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Impact of Transformational Leadership Style on Business Performance of Small and Medium Enterprises in Tanzania

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Abstract:

This study attempts to determine the relationship between transformational leadership style and business performance of small and Medium Enterprises (SMEs) in Tanzania. This study used field data collected by 60 out of 100 mailed questionnaires sent to CEOs of SMEs in various regions of Tanzania. Data was analyzed quantitatively using Pearson product moment correlation and simple regression by SPSS. This study found strong positive correlation between transformational leadership style and business performance of SMEs in Tanzania. Transformation leadership was found to be a strong predictor of business performance of SMEs in Tanzania.

Keywords: Transformational Leadership Style, Business Performance, Organizational Performance, Small and Medium Enterprises

1. Introduction

Performance of SMEs in Tanzania has been a favorite topic among entrepreneurial researchers and policy makers due to its importance in the national economy. 95% of all businesses in Tanzania are SMEs (Madatta, 2011). The government has done enough to make business environment conducive for SMEs to flourish. Conducive business environment has attracted thousands of entrants to entrepreneurial business over the past one decade (Mfaume & Leonard, 2004). It is surprising to note that, despite of such good business environment in Tanzania, SMEs are still experiencing poor performance trends hence failure to survive or even grow to become big firms (Mgeni, 2015). The paradox of rapid increase in number of SMEs yet poor performance of the sector in the economy seems to have a long way to be resolved. Many challenges which were thought to be responsible for the incumbent poor performance of SMEs in Tanzania, have been widely researched and its recommendations implemented, yet no appealing improvement have been realized. To date 3 out of every 5 SMEs established fail within a period of less than five years from their establishment and the surviving firms are usually stagnant (Dalberg, 2011). According to Mfaume, and Leonard, (2004), entry into business is not a problem for Tanzanian SMEs, however its growth is characterized by stagnancy and poor performance.

Literature in Tanzania, unlike elsewhere, have not linked, poor performance of SMEs to leadership styles. The ongoing poor performance of SMEs sector have been associated with challenges other than business leadership such as inadequate capital, incapable legal and market institutions for local businesses, poor marketing strategies and inability of SMEs to change according to the business environment dynamics (Mgeni, 2015, Mgeni & Nayak, 2015). Responding to the findings of existing studies, there has been a remarkable improvement in the business environment related to SMEs in Tanzania. For example, the government has made easier for SMEs to access collateral free loan capital in micro financial institutions, at a very low interest rates, created market opportunities for SMEs products and made a protection policy to local firms against foreign firms (Mfaume & Leonard, 2004). Despite of all these, SMEs sector still experience poor performance and acute failure, suggesting that the real cause is yet to be uncovered. Failure of SMEs in early stages of its life cycle and stagnancy indicate poor business performance associated with leadership factor (Zhelstoukhova, & Suckley, 2014). It has been found elsewhere that, different leadership styles have different impacts on business performance of SMEs (Avolio, Bass & Jung, 1999 and Kurt, 2008). Transformational leadership style is said to have the highest impact in the performance of SMEs (Bakar & Mahamood, 2014). In Tanzania, much emphasize has been given to management in relation to business performance of SMEs under the expense of leadership factor. Of recent, Mgeni, (2015) and Mgeni & Nayak, (2015) found a strong positive correlation between entrepreneurial leadership style and business performance of SMEs in Tanzania. Moreover, entrepreneurial leadership styles were found to be good predictors of business performance variations of SMEs in Tanzania (mgeni, 2015). This study attempts to determine impact of transformational leadership style on business performance of SMEs in Tanzania. The objectives of this study are thus to firstly determine the extent to which transformational leadership style correlates with business performance of SMEs in Tanzania and secondly, determine the extent to which transformational leadership style can predict performance variations in Tanzanian SMEs.

2. Conceptualization of Key Terms

2.1. Transformational Leadership Style

Transformational leadership style conceptualization has been contentious for a long time and consensus view seem to be long way to be realized. There have been various yet complementary theoretical positions on the conceptualization of Transformational leadership style in the organization. According to, Waswa, Munene & Balunywa, (2015), Transformational leadership theory relates to the charisma, intellectual stimulation and consideration of individual leaders (Bass,1985).Ling, Lubatkin, Simsek and Veiga, (20008) defines transformational leadership as a set of behavior which consists of four attributes, namely, charisma, inspirational motivation, intellectual stimulation and individualized considerations. Some studies have associated transformational leadership with adoptive leadership behavior (Bass, Avolio, Jung & Benson, 2003 and Khan, Ur Rehman &Fatima, 2009).Adaptive leadership behaviors are termed as transformational leadership and consist of five components, namely; idealized influence, attributive charisma, inspirational motivation, intellectual stimulation and individualized consideration. Attributive leader's socialized charisma is what is known as attributive charisma and is about the perception of the leader as being confident and powerful (Khan, Ur Rehman &Fatima, 2009). Furthermore, Idealized influence is about charismatic actions of a leader which has its focus in the sense of mission, values and beliefs (Bass, 1985).Moreover, the techniques which leaders use to boost their followers by taking into consideration the optimistic future and determined goals is called Inspirational motivation while the behavior of the leader which has a contribution to the satisfaction of the followers by guiding, supporting and giving attention to the personal needs of the followers is called Individualized consideration (Bass, Avolio, Jung Benson, 2003). Literature associates, transformational leadership with leaders' behavior to draw inspiration to employees so as they can commit all their efforts to help their leader realize organizational goals through teamwork (Hetland, 2011). This is realizable because transformational leadership, imparts intrinsic motivation to followers (Sommers & Birnbaum, 1998).

2.2. Business Performance

Business performance is probably the most researched topic in organizational management (Venkatraman & Ramanujam, 1986). Business performance conceptualization is highly contentious and its consensus seems long way to be realized (Dess & Robinson, 1984 and Barney,1997). It is not surprising to find difficulty in arriving into a universal definition of business performance due to its multidimensionality nature (Hansen & Wernerfelt, 1989 and Wiklund & Shepherd, 2005). Moreover, literature suggests interchangeable use of the word business performance, firm performance and organizational performance to mean the same thing (Mgeni, 2015). Lack of unanimity in the conceptualization of business performance does not suggest failure in organizational studies rather signify growth of organizational management discipline. More studies come in, daily with similar connotation yet varying nomenclature of the concept of business performance. Some prefer to call it business performance; some call it organizational performance while others call it firm performance (Steers, 1982 and Mercer Delta Consulting, LLC., 2003).For example; according to Maalu, (2013), firm performance refers to efficiencies and effectiveness in terms of utilization of resources as well as the accomplishment of its goals (Dess & Robinson, 1984and Ricardo 2001) On the other hand, Daft (2000), defined organizational performance as the organization's ability to attain its goals by using resources in an efficient and effective manner. Likewise, studies like; Yang, (2008), Aziz, et al., (2013a), Arshad, & Rasli, 2013, and Arief, Thoyb & Sudiro,2013). Javier, (2002) as cited by Abu-Jarad, Yusof &Nikbin, (2010), associates, business performance with the famous 3Es (economy, efficiency, and effectiveness) of a certain program or activity. Henceforth, this study regard business performance to be the way the organization maximize output geared towards realization of the organizational goal.

2.3. Small and Medium Enterprises

Literature suggests multiple criteria of defining firms in relation to Small and Medium Enterprises worldwide ((URT, 2003, Mgeni, 2015 and Mgeni & Nayak, 2015). Capital investment and size of the firm are the most used criteria in international classification of firms. These criteria help in the distinction between Small and Medium Enterprises (SMEs) from other firm typology. As suggested by existing literature, size criterion for firm classification includes; number of employees, asset ownership, and firm turnover (van der Vaart & Gibson, 2008). Some studies have attempted to use formulae criterion in defining SMEs (Van der Vaart and Gibson, 2008). Formulae criteria regards SMEs to be any formal enterprise with annual turnover-in U.S. dollar terms-of between 10 and 1000 times the mean per capita gross national income, at purchasing power parity, of the country in which it operates (Van der Vaart and Gibson, 2008). According to Hamisi, (2011), SMEs differ from country to country depending on socio-cultural context, thus any attempt to develop a universal definition would be misleading. In Tanzanian context, for example the term SMEs is used to mean micro, small and medium enterprises, sometimes referred as micro, small and medium enterprises 'MSMEs' (URT, 2003). Tanzanian SMEs are commonly defined using total number of employees, total investment and sales turnover. As shown in table:1, in Tanzania's context, SMEs are all firms whose employees are more than 5 but less than 100 and capital investment of above 2500 USD to 400,000 USD (URT, 2003). This study thus uses Tanzanian conception of SMEs because the study took place in Tanzania.

Category	Employee	Capital Investment In Machinery (Tshs.)	Capital Investment In Machinery (USD) as per September 2015
Micro enterprise	1-4	Up to 5 million	Up to 2500
Small enterprise	5-49	Above 5 mil. to 200 million	Above 2500 to 100,000
Medium enterprise	50-99	Above 200mil. to 800 million	Above 100,000 to 400,000
Large enterprises	100+	Above 800 million	Above 400,000

Table 1: Categories of SMEs in Tanzania
Source: Adopted from URT, 2003

3. Literature Review

3.1. Transformational Leadership style and Business Performance of SMEs

Much has been researched on transformational leadership style and its relationship with business performance (Mgeni, 2015). Transformational leadership style has been widely found to be the most effective style of leadership in relation to business performance of organizations (Yang, 2007, 2008). Transformational leadership style is the most preferred style in most business firms because it is said to be effective in realizing organizational goals (Avolio & Bass, 1991; Fairholm, 1991; Lowe, Kroeck, & Sivasubrahmaniam, 1996 and Lo, Ramayah & Cyril de Run, 2010). Most studies have linked transformational leadership to leadership effectiveness and organizational performance (Bass, 1990; Masi & Cooke, 2000 and Erkutlu, 2007). Some previous studies have found a positive strong correlation between transformational leadership style and business performance of SMEs (Aziz, et al., 2013a, 2013b). It has also been found elsewhere that, transformational leadership style is a good predictor of SMEs' business performance variation Aziz, et al., 2013a, 2013b. On the other hand; Barling, Weber, and Kelloway (1996) found that transformational leadership had a moderate positive correlation with the business performance of SMEs. Similar results were reported by Ramey, (2002). To put the discussion short, most studies conducted elsewhere concluded that, transformational leadership is a strong predictor of business performance of SMEs although, there were minor variations depending on the industry, unit of analysis and country where the particular study focused (Ling, Lubatkin, Simsek & Veiga, (2000) and Howell, Neufield & Avolio (2005).

It is important to point out that, variations of findings on the relation between transformational leadership style and business performance of SMEs was due to difference in the context of the particular studies. Studies done in SMEs on the same country but of different industries had results just as how it happened to the same study when done contradictory in different geographical contexts. For example studies on leadership and business performance like, Aziz, et al, (2013a) ; Arshad & Rasli, (2013); Arham, Boucher & Muenjohn, (2013) and Arham, (2014), found a positive correlation between transformational leadership style and business performance. Likewise, they found that transformational leadership was a significant predictor of business performance. On the other hand Obiwuru, (2013), from Nigeria, found transformational leadership to be an insignificant predictor of business performance of SMEs.

Some studies have gone far to research on the relation between transformational leadership style and employee ambidexterity which in turn influence organizational performance in terms of its ambidexterity. According to these studies, transformational leadership has a positive impact on managers' ambidexterity which in turn influences organizational ambidexterity (Purvee & Enkhtuvshin, 2015). Organizational ambidexterity refers to the ability of an organization to both explore and exploit, to compete in mature technologies and markets where efficiency, control and incremental improvement are prized and to also compete in new technologies and markets where flexibility, autonomy, and experimentation are needed (O'Reilly & Tushman, 2013)

Generally it can be argued that, previous works on the impact of transformational leadership style on business performance of SMEs found the following results: **First**; there is a significant positive correlation between transformational leadership style and business performance of SMEs. **Second**, transformational leadership style is a strong and significant predictor of business performance of SMEs. Since no study was found to have done on this area in Tanzania, this study attempts to bridge that gap.

3.2. Research Hypotheses

This study attempts to test the following hypotheses which were drawn from the review of literature on the relation between transformational leadership style and business performance of SMEs.

- H1: There is a significant strong positive correlation between transformational leadership style and business performance of SMEs in Tanzania.
- H2: Transformational leadership style is a strong and significant predictor of business performance of SMEs in Tanzania

3.3. Conceptual Framework

This study used a conceptual framework developed by authors based on previous studies on the relationship between transformational leadership and business performance of SMES. In this model transformational leadership is considered as independent variable while performance is considered as dependent variable.

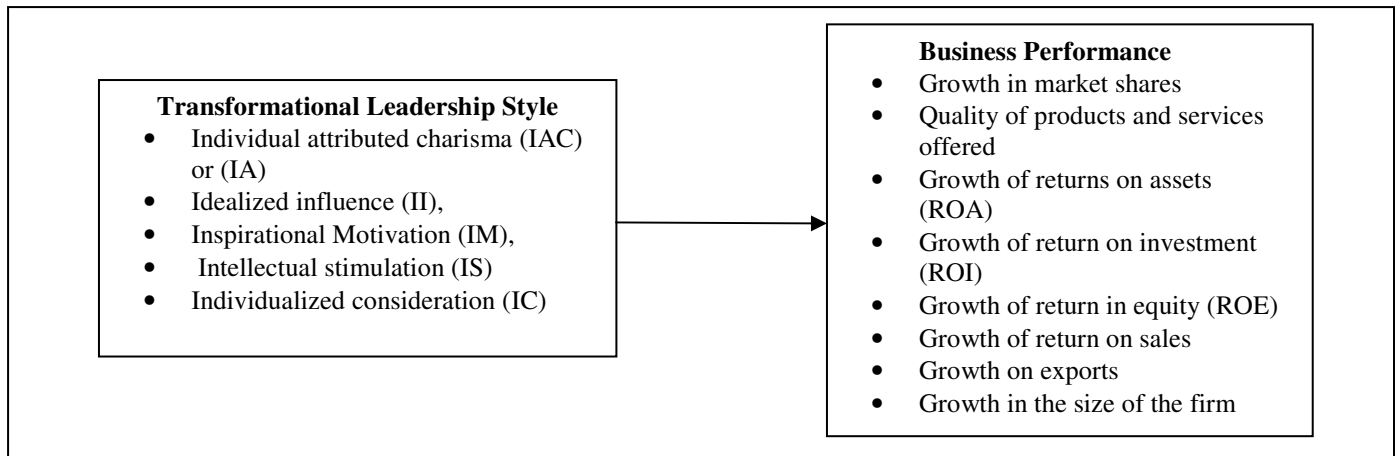


Figure 1: A conceptual framework on the link between transformational leadership style and business performance of SMEs. Source: Authors based on previous studies

4. Research Design

4.1. Research Methodology

This paper used field survey research methodology by mailed questionnaires. Data were collected from CEOs of 60 SMEs in Tanzania. This methodology was found suitable because the study covered 100 SMEs scattered all over the country, of which other methodologies could have been too expensive to afford (Wilcock, 2014). Out of 100 questionnaires sent to respondents 65 questionnaires only returned. Five questionnaires were found incomplete thus discarded because were found to be not suitable for further analysis. Data analysis is thus based on 60 questionnaires.

4.2. Research Method

Quantitative method was used by this study, in which two hypotheses were tested using quantitative statistical tools namely Pearson product moment correlation and simple regression by SPSS. This method was chosen because of the fact that, the nature of the phenomenon involved is widely established thus require quantitative method (Edmondson and Mcmanus, (2007) Furthermore, the hypotheses to be tested required quantitative method because deductive approach was involved (Burke, 2007).

4.3. Measures and Instrumentation

This study used a questionnaire which was formed by merging the first five items of the multi-factor leadership questionnaire (MLQ) which constitutes transformational leadership style and nine items of the Multidimensional business performance questionnaire (MBPQ) which constitutes outcome or result based organizational performance. MLQ and MBPQ are all standard questionnaires developed by Bass & Avolio (1995, 2004, 2006) and Wu, 2009 respectively and used widely by previous studies and thus proven to be valid and reliable. Since this study adopted these tools to be used in Tanzanian context they were retested by factor Analysis (FA) and Cronbach’s Alpha (CR) test to confirm its validity and reliability. FA was used to test construct validity while CR was used to test reliability of the research tools used in this study.

Reliability Statistics		
Cronbach's Alpha	Cronbach's Alpha Based on Standardized Items	N of Items
.827	.823	9

Table 2: Business performance Reliability output

As shown in Table 2, business performance questionnaire (BPQ) had a Cronbach’s Alpha of 0.827 above 0.7 minimum values implying that, the tool is highly reliable. Likewise Transformational leadership questionnaire (TLQ) which is part of MLQ had a Cronbach’s Alpha of 0.806 above 0.7, suggesting high reliability of the particular questionnaire. In other words both TLQ and BPQ have high internal consistency of the items constituting the particular tools

Reliability Statistics		
Cronbach's Alpha	Cronbach's Alpha Based on Standardized Items	N of Items
.806	.804	5

Table 3: Transformational leadership style reliability output

4.3.1. Transformational Leadership Style Measure

Transformational leadership was measured by 5 items from multifactor leadership questionnaire (MLQ) which are summarized as 5Is which includes Individual attributed charisma (IAC) or (IA), Idealized influence (II), Inspirational Motivation (IM), Intellectual

stimulation (IS) and Individualized consideration (IC) (Bass and Avolio, 1995, 1999, 2004, 2006 and Chan I-Harn, 2001). Both five items were rated on a five-points Likert scale ranging from 0 (not at all) to 4 (frequently, if not always). Sample statements which were used in the scale included: 'I go beyond self-interest for the good' (Idealized Influence –Attributes) of the group. And 'I consider the moral and ethical consequences of decisions' (Idealized Influence –Behaviors).

4.3.2. Business Performance Measures

Most of the existing studies on the relation between transformational leadership style and business performance indicates the presence of standard scale of business performance in SMEs. However, it is still controversial on how best performance of SMEs can be measured (Yang, 2007, 2008). Some previous studies used outcome based business performance measures such as Profitability; Gross profit Return on asset (ROA), Return on investment (ROI), Return on equity (ROE), Revenue growth, Market share and stock price for financial business performance of SMEs (FSDT, 2012). Non financial measures were also found in the existing literature as part of the standard measure of business performance of SMEs which included; achieving start up goals overall performance, Provide secure job to employees and Satisfaction with company's performance (Tat Keh, Mai Nguyen, & Ping Ng, 2007). Databases for financial archival data are not certain because in Tanzania SMEs are not legally supposed to keep financial records (Mgeni, 2015). However, most SMEs which conduct self business performance use homegrown measures which in most cases cannot accurately capture what they are intended to measure. In Tanzania, SMEs measure business performance using a number of indicators namely; Turnover, Profitability, Cost of sales, Number of customers, Prices of products/services, Cost of inputs, Number of employees, Stock used, Equipment used and Loss (Ministry of Industry and Trade 2012). Since Tanzania's records of SMEs' business performance is very poor, this study used perceptual business performance approach to ensure smooth data collection process. Self administered questionnaires were mailed to CEOs of SMEs for them to assess and rate the performance of their firms by using existing performance parameters in the particular firm. Since, this study was aware of the perceptual measures limitations including high chances of getting biased and misleading data, maximum precautions were taken when processing data (FCDT, 2012). This study adopted an outcome or result based business performance measures developed by Wu, 2009 as part of multidimensional business performance questionnaire consisting of eight items as shown in figure 1. Business performance questionnaire was measured by 5 point Likert scale ranging from 1 to 5; 1 (very poor to 5 (very good) based on the respondent assessment.

5. Findings

This study used Pearson product moment correlation and simple regression analysis by SPSS 16.0 tool to test the correlation between entrepreneurial leadership style and business performance of SMEs and predict performance variations of SMEs respectively. Pearson product Moment correlation and Simple regression were found to be a convenient method for this study because; they are used to find out how independent variable(s) relates with dependent variable (Levin & Rubin, 2006 and Ken black, 2010). The findings presented here are based on the two hypotheses which were tested by this study. The findings are thus presented in the order of the following hypotheses drawn from the review of literature on the topic covered by this study:

- i. There is a significant strong positive correlation between transformational leadership style and business performance of SMEs in Tanzania.
- ii. Transformational leadership style is a strong and significant predictor of business performance of SMEs in Tanzania

5.1. Data Analysis for Hypothesis 1:

Here we test the hypothesis that; there is a significant strong positive correlation between transformational leadership style and business performance of SMEs in Tanzania. In testing this hypothesis, Pearson product moment correlation was used and its output is shown in table 4. Pearson product moment correlation test found the existence of a strong positive correlation between transformational leadership styles and business performance of SMEs in Tanzania. The Pearson correlation coefficient is 0.851 which is a very strong positive correlation if benchmarked to 1 as a perfect positive correlation. Moreover, Pearson product moment correlation found significant correlation between transformational leadership style and business performance of SMEs in Tanzania. As shown in table three the p-value is 0.000 below 0.01 significant levels (2 tails). Findings thus imply that the hypothesis is supported and that there is a significant strong positive correlation between transformational leadership style and business performance of SMEs in Tanzania. These findings are consistent with previous studies elsewhere such as Aziz, et al, (2013a); Arshad and Rasli, (2013), Arham, Boucher, & Muenjohn, (2013) and Arham, (2014).

Correlations			
		Transformational leadership style	Business Performance
Transformational leadership style	Pearson Correlation	1	.851**
	Sig. (2-tailed)		.000
	N	60	60
Business Performance	Pearson Correlation	.851**	1
	Sig. (2-tailed)	.000	
	N	60	60
**. Correlation is significant at the 0.01 level (2-tailed).			

Table 4: Correlation between transformational leadership style and business performance of SMEs in Tanzania
Source: Authors based on data collected from Tanzanian SMEs between April and July 2015

5.2. Data Analysis for Hypothesis 2:

Here we test the hypothesis that; transformational leadership style is a strong and significant predictor of business performance of SMEs in Tanzania. The regression equation used to test the second hypothesis from the regression output in table 5 can be summarized as $BP=0.403+1.61(TLs)$.

Where BP is business performance

TLs is transformational leadership style

Moreover, table 5 shows that, at 95% level of confidence, p value of the regression model is 0.000, which is potentially less than 0.05 and thus significant; implying that, there is a big possibility that the population slope is significantly different from zero therefore the regression model is capable in predicting variations of dependent variable.

Coefficients ^a								
Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95% Confidence Interval for B		
	B	Std. Error	Beta			Lower Bound	Upper Bound	
1	(Constant)	.403	.262		1.542	.000	.927	.120
	Transformational leadership style	1.161	.094	.851	12.354	.000	.973	1.349
a. Dependent Variable: Business Performance								

Table 5: Regression equation

Source: Authors based on data collected from Tanzanian SMEs between April and July 2015

Model Summary ^b				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.851 ^a	.725	.720	.44256
a. Predictors: (Constant), Transformational leadership style				
b. Dependent Variable: Business Performance				

Table 6: Coefficient of determination (R^2)

Source: Authors based on data collected from Tanzanian SMEs between April and July 2015

As shown in table 6, the coefficient of determination for the regression model was found to be 0.725, implying that transformational leadership style can predict 73% of the variations in business performance of SMEs in Tanzania. This finding suggests that, transformational leadership style is a strong predictor of business performance variations of SMEs in Tanzania. However it does not give us any picture as to whether it is significant and thus useful predictor of business performance unless we include ANOVA regression output. As shown in table 7, P-value of the regression model is found to be 0.000, which is smaller than 0.05 level of significance thus we don't have enough evidence to conclude that transformational leadership style is not a significant predictor of business performance of SMEs in Tanzania. Based on the findings in table 7 we find safe to conclude that, at 0.05, level of significance, transformational leadership style is a significant predictor of business performance variations in Tanzanian SMEs.

ANOVA ^b						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	29.890	1	29.890	152.610	.000 ^a
	Residual	11.360	58	.196		
	Total	41.250	59			
a. Predictors: (Constant), Transformational leadership style						
b. Dependent Variable: Business Performance						

Table 7: Significance of the predictor

Source: Authors based on data collected from Tanzanian SMEs between April and July 2015

Since, table 6 proved that transformational leadership style is a strong predictor of business performance of SMEs in Tanzania and table 7 found the predictor to be significant; we cannot deny the fact that our hypothesis; "Transformational leadership style is a strong and significant predictor of business performance of SMEs in Tanzania" is well supported

6. Conclusion

Based on the findings established by this study, we conclude that, there is a strong and significant positive correlation between transformational leadership style and business performance of SMEs in Tanzania. Moreover, transformational leadership style is found to be a strong and significant predictor of business performance variations of SMEs in Tanzania. These findings are consistent with previous studies elsewhere such as Aziz, et al, (2013a); Arshad and Rasli, (2013), Arham, Boucher, & Muenjohn, (2013) and Arham, (2014). However, this study did not focus into SMEs from specific industry thus further studies are invited to see what happens to the relation between transformational leadership style and business performance, when specific industries are taken into consideration. Further studies are also invited to test whether there is any significant difference when the respondents are managers other than CEOs of SMEs. Generally, policy makers and business leaders in Tanzanian SMEs should take transformational leadership style into serious consideration because it has found to be very effective in influencing business performance in Tanzania and elsewhere.

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