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Employee Outcomes: Human Resource Management Practices and Firm Performance in Small Businesses

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Abstract
[Abstract] Improving company performance is something of interest to all small business leaders. Small business leaders have many tools at their disposal — from finance to marketing to customer service — that could potentially improve the performance of their company. Among these tools is the way that small business leaders manage their people.

As has been mentioned in previous reports, research has shown that people management does indeed impact company performance, even at the financial level. Studies show increases in value per employee of up to $40,000 and survival rates for IPO firms as much as 20% higher for companies that effectively manage their human resources.

The Cornell University/Gevity Institute study of human resource management practices in small businesses is attempting to answer two important questions faced by small business leaders:

1. Do people contribute to the success of small businesses?

2. What human resource management strategies and practices can small business leaders employ to foster firm success?

In phase two of the study, we found that employee management practices help small employers improve workforce alignment, which was defined as having the right people with the right skills in the right jobs. Firms with high levels of workforce alignment experience higher performance than firms with lower levels of workforce alignment.

Building on these findings, the third phase of the study addresses the positive employee outcomes that can result from effective people management and seeks to understand which employee outcomes or behaviors tend to lead to different types of performance outcomes important to small business leaders.

The results for this study were taken from a sample of 111 small companies where responses were received from both the top manager as well as the employees. Companies ranged in size from 10 to 165 employees with an average size of approximately 30 employees representing a broad range of industries.

The results of the study will be presented as follows: First, we briefly discuss what is known about how human resource management impacts performance through employees. Second, we discuss the performance outcomes, and employee outcomes and behaviors that were studied as well as the specific employee behaviors and outcomes that seem to drive the different kinds of performance. Finally, we present some key takeaways from the results of this study.

Keywords
small business, human resource management, performance, practices

Disciplines
Human Resources Management

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WORKING PAPER SERIES

Research Report On Phase 3 of the Cornell University/Gevity Institute Study – Employee Outcomes: Human Resource Management Practices and Firm Performance In Small Businesses

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Working Paper 08 – 09

CAHRS WP 08-09

HUMAN RESOURCE MANAGEMENT PRACTICES AND FIRM PERFORMANCE IN SMALL BUSINESSES.

RESEARCH REPORT ON PHASE 3 OF THE CORNELL UNIVERSITY/GEVITY INSTITUTE STUDY – EMPLOYEE OUTCOMES

Prepared by the Cornell Research Team
September 2005

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INTRODUCTION

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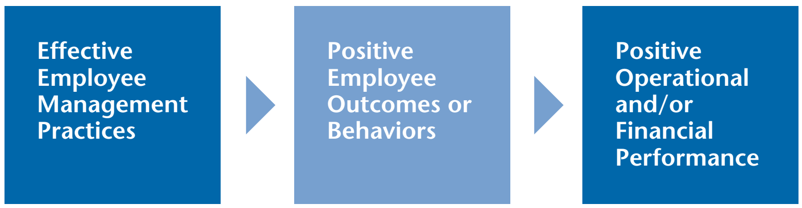
EMPLOYEE OUTCOMES AND FIRM PERFORMANCE

Multiple models exist to explain the process through which human resource management impacts company performance. Most of these models follow a process similar to the one shown in the figure below.



Since the purpose of human resource management practices is to more effectively manage people, it is intuitive that the impact of effective human resource management would be felt first at the employee level. Human resource practices should directly impact the employees of the firms where they are practiced and, if done effectively, will result in a number of positive employee outcomes. These outcomes might include such things as: commitment to the company, trust in management, higher levels of cooperation, higher levels of effort and involvement, and a lower inclination for employees to leave the company. These positive outcomes for the employees in the company in turn should lead to higher levels of operational and financial performance. Operational performance is any kind of performance resulting from the operations of the business and could include items such as high quality or improved customer satisfaction. Financial performance refers to performance measures taken directly from the company financial statements such as profit or revenue growth.

Do HR practices lead to positive employee outcomes? The results of this study indicate that a higher use of effective HR practices is directly related to higher levels of commitment to the company, trust in management, cooperation, effort and involvement and lower intentions to leave the company.

Do positive employee outcomes impact the operational and financial performance of small businesses? This study's results indicate that this is indeed the case. Various employee outcomes were shown to be significantly related to different measures of operational and financial performance. The details will be explained in the following sections.

DETAILED DISCUSSION OF RESULTS

In order to clearly discuss the findings of the study, it is important first to understand the kinds of employee outcomes as well as company performance that were studied. Each is discussed in detail below followed by an analysis of the findings.

Performance outcomes studied

For the purposes of this study, the effects of employee outcomes on four different performance measures were studied. Small business leaders are faced with many different concerns related to business performance, and the study attempted to address concerns that were especially important to small business leaders. Financial performance is important to small business leaders because strong financial performance will allow small business leaders to meet current obligations, invest for the future and provide a return to the owners and managers. Two measures of financial performance were used in this study: financial growth and financial performance compared to competitors. The first is a measure of the growth or increase in both revenues and profits, and the second is a measure of the financial performance of the company in relation to similar organizations.

Operational performance is important to small business leaders because it is an indication of the effectiveness and efficiency with which the company is providing its particular products or services. Three measures of operational performance were used for this study: customer satisfaction, quality, and new product or service development. Each is a measure of how the company performs in relation to similar organizations in those three particular areas. Customer satisfaction is a measure that indicates the extent to which the company is able to please its customers or clients. Quality is a measure of the level of quality of the products or services provided by the company, and new product or service development measures the rate at which new products, services or solutions are deployed.

Employee outcomes studied

Five different employee outcomes and their impact on the above measures of performance were studied. They were: commitment to the supervisor, trust in company management, cooperation, effort and involvement and inclination for employee turnover. Each outcome is defined briefly below.

Commitment to supervisor – Employees with high commitment to their supervisors are happy working with their current manager and feel that their manager is concerned about them and their problems.

Trust in management – Employees with high levels of trust in company management feel that management has their best interests as employees at heart and are comfortable allowing management to make decisions that impact employees.

Cooperation – Employees exhibiting high levels of cooperation are supportive of one another in their roles and expect to cooperate with others and to receive cooperation from others in performing their responsibilities.

Effort and involvement – Employees with high levels of effort and involvement are committed to and fully apply themselves to their work. They are willing to spend extra time to get the job done and do extra work that is not part of their own job.

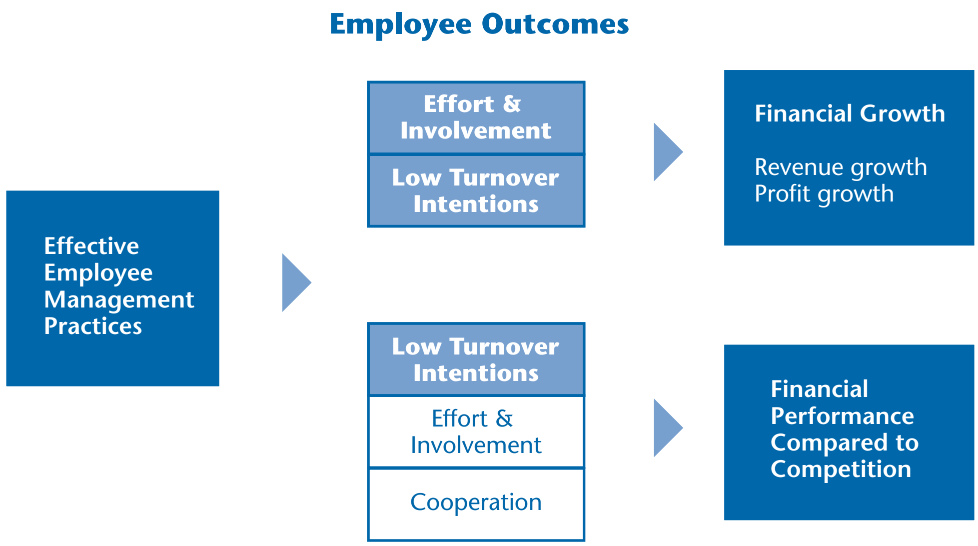
Turnover intentions – Employees with low turnover intentions are not actively seeking new employment, do not expect to leave the company in the future and do not often think about quitting their job.

Results

First of all, the results indicate that a higher use of HR practices leads to higher levels of each of the employee outcomes discussed above. That means that employees of companies employing effective human resource practices are more likely to demonstrate: higher levels of commitment to the supervisor, higher levels of trust in management, higher levels of effort and involvement in the company, higher levels of cooperation and a lower inclination to leave the company. The specifics of which HR practices are most effective in eliciting the different employee outcomes will be the topic of the next report.

Second, the results of the study indicate that these positive employee outcomes do indeed lead to higher levels of performance. We will discuss each performance outcome and the employee outcomes that lead to them separately.

Financial Performance



(The employee outcomes shown in light blue were the most significant in predicting better financial performance; those in white were still significant, but not at the same level as those in light blue.)

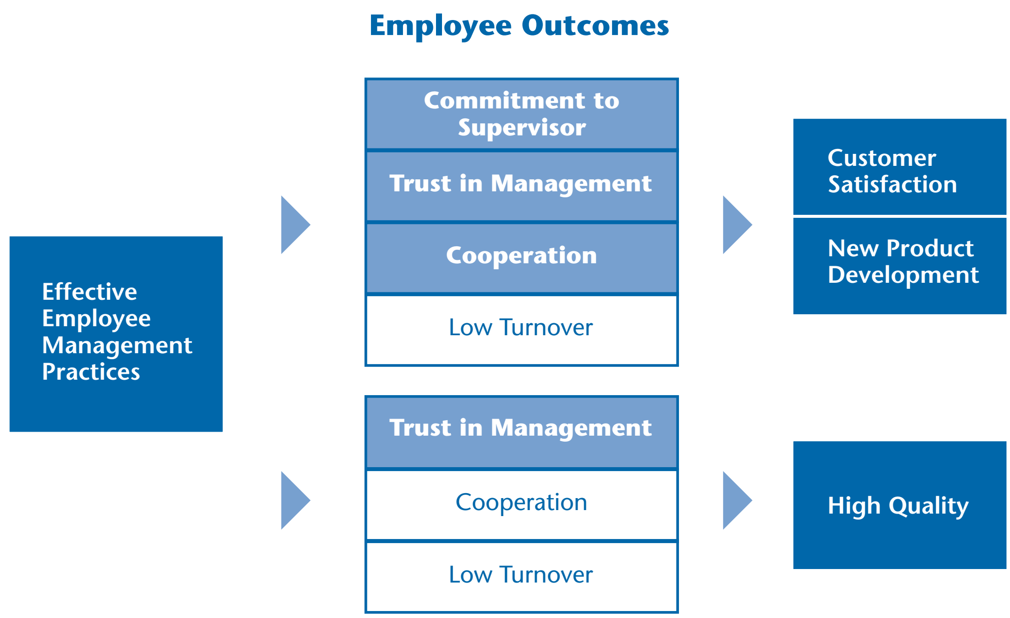
Financial growth

Financial growth was highest in companies that had high levels of employee effort and involvement and low levels of turnover intentions among employees. The conclusion that can be drawn from these findings is that companies that are able to foster involvement and low turnover intentions among their employees are more likely the experience growth in revenues and profits. Likewise, companies wishing to improve profit or revenue growth should focus on increasing employee involvement and decreasing intentions for turnover among employees.

Financial performance compared to competitors

Financial performance that was better than that of competitors was highest in companies where employees had low levels of turnover intentions. There was also some indication that high involvement and high levels of cooperation among employees contributed somewhat to higher performance compared to competitors. The conclusion that can be drawn from these findings is that companies that are able to foster low intentions of turnover among their employees and, to a lesser extent, high effort and involvement and high levels of cooperation are more likely to experience better financial performance than competitors. Likewise, companies wishing to improve their financial performance compared to competitors should focus on lowering turnover intentions among their employees.

Operations Performance



(The employee outcomes shown in light blue were the most significant in predicting better financial performance; those in white were still significant, but not at the same level as those in light blue.)

Customer satisfaction

Customer satisfaction was highest in companies where employees had high levels of commitment to their supervisors, a high level of trust in management and exhibited high levels of cooperation. There was also some indication that low intentions for turnover among employees had somewhat of an impact on customer satisfaction. The conclusion that can be drawn from these findings is that companies that are able to foster high levels of commitment to supervisors, trust in management and cooperation among their employees and, to a lesser extent, low turnover intentions are more likely to experience higher levels of customer satisfaction. Likewise, companies wishing to improve customer satisfaction can focus on elevating commitment to supervisors, trust in management and cooperation among their employees.

Quality

Product and service quality was highest in companies where employees had high levels of trust in management. There was also some indication that low levels of turnover intentions and high levels of cooperation have somewhat of an impact on quality. The conclusion that can be drawn from these findings is that companies that are able to foster high trust in management and, to a lesser extent, low turnover intentions and high levels of cooperation among employees are more likely to produce high quality products and services. Likewise, companies wishing to improve the quality of their products or services should focus on increasing the level of trust that employees have in management.

New product development

New product or service development was highest in companies where employees had high levels of commitment to their supervisors, high levels of trust in management and high levels of cooperation among employees. There was also some indication that that low levels of turnover intentions have somewhat of an impact on new product or service development. The conclusion that can be drawn from these findings is that companies that are able to foster high commitment to supervisors, high trust in management and high levels of cooperation and, to a lesser extent, low turnover intentions among employees are more likely to effectively develop new products or services. Likewise, companies wishing to improve their new product or service development should focus on increasing commitment to supervisors, trust in management and cooperation among employees.

KEY TAKEAWAYS

The results of this study offer several key takeaways for managers interested in improving the performance of their small businesses.

Effective employee management practices lead to positive employee outcomes

The use of effective employee management practices in small companies was shown to be directly related to:

- Higher commitment to supervisors.
- Higher trust in management.
- Higher effort and involvement in the company (more discretionary behaviors).
- Higher levels of cooperation with co-workers.
- Lower intentions to lead the company.

Employees do matter

Employees do matter and were shown to impact both operational and financial performance for small companies. Employee outcomes and behaviors such as trust in management, cooperation and employee effort did positively impact small firm performance.

Understand which employee responses you are looking for

As a leader of a small business, you need to understand which employee responses are associated with different kinds of performance. A summary of the findings is outlined in the table below.

	Commitment to Supervisor	Trust in Management	Cooperation	Effort and Involvment	Low Turnover Intentions
Financial Growth				**Very Important**	**Very Important**
Financial Performance Compared to Competitors			Somewhat Important	Somewhat Important	**Very Important**
Customer Satisfaction	**Very Important**	**Very Important**	**Very Important**		Somewhat Important
Quality		**Very Important**	Somewhat Important		Somewhat Important
Developlment of New Products or Services	**Very Important**	**Very Important**	**Very Important**		Somewhat Important

Focus on your human resource management

When evaluating the many options that are available to you as a business owner or manager, be sure to not discount the importance of your human resource management. Effective human resource management practices lead directly to positive outcomes for your employees, which in turn lead to positive financial and operational outcomes for you as a business manager or owner.

Examples of effective employee management practices include:

Employee Selection

- Employee selection practices focus on the potential long-term contribution of applicants.
- Leaving a position open until finding the best and brightest possible new employee.
- Looking to elite sources (e.g., top universities, head hunters) to find the best available talent.

Employee Management

- A highly formalized compensation system with predetermined pay bands, scales, and ranges.
- Using a formal performance appraisal process to provide feedback to employees.
- Managers follow a regular schedule in providing feedback to employees.
- Managers empower employees to monitor their own work and performance.
- Managers assume that employees are experts who will get the job done right the first time without direct oversight.
- Employees are given the opportunity to complete their work however they see fit.

Employee Motivation and Retention

- Offering employees profit- or gain-sharing pay.
- Regularly holding company wide meetings to share information about the company with employees.
- Creating a strong social environment at work.
- Sponsoring company social events so employees can get to know one another.

THE GEVITY INSTITUTE: KNOWLEDGE AND APPLICATION

The Gevity Institute was established to identify and quantify the link between people management practices and small- and medium-sized business performance.

The Institute's goal is to establish an ongoing stream of information, data and recommendations focused on effective people management for smaller companies. The Institute sponsors research at leading universities and business organizations.

Gevity will apply knowledge gained from Gevity Institute research to practical solutions that help small- and medium-sized businesses to improve profits, productivity and longevity.

To learn more, visit our Web site at www.gevityinstitute.com.

ABOUT GEVITY

Gevity helps clients increase profits, grow sales and improve customer satisfaction through our comprehensive employee management solution. We serve as the insourced human resource department to small- and medium-sized businesses nationwide. Our unique approach integrates three key drivers of business success: workforce alignment, administrative relief and business protection. We deliver our solution through our innovative people, processing and portal approach, combining the resources of our highly skilled human resource consultants and our scalable, Web-enabled technology platform.

To learn more, visit our Web site at www.gevity.com.

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