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## Does Firm Size Affect HRM Formality in Organizations?

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### **Abstract:**

*There have been many researches on the human resource management (HRM) in organizations. But the degree to which human resource management (HRM) has been formalized is still relatively unknown, as well as how this formalization relates to organizational performance. The aim of this paper is to identify the relationship between firm size, HRM formality and organizational performance. The findings of this paper contribute to existing research by further clarifying the relationship between HRM formality and organizational performance. This paper identifies that changes in the size of the organization affect the degree of HRM formalization in the organizations. This study also finds that the effect of HRM formality on organization's performance becomes larger when the firms are larger in size.*

**Keywords:** firm size, HRM, HRM formality, organizational performance

### **1. Introduction**

Every owner of organization wants to have successfully organized enterprise which is competitive on the market and realized high profits with employees. And employees of the organization should have high level of motivation in regard to the successful operating of the enterprise. HRM is about managing the managing the workforce of the company. HRM is considered as the driving force behind the stimulating effect on organizational performance (Deshpande and Golhar, 1994). Firm size affects the HRM sophistication in organizations, as firm growth requires formal structure for gaining legitimacy in challenging external and internal environment for labor relations (Daft, 1998; De kok *et al.*, 2003; Nooteboom, 1993). The changes in the size of the organization affect the degree of centralization, standardization, formalization and division of labor. The changes in these variables can lead to changes in the span of control in the organization and this might be the sophistication of management practices in organizations. There is a broad consensus about HRM sophistication having a positive relationship with organizational performance (Guthrie *et al.*, 2004). Some studies only measure HRM and performance indicators e.g. profit, productivity etc. in the hope to find a positive relationship between the two.

### **2. HRM and Small Firms**

Small firms don't have the advantage of scale of operations; due to this they have fewer resources to cover the development costs (Nooteboom, 1993). This study also noted that a lack of benefits from economies of scales makes it harder for them to return the fixed costs of the high performance work system. As a result, it increases their costs to develop and implement the HRM practices even more. Kamble (1998) findings showed that most of the small units are depend on existing workers or advertisement for recruitment purpose. Results also revealed that majority of the firms do not have HR planning, promotion policy and training & development programmes for the employees. A study conducted on HRM in small firms in hotel industry finds that there is no written personnel policy and recruitment is done on the basis of personal approach considering employees' readiness to accept the salary offered. Results show that there are no formal leave rules and labour turnover is very high in small enterprises (Panda, 2000). A large majority of the SME units do not have HR policies, training & development policies and do not have personnel department too. This study observed that recruitment is done on temporary basis and contacts & walk-ins were the main sources of recruitment. Employees are evaluated on the basis of their productivity and behavior (Eresi, 2001). There is considerable diversity amongst SMEs in relation to their use of HR practices (Cassell *et al.*, 2002). Hornsbay and Kuratko (2003) results showed that there is little advancement in the human resource function of smaller firms over the last ten years in USA. SMEs are not able to give to their employees what they want from their job like career development and participation in decision making. Results has also identified that women in these organizations received different treatment than men, resulting into imbalance within the workforce (Szamosi *et al.*, 2004). A study on 89 Vietnamese small firms on the level of formality as a dimension of HR management has found that firm size is closely associated with HR formality and HR formality has positive relation with owners'

perception of firm performance (Nauyen and Bryant, 2004). Sels *et al.* (2006) concluded that the high intensity of HRM in organization is helping in stimulating the firm profit. On the basis of the data collected from 18 small business units of pharmacy sector in Andhra Pradesh, Jyothi (2004) has found that news paper advertisements, consultants and referrals are the sources of recruitment. This study also noted that small scale units do not have any employee promotion policy. Evidences noted that most of the firms made use of performance appraisal and training programmes. King-Kauanui *et al.* (2006) conducted a study on a sample of 200 Vietnamese small and medium sized enterprises and finds that there is a positive relationship between HRM practices like training, performance appraisal, and incentive compensation.

### 3. HRM and Large Firms

According to study of Farh (1995), it is noted that, in the past few decades, large sized private enterprises have gradually established HR systems and learned HR techniques from foreign owned companies. Many research studies find that HRM practices in large organizations are more formalized and structured than smaller firms (Huselid, 1995; Delaney and Huselid, 1996; Delery and Doty, 1996). All of these studies show a positive relationship between some of the HRM practices and various measures of organization's performance. There are three perspectives of HRM practices in large firms as i) universalistic (also known as "best practices") ii) Contingency (also known as "fit" perspective) iii) Configurationally (also known as 'very effective'). The results do not reject any of these perspectives of HRM practices in large firms and differences in their quantitative coefficients and measures of statistical fit are relatively small (Delery and Doty, 1996). A study shows that there are no significant differences in the adoption of HRM by the larger Taiwanese owned firms and foreign subsidiaries. Also with the increase in the subsidiaries and JVs from Japan and Western countries, large sized and SOEs in Taiwan are, gradually establishing Western HRM practices (Shyn-Jer Chen, 1997). Small sized firms lag behind large sized organization with respect to HRM implementation due to lack of resources and government support as well as leadership competence and attention (Stavrou-Costea and Manson, 2006). There are positive effects of formalized HRM practices on the profitability of large firms at the system level i.e. when they firms with innovative systems to firms with traditional systems, they find no major effect when an individual HRM practice is introduced by a firm (Ichniowsky and Shaw ,2003). A research conducted by Singh (2003) identifies that four individual HRM practices like performance based compensation, information sharing, selection, and promotions based on merit are highly related to all the measures of objective firm performance. Chee-Yang Fong *et al.* (2011) conducted a study to identify the association between HRM practices and knowledge sharing in the Malaysian industry context and finds that HRM practices like recruitment, selection, training and development, teamwork, and performance appraisal are positively related with knowledge sharing as perceived by the managers in the manufacturing and service organization.

### 4. HRM and Firm Size

Size of the firm is considered as a major determinant of a number of HRM practices in firms (Hornsby and Kuratko, 1990; Deshpande and Golhar, 1994; Wagar, 1998; Nguyen and Bryant, 2004). Study conducted by Hornsby and Kuratko (1990) shows that the presence of personnel department in firms increases with firm size. Firm size has an indirect effect on the formalization of HRM practices (Hendry and Pettigrew, 1992). Firm size has a significant influence on the adoption of HRM practices in firms (Little, 1986; Hornsby and Kuratko, 1990; Wagar, 1998). Jackson and Schuler (1995) research noted that the larger organization should adopt more formalized and socially responsive HRM activities because these more visible organizations are under more pressure to gain legitimacy. Smaller firms distinguish themselves by lower level of horizontal and vertical complexity, specialization, formalization, decentralization and staff support (Daft, 1986). According to Jackson *et al.*, (1989), HRM system reflects these distinctions, and is less formalized in smaller firms.

### 5. HRM and Organizational Performance

The impact of HRM on firm's performance has become the dominant research issue these days (Guest, 1997). This research issue has led to a number of a number of studies which linked the impact of HRM practices on organizational performance (Faems *et al.*, 2005). HRM matters a lot in achieving the high performance of the organization (Ulrich, 1997). Also, research study noted that the overall set of HRM practices is generally associated with firm performance and competitive advantage (Ferris *et al.*, 1999). HRM is believed to be a very important asset in any organization and will therefore be helpful in the effective management of employees (Barney, 1991) and to create organizational effectiveness for gaining sustained competitive advantage (Guest *et al.*, 2003).

### 6. Conclusion

In general, it can be said that HRM has a positive relationship with organizational performance. According to some of the studies, it can be said that HRM leads to high employee performance and that in turn leads to highest level of organizational performance. In addition, the underlying theories for the research are mostly developed and verified in large organizations, so there exist the uncertainty about the extent to which the theories extend to smaller organization (Heneman *et al.*, 2000). Also, the relative few studies done (compared to research done in larger companies) will consider the impact of HRM on organizational performance in smaller organization still more questionable (Way, 2002). The changes in the size of the organization affect the degree of centralization, standardization, formalization and division of labor. The changes in these variables can lead to changes in the span of control in the organization and this might be the sophistication of management practices in organizations.

## 7. Future Research

It is important that the future research studies should give more attention to the question, “How will HRM formality influence organizational performances?” Because there is very little knowledge about the paths that HRM formality takes to become valuable in achieving organizational performance. Only if the paths between HRM formality and organizational performance are known, then differences on these paths can be signaled and linked to factors such as firm size. More research studies will surely help in solving the puzzle of a phenomenon that now is still indicated as a black box.

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