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# Can Firms Perform Without Good HR Practices and Inspiring Leaders?

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# Can Firms Perform Without Good HR Practices and Inspiring Leaders?

## **Abstract**

### Key Findings

- A positive match between leadership behaviors and HR practices produce the best organizational outcomes. However, there is evidence that having either strong HR systems or charismatic leaders results in better organizational outcomes over having neither in place;
- Voluntary turnover is lowest when charismatic leadership and high commitment human resource (HCHR) practices are both high;
- Firm performance relative to peers is highest when charismatic leadership and HCHR practices are both high; and
- If either HCHR practices or a charismatic CEO is present within a firm, then employees will be less likely to quit or turn over and performance will be higher compared to when neither exists, suggesting that firms with limited resources can get some positive results if they have the ability to only develop great leaders or invest in great HR practices for their employees.

### **Keywords**

leadership, performance, human resource practices, organizational outcomes

### **Comments**

#### **Recommended Citation**

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# CAN FIRMS PERFORM WITHOUT GOOD HR PRACTICES AND INSPIRING LEADERS?

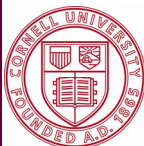
## Key Findings

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## Topic: The Concept of Fit as Multi-Faceted

The effectiveness of HR systems is thought to be dependent on the fit of these systems to the broader context of the organization. Historically, scholars have argued that strategic fit includes both:

*horizontal fit* – the alignment between HR practices. This fit is important within a system for firm performance because practices in a system that reinforce one another are thought to be more effective, or



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*vertical fit* – the alignment with the broader context of the organization. This fit is important because particular sets of HR practices are more likely to positively affect performance when aligned with specific organizational strategies.

By emphasizing the concept of *external* fit, strategic HR scholars may have overlooked a more salient aspect of *internal* fit, because fit with strategy may depend on whether HR practices are aligned with these other aspects of the organization. For example, if an HR system fits with the strategy of the firm, but the HR system is not aligned with firm technology; leadership; or culture, then an appropriate and consistent response from employees may be less likely because employees will receive inconsistent messages from the organization about appropriate behaviors and actions. Therefore, the researchers argue that the concept of fit is more multi-faceted than previously thought.

In this study, the researchers explored the relationship between a system of HCHR practices and CEO charismatic leadership and reviewed the potential relationships between these variables. Various forms that the interaction may take were identified (e.g., positive synergistic, deadly combinations, and substitutes). Theoretical arguments regarding the impact of each on firm performance relative to peer organizations and voluntary turnover were developed.

The researchers expanded upon prior conceptualizations of strategic HR fit to include fit with other aspects of the people management system and test for the effect of the various forms that this relationship can take on organizational outcomes. There is a need to look beyond just fit with strategy or among HR practices to other variables such as leadership.

### **Variables of Interest**

Because of the overlapping nature of how charismatic leadership and HCHR practices affect employee motivation, the researchers argue that natural synergies exist between them which are likely to enhance or reduce the impact of HR practices on firm outcomes.

Charismatic leadership and HCHR practices both provide employees clear signals of what is important, the direction the organization is headed, and what is expected from employees. Both also demonstrate a high level of investment in employees and lead employees to believe that they are valued by the organization.

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Charismatic leaders are described as:

- articulating and providing a consistent and inspirational strategic vision,
- being sensitive to his/her environment and members' needs,
- being willing to take personal risks for the good of the firm, and
- engaging in unconventional behavior to achieve organizational goals.

These dimensions of charisma motivate employees to follow such leaders because of the extraordinary impression that they make. In turn, this affects followers' emotions, loyalty towards the leader's mission, self-esteem, trust, and confidence in the leaders, and intrinsic motivation. Charismatic leaders profoundly affect follower attitudes, behaviors, and performance – resulting in their employees finding work more meaningful and therefore, being more self-engaged.

The behaviors of top leaders (i.e. CEOs) are particularly likely to impact employee motivation in small businesses – the context of this study – because they tend to have frequent personal interactions with the employees of the organization. The small business context may provide a good proxy for how the relationship between HR and leadership may play out at the unit level within large organizations.

HCHR is generally composed of the following subsystems that are part of the larger management system:

1. selection based on fit to the culture and values of the organization,
2. individual discretion and on-going learning opportunities, and
3. compensation and other HR practices that reinforce organizational goals and embeddedness.

Together, these subsystems create a system of practices that represents an organization's overall strategy to manage the employment relationship. Collectively, they demonstrate a long-term commitment to employees which reinforces a positive work environment resulting in more optimistic work attitudes and employee behaviors that are beneficial to the organization. Theoretically, the combined subsystems of the HCHR create a mutually supporting climate that communicates a consistent signal of high investment in the employee, and the consistency of the practices reinforces the environment that leads to extra effort, contribution of discretionary effort, and other positive behavioral response from employees.

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### Theory and Hypothesis

Positive synergistic effects – or powerful connections – occur when two activities within a firm have a more positive effect than the sum of each individually. For example, within the context of HR systems, two practices that reinforce the same message create a strong context in which employees are more clear on expectations and thus, more likely to carry out an expected behavior in the presence of both compared to if the employees were exposed to each practice individually.

In the context of this study, researchers suggest that HCHR and charismatic CEO leadership may create a powerful connection if the messages to employees are consistent and reinforce employees' understanding of what they can expect from the organization and what is expected of them in return. Further, organizations are likely to achieve improved outcomes if HCHR and charismatic leadership are consistent, as both will positively reinforce employees' motivation and feelings of engagement.

### Deadly Combinations

In the context of an HR system, firms may see a net negative outcome (a.k.a. "deadly combination") when combining two HR practices that conflict with one another or confuse employees in terms of how to direct their actions. For example, organizing work and work flow around teams yet rewarding employees based on individual performance may lead to negative outcomes because employees will be unsure of whether to focus maximizing their own outcomes or supporting their teammates.

When HR and leaders are inconsistent, the message of the firm's values will be weaker than when both are consistent because there is no reinforcement of policies. More importantly, the inconsistencies may lead to confusion resulting in either higher employee turnover or lower organizational performance compared to when the messages are consistent. In fact, the inconsistent messages may be more negative than if *both* HCHR and charismatic leadership are low because the contradicting messages are more confusing and detrimental than the lack of support from the organization. In the low-low situation, employees

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may not be as committed to the organization (as compared to the high-high situation), but employees understand what is expected of them and what they will receive (or not receive) in return for their work.

When inconsistencies exist between the practices and leader behaviors, employees will be confused about their roles in the organization, resulting in disequilibrium. To remedy the confusion and resulting cognitive dissonance, employees will likely look to find a work environment with a more clear understanding of what is expected of them. Indeed, employees are more likely to leave their positions and the organization when they are unclear about what is expected of them. Further, in this situation, as a group, they will be less likely to consistently engage in behaviors that are beneficial to the organization because they will not know which are most important or will be rewarded, resulting in lower firm performance.

### **Substitutes**

HCHR practices and charismatic leadership behaviors may substitute for each other, at which point, the presence of both HCHR and charismatic leadership does not create a stronger situation – and an organization that is high on either one will result in positive outcomes. The presence of one or the other at a high level will result in the same outcome as when both are high and will result in better outcome compared to when both are low. Two possible situations can occur: either high commitment HR practices substitute for charismatic leadership or charismatic leadership substitutes for high commitment HR practices.

For example, if a firm's leader does not seem in tune with employees' needs or interact with employees informally, high commitment HR practices can provide a more formal means for feedback and appraisal and create a positive social environment. A firm can show that it is committed to developing and rewarding employees by providing regular feedback, following a formal process for performance appraisals, creating opportunities for social interaction, and providing performance-based incentives to substitute for a less charismatic leader.

Conversely, if a firm does not have a formal HR system of practices and doesn't follow a regular schedule for feedback and appraisal or reward employees with cash incentives, a charismatic leader may act as a substitute by providing more informal feedback, showing sensitivity to members' needs and abilities, or using other more unconventional methods for rewarding employees.

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If either high commitment HR practices or a charismatic CEO is present within a firm, then employees will be less likely to exit and performance will be higher compared to when neither exists, but turnover and performance will be equal to the situation when both are present.

### Method

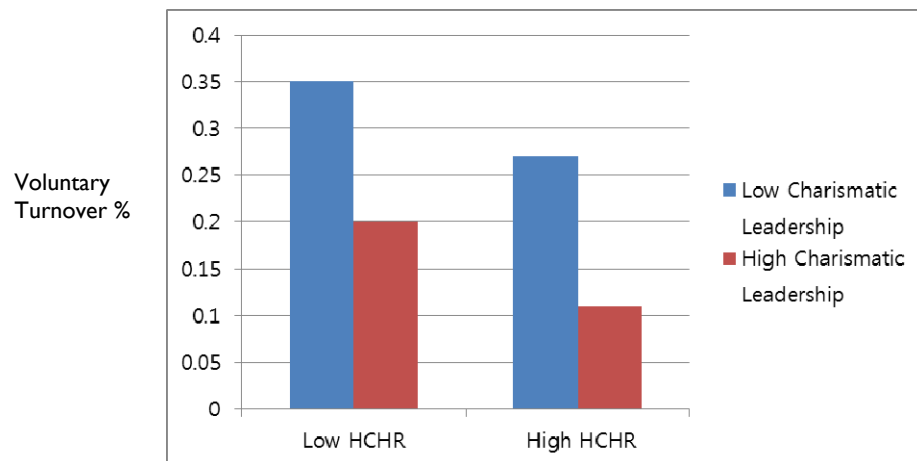
The following items were measured in surveys collected from senior leaders and employees:

- HCHR practices
- Charismatic leadership
- Employee turnover
- Perceived firm performance
- Control variables

The managerial sample consisted of 281 managers with on average 10 years of managerial work experience at the establishment and 19 years of managerial experience in a similar job. The total number of non-managerial employee respondents was 12,914, with an average of 45 responses per firm. On average, employees had seven years of work experience at the establishment and 11 years of experience in a similar job.

### Results

**Figure 1: Interaction Between HCHR System (HCHR) and Charismatic CEO Leadership on Voluntary Turnover**

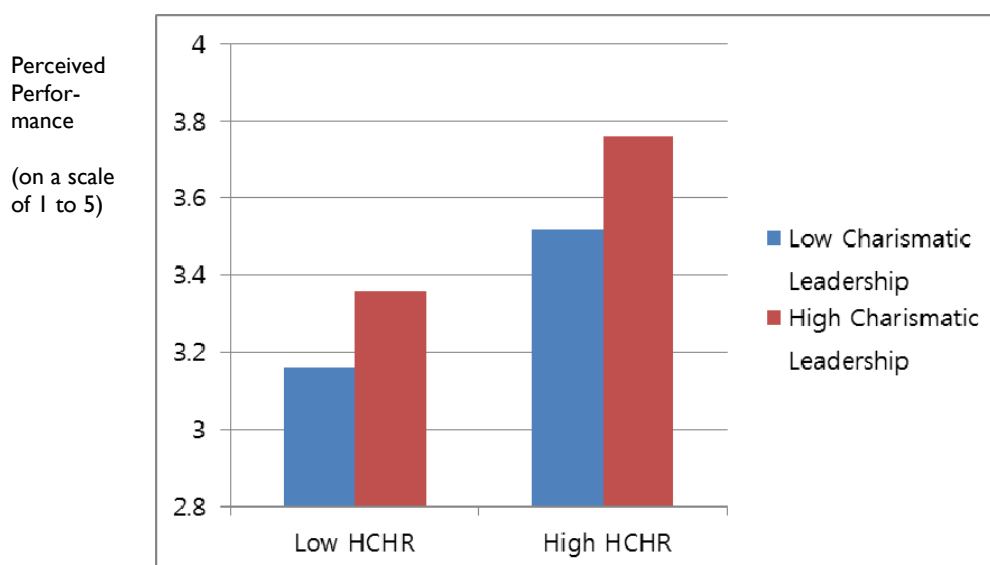


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Figure 1 shows that voluntary turnover will be highest when charismatic leadership and HCHR practices are both low, whereas the combination of HCHR and charismatic appear to lead to the lowest level of turnover. Consistency in message of investment and caring about employees reinforces employees' engagement and attachment to the organization. In support of the idea of substitutes, the findings suggest that investing in middle of the road strategy (that is, either investing in attracting and building great leaders or investing in an HCHR system) is better than doing neither. Interestingly, the findings do provide some support that the old adage that employees quit their boss and not the company may have an air of truth. There is lower turnover when charismatic leadership is high and HCHR is low relative to those companies where charismatic was low and HCHR high.

### Figure 2: Interaction Between HCHR System (HCHR) and Charismatic CEO Leadership on Perceived Relative Performance



The findings shown in figure 2 again illustrate that the best outcome comes when firms invest both in good HR practices and building/attracting motivational leaders. The highest levels of firm performance relative to peers occurred when both HCHR and charismatic leadership was high.

Similarly to turnover, there was again support for the substitutes hypothesis rather than deadly combinations. However, with substitutes, performance was higher in the high HCHR/low leadership versus the high leadership/low HCHR

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companies. A possible explanation is that HCHR practices not only motivate employees but also impact the skills and capabilities of the employees.

### Takeaways

- The results speak to the importance of not only having a motivational leader, but also to the importance of great HR practices in small firms. Companies achieve the best results when they are able to invest in both state-of-the-art HR practices and building/attracting visionary leaders who are able to motivate employees;
- HCHR and charismatic leadership may be substitutes for one another. “Substitutable” effects such as either HCHR practices *or* a charismatic CEO present within a firm would mean that employees will be less likely to exit and performance will be higher compared to when neither exists.
- While conducted in smaller organizations, the findings have direct implications for larger organizations at the business unit level. Like CEOs of small firms, leaders of business units have high levels of interpersonal contact with employees and their behaviors and vision can have a large impact on employee motivation. Further, at the business unit level, leaders sometimes need to make tradeoffs in terms of how to spend limited HR budgets. Should they spend HR dollars on building great leaders or in more HR practices? These findings would suggest there are returns for doing both but when limited, investing highly on one direction is better than not investing at all.

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