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The Relationship between Human Resource Practices and Firm Performance in Iran

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Abstract: This study examines the role of Human Resource practices on Firm Performance in Iran. This study uses regression analysis to test the hypotheses. The research uses a sample of 65 firms surveyed in Qazvin, Iran. The findings suggested that Training, Compensation, Performance appraisal and Participation are positively related the firms' performance. Implications of the findings, potential limitations of the study and directions for future research were further discussed.

Keywords: Compensation, firm performance, human resource practices, participation, performance appraisal, training

INTRODUCTION

Rapid environmental change, globalization, competition to provide innovative products and services, changing customer and investor demands have become the standard backdrop for organizations. To compete effectively, firms must constantly improve their performance by reducing costs, enhancing quality and differentiating their products and services. Armstrong and Baron (2002) have recently regarded the concept of strategic human resources as "a general approach to the strategic management of human resources in accordance with the intentions of the organization on the future direction it wants to take. Human resource management (HRM) refers to the policies, practices and systems that influence employees' behavior, attitudes and performance (De Cieri *et al*., 2008). Human resource practices include determining human resource needs, recruiting, screening, training, rewarding, appraising and also attending to labor relations, health and safety and fairness concerns (De Cieri *et al*., 2008; Dessler, 2007).

The relationship between HRM and firm performance has received considerable attention from HRM researchers and innovation researchers in recent years. A vast amount of research has proved the positive relationship between HRM and a given firm performance (Huselid, 1995). Some studies show that certain HRM practices, such as working in teams, greater discretion and autonomy in the workplace and various employee involvement and pay schemes, do motivate workers and hence generate higher labour productivity (Boselie and DerWiele, 2002). Several researchers have noted that HRM leads to firm sustainable competitive advantage and superior performance and HRM is an important means of gaining this competitive advantage (Schuler and Macmillan, 1984; Barney, 1991). Powers and Hahn (2002) found that skill and resource-based competitive methods impact on firm performance. Accordingly, HR practices help firms select and implement skills and resources that will create marketplace uniqueness. Skills can be defined in terms of staff capability, systems, or marketing savvy not possessed by a competitor (Powers and Hahn, 2002). Delaney and Huselid (1996) found impact of HR on organizational performance. In addition, humancapital- enhancing HR practices have main effect on performance when firms link HR systems with quality manufacturing strategy (Youndt *et al*., 1996). Moreover, Batt (2002) demonstrated significant and positive relationship between HR and sales growth because organization has a foundation for superior performance when it possesses skills or resources that provide superior value to customers (Mavondo *et al*., 2005).

Guest *et al*. (2003) also argue that the case for an association between human resource management and performance is based on two arguments. The first one being that the effective deployment of human resources offers one of the most powerful bases of competitive advantage. The second argument is that effective deployment of human resources depends on the application of a distinctive combination of practices, or the use of a consistent set of human resource practices. Additionally, Guest *et al*. (2003) stress that there is a plausible case that human resource management will be more effective if it fits the business strategy of the firm. Several studies in the HR literature investigated the impact of HR practices on organizational performance. Although some studies related to HR practices can be

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found in the operations management literature (Jayaram *et al*., 1999; Youndt *et al*., 1996), this discipline has tended to address structural issues and analytical questions and has paid little attention to human resources issues.

RESEARCH BACKGROUND AND HYPOTHESES

Firms performance: Performance can be viewed in many aspects and connotations depend on the application. Performance is a measure for assessing the degree of a corporation's objective attainment (Daft, 1995). In fact, Laitinen (2002) defined performance as the ability of an object to produce results in a dimension determined a priori, in relations to a target. OP is an indicator which measures how well an enterprise achieves their objectives (Hamon, 2003). Ho (2008) defined OP in terms of how well an organization accomplishes its objectives. Schermerhorn *et al*. (2002) point out that performance refers to the quality and quantity of individual or group work achievement. Delaney and Huselid (1996) suggest two ways to assess OP and market performance.

Employee training and firm performance: Training can advance employees' capabilities of accepting new skills and using new knowledge and therefore, improve employee competence in innovation because through training employees can acquire new knowledge and can increase their innovation ability (Li *et al*., 2006). Becker (1964) suggests that employee training allows employees to use the new skills. In high-tech firms, employees with more innovation knowledge are important resources of the firms and they are required to continually attain new knowledge and skills to keep pace with development of technologies. Training can advance employees' capabilities of accepting new skills and using new knowledge and improve employees' competence in innovation. Bartel (1994) established a link between the use of training programs and productivity growth. Training, according to Armstrong (2006) "is the use of systematic and planned instruction activities to promote learning". It involves the use of formal processes to impart knowledge and help people acquire the skills necessary for them to perform their jobs satisfactorily.

H1: Employee training will be positively correlated to firms' performance.

Compensation and firm performance: One purpose both of direct and indirect compensation is to enhance employees' motivation and attachment to the organization (Arthur, 1994). Both Meta-analyzes (Hom and Griffeth, 1995) and empirical studies (Powell *et al*., 1994; Shaw *et al*., 1998) show an inverse relationship between high relative pay and/or pay satisfaction and employee turnover. Strong salary growth significantly reduces turnover for high performing employees (Trevor *et al*., 1997). Incentive pays are part of a complex arrangement to express and to maintain the working relationship between the employers and employee.

H2: Compensation will be positively correlated to firms' performance.

Performance appraisal and firm performance: The process of performance management, according to Mullin (2002), involves a continuous judgement on the behaviour and performance of staff. It is important that employees know exactly what is expected of them and the yardstick by which their performance and results will be measured. A formalised and systematic appraisal scheme will enable a regular assessment of the individual's performance, highlight potential and identify training and development needs. Most importantly, an effective appraisal scheme can improve the future performance of staff. The appraisal scheme can also form the basis for a review of financial rewards and planned career progression. Dave and Wayne (2005) argued that performance appraisai is an instrument whereby an individual was retaliated by the assessment due to certain personal disgruntled and it has adversely affected future performance. Hence, the following hypothesis has been stated.

H3: Performance appraisal will be positively correlated to firms' performance.

Employee participation and firm performance: Employee participation is the process whereby employees are involved in decision making processes, rather than simply acting on orders. Employee participation is part of a process of empowerment in the workplace. Empowerment involves decentralising power within the organisation to individual decision makers further down the line. Team working is a key part of the empowerment process. Team members are encouraged to make decisions for themselves in line with guidelines and frameworks established in self managing teams. Employee participation is in part a response to the quality movement within organisations. Individual employees are encouraged to take responsibility for quality in terms of carrying out activities, which meet the requirements of their customers.

H4: Employee Participation will be positively correlated to firms' performance.

RESEARCH METHODOLOGY

Sample: With an aim to generalize on firms in Qazvin, the population of the present study consists of

Table 1: Demographic profile of the respondents

Demographic Characteristics		Frequency	Percentage
Age	<25	4	6.1
	26-35	12	18.5
	36-45	24	37
	46-55	19	29.2
	Above 55	6	9.2
Gender	Male	48	73.8
	Female	17	26.2
Year with present organization	<10	28	43
	11 to 20	20	30.8
	20 to 30	12	18.5
	31 to 40	5	7.7
Position in the company	Clerical	13	20
	Lower level of management	11	16.9
	Middle level of management	17	26.2
	Top level of management	22	33.8
	Others	2	3.1

Table 2: Results of reliability analys

Variables	Cronbach's alpha
HRP factors	
Training	0.73
Compensation	0.81
Performance appraisal	0.84
Participation	0.79
Firm performance	0.88

N = 65

manufacturing companies located in Qazvin, Iran. One Hundred and fifty sets of questionnaires were distributed to executives working at manufacturing companies in Qazvin, however only 65 copies of questionnaires were usable for analysis.

Measures: The questionnaire used in this study consists of three parts. Section 1 required the respondents to rate a total of 20 items on the four components of Human Resource practices namely, Training, Compensation, Performance appraisal and Participation which were extracted from past researches such as Snell and Lau (1994), Kuratko *et al*. (1997) and Zahra *et al*. (2000). Section 2 contained 5 items of questions pertaining to firm performance based on the research of Daily and Johnson (1997). Finally Section 3 contains items regarding the demographic of the respondents such as gender, age, education background, working experiences, monthly gross salary, etc. The respondents were asked to describe on a 7-point Likert scale with: 7 = strongly agree, 6 = agree, 5 = slightly agree, 4 = neutral, 3 = slightly disagree, 2 = disagree and 1 = strongly disagree.

ANALYSIS AND RESULTS

Demographic Profile of the Respondents is summarized in Table 1. The Cronbach's coefficients alphas for HRP factors are summarized in Table 2. The firm performance retained all the 5 items which accounted for its Cronbach's coefficients alpha of 0.88. Generally, the values indicated good internal consistency estimate of reliability of the grouped items for both factors. The findings of the reliability analysis are summarized in Table 2. Table 3 illustrated the intercorrelations among the subscales were obtained from the Pearson Correlations Matrix to determine whether the subscales were independent measure of the same concept. Multiple regression analysis was carried out to test the hypotheses that comprised the direct effects of HRP on firm performance. Table 4 shows the results of regression analyses of the effects the four-dimensional structure of HRP on firm performance. The result has clearly indicated that all of HRP factors are positive and significant for firm performance, Training, Performance appraisal and Participation ($p<0.01$) and Compensation ($p<0.05$).

In summary, all four factors of HRP have the expected signs and also have significant effects on firm performance. Accordingly, the results support all of hypotheses.

CONCLUSION

This study examines the role of Human Resource practices on Firm Performance. Our results indicate that HRP have positive and significant effects on Firm Performance. These findings highlight the critical roles of HRP in Firm Performance. A number of researchers have revealed that there is significant relationship develops between HRM and firm performance (Huselid, 1995; Li *et al*., 2006) and this is also confirmed by resource-base theory. Delaney and Huselid (1996) found impact of HR on organizational performance. This is also consistent with the research findings by Nelson (1991) that it is inevitable that incentive rewards is a technique which must be applied in forming organizational strategy if companies strive to achieve better performances. Interestingly, the

Table 3: Pearson correlations for HRP and firm performance measures

Variables	Training	Compensation	Performance appraisal	Participation	Firm performance
Training	1.00				
Compensation	0.18*	1.00			
Performance appraisal	0.42**	0.32**	1.00		
Participation	0.21*	0.34**	0.20*	1.00	
Firm performance	0.52**	0.18*	0.40**	0.21*	1.00

N = 65 *: $p<0.05$; **: $p<0.01$

Table 4: Regression results: The relationship between HRP factors and firm performance

Independent Variable	Std Beta
Model variables	
Training	0.42**
Compensation	0.21*
Performance appraisal	0.34**
Participation	0.38**
R^2	0.584
Adj R^2	0.322
R^2 Change	0.584
F-value	19.37**

*: p<0.05; **: p<0.01

findings have demonstrated that employee training and performance appraisal did not correlate with better firm performance. The results contradicted with the study by Mullin (2002) that training is the key element in influencing the performance of a firm. Mehr and Shaver (1996) also find that rewards based on innovation outcomes can impair innovation. Powers and Hahn (2002) found that skill and resource-based competitive methods impact on firm performance. Kasturi *et a*l. (2006) noted that Singh (2003) demonstrates impact of four HR practices on firm performance such as performance-based compensation, information sharing, selection and promotions. There are several limitations of this study that suggest further research. Perhaps, the most serious limitation of this study was its narrow focus on Iranian firms. Future studies could use the model developed in this study and test it in other developing countries.

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