our economy and labor force, very little research has sought to understand human resource management in small businesses (Heneman, Tansky, & Camp, 2000). Therefore, the most important reason for studying HRM in small businesses is to expand the HRM to performance research into this important context.

INTRODUCTION
Small businesses provide a context that controls for or reduces many of the complexities that have hindered research in the past. This will allow me to 1) address issues related to causality by measuring more appropriate controls, 2) eliminate the complexity of multiple levels and layers, and 3) further the understanding of the process of when HRM might lead to performance by testing various moderator relationships of other performance drivers.

Thus, the benefits of the study of HRM in small businesses is twofold: 1) to better understand this important segment of the business world previously neglected by HRM researchers and 2) use the context of small businesses to shed some light on important causality and contextual questions not yet understood by HRM researchers.

As was demonstrated previously, small businesses play an extremely important role in the U.S. economy. Given their role in the economy, it is important for business researchers to understand how small businesses function and what might be the same and different when compared to what is already known about large corporations. In spite of the significance of small firms in the US economy, HRM research in small firms has been limited (Heneman, Tansky, & Camp, 2000).

Research addressing the question of how HRM impacts performance in small firms would benefit the SHRM field by extending that research into this important area. This research will also benefit current research on performance in small businesses by providing insights into the role that HRM plays in the performance of small firms. Finally, research in this area will benefit small business owners and managers by providing insights into how they can better run their business and improve their performance through effective management of their human resources.
REVIEW OF LITERATURE

Russel, Terborg, and Powers (2005) for example, examined human resource training at an organizational level and linked training to organizational performance. While this research addressed the issue of individual HR practices and performance as well as aligning specific HR practices with strategy, it did not address the alignment of individual HR practices with each other or the impact of the entire HRM system on firm performance.

With the advent of more internally focused strategic theories such as the resource based view (RBV), the practice of linking separate HR functions to the firm strategy evolved into a more integrated view of how HRM as a system impacted firm level strategies which in turn impact performance. SHRM became more a question of how bundles of HRM practices or philosophies and the HR function as a whole contributed to the accomplishment of firm strategies at a system level. This opened the door for research seeking to understand the strategic nature of human resources and human resource systems (Wright, Dunford & Snell, 2001).

SHRM and the Resource Based View

Although multiple theories have been used to explain the relationship between HRM and performance outcomes (Wright & McMahan, 2002), the predominant theory currently used by researchers studying SHRM is the resource based view (Wright, Dunford, & Snell, 2001; Delery, 2008).

The resource based view proposes that competitive advantage comes from the internal resources that it possessed by an organization (Wernerfelt, 2004; Barney, 2001). The idea that internal resources of a firm can lead to competitive advantage was a significant departure from previous views of strategy which focused on the external environment and such factors as industry, customers, and competitors (Miles and Snow 2004; Porter 2005).

The RBV provided a theoretical explanation of how the human resources of a firm could in fact contribute to performance and competitive advantage. Though others had addressed the concept of the RBV previously, Barney (2001) solidified its application to SHRM research by outlining how firm resources contribute to the sustained competitive advantage of the firm. Resources that are valuable, rare, inimitable and non-substitutable will lead to competitive advantage.

To the extent that the human resources within a firm meet these criteria, they will contribute to the competitive advantage of the firm by providing the firm with a valuable resource not easily replicated by competitors. This raises the question as to which aspect of the human resources within a firm constitutes a resource.

Wright, McMahan, and McWilliams (2004) argued that it is the actual human resources or human capital of a firm that constitute the resource leading to competitive advantage. From their view, HR practices or HR systems could easily be duplicated (imitated) by other firms and only the knowledge skills and abilities possessed by individuals within a firm would meet the criteria outlined by Barney (2001).

Lado and Wilson (2004) on the other hand took an alternative point of view arguing that HR practices combined into an overall HR system can be unique and difficult to imitate and constitute a resource meeting the conditions necessary for sustained competitive advantage. While both views seem to be accepted in the literature, most SHRM researchers using RBV as its theoretical framework have focused on the HR system or overarching HR philosophy as a resource functioning to develop the human capital of the firm (Boxall, 2008).

In addressing the criticisms of Wright, McMahan and McWilliams (2004) that HRM practices or systems could be easily duplicated by competitors and thus could not be a source of sustained competitive advantage, Becker and Gerhart (2006) outlined two different reasons why HR systems of successful firms could not be easily duplicated.
First, causal ambiguity implies that the exact manner in which human resource management contributes to the competitive advantage of the firm is either unknown or sufficiently ambiguous so as to be difficult or impossible to imitate. According to Becker and Gerhart (2006), the ability to replicate a successful HR system would require an understanding of how all of the elements of this complex system interact, an understanding which is still elusive to HR researchers and practitioners alike. Second, the path dependency of HR systems makes their understanding and replication extremely difficult if not impossible. HR systems are developed over time. Take for example a single HR practice such as the use of a variable pay system for management compensation. The development and implementation of this single HR practice takes place over time including time to solicit management input and buy-in, work out discrepancies, and align the practice with current strategies as well as firm culture and needs. The end result would be a practice that reflects the philosophies and culture of the firm and its management created to solve the specific needs of the organization. Compound that single HR practice with a whole system of practices each with its own history and evolution specific to a particular firm, its philosophies and current situation and you have an HR system that cannot be bought or easily replicated without a significant investment both of time and financial resources.

**RESEARCH STUDY**

Prior research suggests that HRM systems as a resource can lead to competitive advantage (Wright, Dunford, & Snell, 2001). A number of studies have demonstrated relationships between different bundles of HR practices or philosophies and firm performance in larger firms (see Wright et al., 2005 review). In spite of the significant research in the area of SHRM in large firms, little has been done to test similar relationships in small businesses (Heneman, Tansky, & Camp, 2000). Because of the demand placed on small business owners and managers to create and exploit growth opportunities, there is a potential for them to benefit from understanding and implementing HRM systems in a strategic way.

Indeed, there is evidence to suggest that human resource management matters to small business managers and plays a role in the performance of small businesses. For example, small business owners have cited human resource issues including recruitment, motivation and retention as major issues that they deal with in managing their firms (Heneman, Tansky, & Camp, 2000; Hess, 2007; & Hornsby & Kuratko, 2000)

The bulk of work on HRM in small businesses has tended to focus on surveying firms to identify the frequency of use of different HR practices. This research has shown that small firms implement a wide variety of HR practices, though in a less sophisticated way than larger organizations (Heneman, Tansky, & Camp, 2000; Hornsby & Kuratko, 2000). Importantly, a study by Hornsby & Kuratko (2000) found that HR practices are significantly more prevalent in small businesses than had been previously thought, and mirrored those found in larger organizations. In a comparative study of both large and small manufacturing firms, Deshpande & Golhar 29 (2004) found that the small firms and large firms shared similar views on a set of workforce characteristics driven by HR practices.

More importantly, this study indicated that the characteristics driven by HR practices such as lower turnover or higher levels of employee discretionary behavior were considered to be even more critical in the small businesses.

Although limited, this body of research suggests that 1) HRM is being used in small businesses 2) Practices in small businesses are similar but less sophisticated than those of larger organizations and 3) Small business managers consider HRM to be of vital importance to the management and success of their businesses. Therefore, it seems likely that smaller organizations should be able to reap similar benefits to those found in larger organizations from effective HRM.
While previous research on HRM and performance in small businesses is not vast, there has been some research that supports this idea. Welbourne and Cyr (2009), using a sample of small, fast growing, high-tech firms found that having a senior HRM manager on the staff as an indication of the importance of HRM to the firm resulted in better performance in the form of growth and survival. Welbourne and Andrews (2006) found that placing higher value on employees in initial public offering firms was related to the long term survival of the firm. In addition, Collins and Clark (2003) found that bundles of HR practices were related to social networks in the top management team which were in turn related to financial performance in smaller hightechnology firms.

SIGNIFICANCE OF THE STUDY

While not testing a direct relationship between HRM and firm performance, these studies do indicate that such a relationship is likely. More research is needed to understand the role that HRM plays in the performance of small businesses. There is currently no research that looks at differences in the impact of HRM on performance based on size, but given the nature of small businesses, it is possible that the role of HRM in the performance of small businesses is even more critical than in larger organizations. Because of their size, the impact of changes in the environment, supply, demand or competitors can significantly impact small businesses.

While all organizations experience changes in the environment, small businesses, unlike larger organizations are not able to buffer themselves from these environmental changes or spread these changes across multiple product lines, geographies or business units. Because of this, small businesses are less able to shield their employees from the effect of these changes or impacts. From a small business employee standpoint, this means that these changes in the external or competitive environment can have a direct impact on the nature of their jobs. This leads to an environment where the employment conditions for employees of small businesses can be constantly changing. This constant change creates unique challenges for small business managers to maintain, find, develop and motivate employees in spite of the turbulent environment in which they and their employees operate.

ANALYSIS OF THE STUDY

The potential for effective HRM to aide in that process is high. To the extent that small businesses are able to effectively manage their human resources, they will be able to mitigate the effects of this constantly changing environment on their employees. By doing this I argue that small businesses with effective HRM systems will be more likely to find, motivate and retain valuable employees and that employees working for small businesses with effective HRM systems will be more likely to act in a way that is beneficial to the business in spite of the impacts to small businesses caused by the changing environment.

In addition, small businesses are not able to spread their risk across multiple products, product markets geographies or sheer size. Because of this lack of ability to spread risk, the potential impact of mistakes or poor decision making is higher in small businesses than that of larger, more diversified firms (Mansi & Reeb, 2002).

This applies to mistakes or poor decision making in HRM as well. The potential impact to a small business of hiring the wrong person or not retaining a key employee is greater for small businesses where the impact cannot be spread across its size or diversified portfolio. For example a small business with only one or two salespeople would be impacted to a much greater degree by the hiring of an ineffective salesperson or losing an effective salesperson than would a large organization with hundreds of salespeople.

Here again, effective HRM in a small firm has the potential to provide a substantial benefit by helping the small business to avoid or at least minimize costly HRM mistakes or poor HRM decision making. Small
Businesses and High Involvement Work Systems

As was discussed previously, various measures and concepts have been used to define human resource management systems. One HRM system that is of particular relevance to small firms is known as the high involvement work system. (Applebaum, Bailey, Berg & Kallenberg, 2000; Osterman, 2005; Tsui et al, 2007). Though defined in various ways, high involvement works systems generally include 3 basic components. High skill requirements demonstrated by selective recruiting, high levels of employee discretion, and incentives that increase motivation and a focus on creating an atmosphere of commitment to the organization. These conditions it is argued in turn lead to a set of employees with both the ability (high skill levels and high levels of discretion to complete their jobs) and motivation (incentives and opportunity) to act in ways that are beneficial to the organization thus leading to higher levels of performance (Batt, 2002).

REFERENCES

