



# Human Resource Management in Small and Medium Sized Enterprises (SMEs). A Literature Review

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## Abstract

*Literature in the discipline of Human Resource Management (HRM) is mostly based on research conducted in large, formal and established firms. However, most people in developing economies like Zimbabwe are employed by the Small and Medium Sized Enterprises (SMEs) which, unlike large firms, operate informally. As such, it follows that a body of literature focusing on people management practices in SMEs. This paper steps in to close this gap in literature by systematically examining literature informing the practice of HRM in Small and Medium Sized Enterprises (SMEs). The methodology used to examine the literature entailed identifying studies related to HR Management in SMEs in peer-reviewed journals were searched on the Academic Search Premier, ERIC, Business Source Elite and Business Source Premier databases. Boolean logic was then used to refine the literature searches within the range of 100–150 hits per keyword search. This had the effect of focusing on the arguments making up this paper. The findings indicate that extant though HR management functions carry the same nomenclature between small and large firms, in practice there is a difference. Whilst, HR management in SMEs is informal, cheap, eclectic and driven by non-professionals, in large firms, HR is the hands of professionals and as such it becomes formal, expensive and dominant in the HR management discourse. The study recommends that future researchers should refocus their attention to HR management in SMEs as the sector is a major contributor to economic development in developing countries and as such demands research attention.*

## 1. Introduction

Most research attention in the field of Human Resource Management (HRM) is mostly targeted at large companies at the expense of Small and Medium Scale Enterprises (SMEs) (Saridakis, Muñoz Torres, & Johnstone, 2013). Therefore, as Richbell, Szerb and Vitai (2010) observe, mainstream human resource literature takes little account of the situation of SMEs. This is reflected in the acute shortage of literature on HR practices in SMEs. This paucity of empirical literature relating to SMEs lends justification to this research, which to some extent, is an attempt to cover the gap from the perspective of SMEs in Zimbabwe.

## 2. Materials and methods



This paper is based on a secondary literature review to examine the contextual factors informing HRM in Small and Medium Sized Enterprises (SMEs). To strike a balance between the most recent literature and the need for an in-depth analysis, literature was systematically searched, and the identified studies were matched against a preselected criterion. Firstly, peer-reviewed journals were searched on the Academic Search Premier, ERIC, Business Source Elite and Business Source Premier databases using the key terms 'The practice human resource management in SMEs'. As recommended by Bergh (2012) Boolean logic was then used to refine the literature searches within the range of 100–150 hits per keyword search. This had the effect of focusing on the arguments making up this paper.

### **3 Results and findings**

According to Storey (2007), a firm may have the best infrastructure and substantial financial resources but not all of these cannot contribute to effectiveness in an optimal way if there is no suitable human resource to operate them. Thus, HRM has proven to play a significant role in staffing, training, and helping to manage people so that organisations can operate to their maximum capability (Price, 2011).

Since Richbell, Szerb and Vitai (2010) observed that there is an acute shortage of literature, research aimed at understanding the conditions affecting HR practices in SMEs has been generally passive, partly because of a belief that HRM practices based on research conducted in larger organisations can also be applied to SMEs (Psychogios, et al., 2015; Tsai et al., 2007). Therefore, the study of HRM in SMEs is frequently overlooked as most HR management practices and literature are developed and tested in the context of large firms.

However, as Tocher and Rutherford (2009) report, HR practices applied in large firms are not always suitable for SMEs thus rendering invalid the textbook prescription of HR practices contained in mainstream literature. To make matters worse, SMEs are widely known for their informal and reactive approach to management partly because of the owner-manager's role in all managerial decisions (Singh & Vohra, 2009). As such, HRM in smaller organisations also tends to be informal in line with other management (Psychogios, et al., 2015). This informality is partly driven by the fact that the SME owner-manager, who instances is not an HR expert centralises all management decisions including HR decisions. The informality may also be spawned by the absence of a standalone HR department in the firm to guide the proper implementation of HR policies and procedures.

Under these circumstances, Wiesner and Innes (2010) conclude that HRM in SMEs manifests themselves in two divergent perspectives; the "small is beautiful" and the "bleak house" perspective. The "bleak house" view perceives HR management in SMEs as characterised by low wages, long working hours, and an exploited workforce. The "small is beautiful" perspective, on the other hand, represents a "happy family" scenario characterised by reasonable pay, flexible hours and close interpersonal relationships between employees and owner-managers.



### **Small is Beautiful approach to HR management**

The *Small is beautiful* scenario refers to HR practices that foster a familiness in the SME business characterised by less bureaucratic control, good employee relations, and mutually beneficial goals between the employees and the owner-manager (Lai, et al., 2017; Rauf, 2016). This picture is reflective of the soft version of HR management, which according to Storey (2011) refers to a healthy working relationship where the interests of employees take centre stage in shaping the direction of the firm. The same view is echoed by Barrett and Mayson (2007) who explain that, like the approach to HRM, the *small is beautiful* approach to HR management in SMEs is reflective of the human relations movement through eliciting employee flexibility, adaptability, commitment, communication and commitment. As such, the beauty in this perspective lies in the HR management practices spawned by the small size of the employee stock which then fosters familial relationships between the employees and the owner-manager. Therefore, as Saridakis, et al., (2013) reason, SME owner-managers practicing the *small is beautiful* scenario pay strategic focus on fostering familial relationships through regular two-way communication and, a democratic leadership style.

The same observation is made by Kroon et al., (2013) who note that the smallness of SMEs plays fertile ground for a healthy psychological contract between the SME owner-manager and the employees. This positive and close psychological contract between the owner-manager and the employees contributes to the owner-manager assuming a paternalistic role which compels him to trust his employees and treat them fairly (Saridakis, et al., 2013).

### **HR practices under the Bleak House scenario**

On the polar side of the small is beautiful perspective is the *“bleak-house”* scenario which Innes and Wiesner (2012) allude to the fact that the small size of SMEs acts as a liability in terms of their people management practices. Psychogios, et al., (2015) agree with this notion and explain that, since most SMEs do not have professionally run HR departments, their HR practices are poor which manifests in poor working conditions, poor health and safety standards, limited access to trade unions, leading to higher levels of potential conflict, higher turnover, and more absenteeism. These *“Bleak House”* conditions can also be traced to the informality in the general management of the firm which opens up the potential for employee exploitation akin to the *bleak house* conditions (Bannò & Sgobbi, 2016).

Therefore, as Psychogios et al., (2015) reiterate, the small size of SMEs asserts that the firms are autocratically controlled by owner-managers with little employee involvement in the running of the business. Therefore, as Guest and Conway (1999) observe, the HR management practices in SMEs reflect a ‘black hole’ representing the ghost of the Scientific Management school of Managing employees and the Hard approach to HRM. As such,



employees in SMEs are viewed as nothing more than a resource that must be exploited to gain maximum gains by the overbearing owner-manager (Henderson, 2008). As a result, employees employed in SMEs experiencing the bleak house phenomena suffer from low wages, minimal training, close supervision and monitoring, appraisal and short-term changes, minimal communication from the top and in short, an autocratic leadership style (Henderson, 2008; Barrett & Mayson, 2007).

Thus, in conclusion, according to the bleak house philosophy, HRM in SME firms is characterised by a high degree of uncertainty concerning the individual, as well as, firm performance outcomes, “resource poverty” and a liability of smallness (Kotey & Slade, 2005).

### **HR Management Functions in SMEs**

The two approaches to HR management in SMEs lay the groundwork for the practice of people management in firms. As such, the nature of the HR practice in the different functions of recruitment, training, rewards, and performance management will reflect both the soft and the hard approaches to people management in SMEs.

### **Recruitment Practices in SMEs**

In SMEs, the owner-manager normally carries out all of the HR management functions. Therefore, informality is a key characteristic of the recruitment and selection activities in SMEs (Chandrakumara & Rao, 2014). Another feature of recruitment practices in SMEs is the nature of the employees targeted by the recruitment and selection efforts. Cameron (2008) argues that many SMEs tend to employ the majority of employees as unskilled labour either from among their family kinship ties or from the immediate operating environment. As such, the recruitment and selection efforts are banal, cheap, and fast as compared to what transpires in larger enterprises that recruit skilled employees from the open market (Tsai, 2010).

All the same, as a result of these differences in recruitment and selection approaches, between large firms and SMEs, the SMEs end up facing a number of unique challenges when recruiting capable employees, because they apply less appealing hiring channels like word of mouth and walk-ins, and staff recommendations in contrast to online advertisements and external recruitment agencies used by large firms (Young-Thelin & Black, 2012).

When it comes to selection, like recruitment, formal selection processes are rare in SMEs. Instead, selection procedures are largely based on the personal appraisal by the owner-manager and the most common selection tool is the one-on-one interview which concentrates on a few qualitative employee attributes such as person to organisation fit, values, norms, and beliefs (Rand & Torm, 2012). However, this weakness can be counteracted by the fact that by employing friends and family members, potential employees are likely to be drawn from people recommended by current employees and would therefore easily fit into the value system of the firm (Rand & Torm 2012).

### **Training and development**



According to Ogunyomi and Bruning (2016), unlike large firms, SMEs view training as an unnecessary cost and an anathema to the conduct of business. As Innocenti, et al., (2013) explain, this attitude towards training is due to the fact that small firms have a higher probability of employee turnover, and as such, it does not pay to invest in employee training. Rolle (2008) concurs and reports that most owner-managers in SMEs are sceptical about the efficacy of training and view training as an unnecessary expense to the firm. Moreover, training resulting in highly specialized skills is considered inappropriate as SME operations prefer staff with multiple skills to cope with the highly flexible nature of the work of SMEs (Tocher & Rutherford, 2009). As a result, according to Leach (2012) in SMEs, family members should be trained according to what is best for them as individuals, yet business norms dictate that training should improve the individual's ability to contribute to the achievement of organisational objectives.

### **Rewards Management**

Since in most SMEs, the guiding norms are that family wealth should be distributed either according to need or according to principles that are transparently fair. However standard HR procedures dictate that remuneration should be based on the individual's contribution regardless of family affinity (Leach, 2012,30). Common causes of pay problems in small firms include financial carrots, and confusion over the business and personal funds, pay or perks are used as a means of transferring money from the family business to the family (Innocenti, Profili, & Sammarra, 2013).

Rewards management in SMEs is viewed by Songini and Gnan (2013) as a complex matrix involving balancing decisions that relate to pay levels, pay mix between salary, benefits, and incentives, pay structure, and pay raises. Like most HR issues in SMEs, reward policies are mostly informal with the firms rarely using formal salary surveys to assure that their pay levels are competitive (Songini & Gnan, 2013). Likewise, the firms do not use formal job evaluation systems to assure that their pay structures are internally fair thus resulting in flat organisational structures with few hierarchical managerial levels (Psychogios, Szamosi, Prouska, & Brewster, 2015). These rewards policies are often characterized by a lack of transparency, which in turn results in perceptions of unfair reward distribution (Tocher & Rutherford, 2009).

Songini & Gnan, (2013) concur and claim that the presence of a combination of economic and altruistic motives that lead SMEs to replace merit-based rewards with need and equality criteria and consequently to adopt less formalised practices, may entail paying allocations that employees find difficult to understand. Formalising reward practices in SMEs can have advantages as well as disadvantages. On the one hand, employees may consider formality as a positive thing because it increases feelings of fairness and consistency, which is central to gaining their commitment to the firm (Rauf, 2016). On the other hand, introducing formalised reward practices can also have disadvantages for small firms. For example, the high cost associated with these practices might be a burden for SMEs given their shallow pockets. Formalising the rewards function might also limit the flexibility that allows employees to negotiate their salary and benefits, which may in turn decrease their motivation in addition to



undermining the informal culture that characterises rising relationships in SMEs (Barrett & Mayson, 2007) (Innes & Wiesner, 2012).

Finally, the Agency theory also comes to the fore when we discuss rewards issues in SMEs. Agency costs are not huge when crafting rewards systems in small firms because family involvement in both ownership and management aligns the interests of the owners who are also the managers of the firms. (Michiels, et al., 2012). This makes SMEs the most efficient form of rewards delivery from an agency perspective as the ownership characteristics of the firms imply several agency benefits given that possible acts of self-interest will be tempered by kinship, altruism, and family loyalty (Michiels, et al., 2012). These minimal agency costs for example will imply that performance-based pay is not needed in SMEs, as the main goal of the pay-for-performance is to reduce a firm's agency costs.

### **Succession Planning**

Researchers have long argued that succession planning is important in the sustainability of small firms as it is the key ingredient in their success. (Chandrakumara & Rao, 2014). Therefore, as Michiels, et al., (2012) concur, the success of an SME is based on how the succession process is planned for and implemented. Chrisman et al. (2007) suggested that succession planning also involves the ability of the small firm to identify the number of successors, detailing the criteria and designating the successor. This may be followed by communicating the decision to the chosen successor and all other stakeholders, and successor training and formulation of a post-succession business strategy. Unfortunately, a common challenge in the succession process in small firms stems from the traditional family-based expectation that the oldest child (usually the son) will take over the business despite his motivation or ability to run the business (Nordqvist & Melin, 2010). As such, such small businesses run the risk of falling into the hands of incompetent leadership each time family dynamics shift (Psychogios, Szamosi, Prouska, & Brewster, 2015). This means that succession planning in SMEs is a unique and difficult process given the fact that planning for succession involves the simultaneous reviewing of family and business governance structures and processes to come up with a win-all situation, a feat that is not easily achievable (Nordqvist & Melin, 2010).

### **Employee Performance Evaluation**

According to Armstrong (2011), *'performance management is a process of designing and executing motivational strategies, interventions and drivers with an objective to transform the raw potential of human resources into performance'*. It acts as an agent of converting the potential in employees into actual performance by removing intermediate barriers as well as motivating and rejuvenating individuals. Employee performance is evaluated regularly to find out whether an employee continues to contribute to the organisation, and whether the employee should receive a bonus, a pay raise (increment) and/or a promotion (Ogunyomi & Bruning, 2016).



All the same, the most common appraisal methods within SMEs are the easy and cheap narrative descriptions and rating scales. Owner-managers who at most times do not have the skills to carry out effective performance reviews may perceive formal performance appraisal systems as time-consuming and complex (Michiels, et al., 2012). In fact, performance evaluation remains an ongoing process given the fact that the small family environment in SMEs entails that owner-managers can directly observe the activities of their employees and intervene in wrong performances on a day-to-day basis (Barrett & Mayson, 2007). Therefore, performance appraisal mainly tends to be informal and continuous.

Leach (2012) posits that in SMEs senior family members often face the unenviable task of having to assess the managerial competence of their offspring or other relatives. It is therefore simply not possible for them to do justice to the requirements and norms of both the family and the business at the same time (Young-Thelin & Black, 2012).

### 3. Conclusions

This analysis of HR practices in SME business has revealed that there is a divergence of views among scholars on the nature of HR practices. One set of scholars views the HR environment in SMEs as harmonious and unitarist in the relationship between management and employees. An alternative perspective is provided by another set of scholars who claim that SME firms are 'bleak houses' in the sense that they suffer from the liability of smallness and hence end up practicing informal HRM and reap its attendant drawbacks. However, some scholars counter this argument and claim that when it comes to managing people, SMEs have an upper hand over big firms because their lack of formality towards employee management enables flexibility within the labour process and an individual approach to the employment relationship.

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