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Strategic Human Resource Management and Firm Performance: The Mediating Role of Entrepreneurial Orientation

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Abstract

With the emergence of strategy literature both strategic aspect of human resource management and entrepreneurial activities in the organizations have been among the most remarkable subjects of research papers. In the literature the effect of strategic human resource management (SHRM) on firm performance has been extensively examined. The latest papers started to extensively investigate the effects of third variables in this relationship. Also, in recent years some researchers have studied and shown significant interactions between entrepreneurial orientation (EO) and human resource practices. In this study we focus on the important role of entrepreneurial orientation on the relationship between SHRM and firm performance. For this purpose a questionnaire was prepared and data were collected from the firms that operate in different industries in Istanbul. The collected data from questionnaires were analyzed with SPSS and AMOS software programs. Analyses results indicated that entrepreneurial orientation mediated the relationship between strategic human resource management and firm performance (both financial performance and employee performance).

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1. Introduction

In recent years, many organizations and researchers investigate the value of HR functions such as selection, development and retention of employees. Researchers in this field have depended on resource based view to explain the effects of strategic HRM practices on firm performance. With the development of strategic orientation in HR departments, firms have understood that their human capital can provide sustainable competitive advantage (Barney, 1991; Ulrich, 1997). With the emergence of strategic management in firms, many functions and departments of organizations have tried to match their strategies, practices and processes with the business strategy. HRM is one of them and strategic HRM emerged when firms tried to link their HR strategies and practices with business strategy (Wright and McMahan, 1992). Many researches have been conducted to show the effect of strategic HRM practices on firm performance. In previous researches, it has been showed that effective use of HR practices improve firm

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performance by increasing productivity of employees, decreasing turnover rates and increasing sales and profits of the company (Huselid, 1995; Becker and Gerhart, 1996; Delery and Doty; 1996).

With the emergence of strategic management literature, entrepreneurial orientation has become another subject studied deeply in recent years (Lumpkin and Dess, 1996). In today's rapidly changing environment firms always try to renew their products, services and business processes to adapt changing conditions. In order to achieve this, firms give importance to corporate entrepreneurial activities and they are known as entrepreneurially oriented firms. Developing new business processes, new products and services, encouraging research and development processes, supporting new technologies and ideas can be seen as the indicators of entrepreneurially oriented firms.

One of the main focuses of strategic HRM researches is to investigate the effect of strategic HR practices on firm performance (Boxall & Macky, 2007). But most of the previous researches, except researches in recent years, do not have any mediators to explain the relationship between SHRM and firm performance (Becker & Gerhart, 1996). In this study we will investigate the mediator effect of entrepreneurial orientation on the relationship between SHRM and firm performance.

Literature that examines the association between HRM practices and corporate entrepreneurship is a new but growing field (Hayton, 2005). According to Balkin and Logan (1988), poorly established compensation and performance appraisal systems can influence entrepreneurial activities in a negative way. Also, in many other researches (Burgelman, 1983; Schuler, 1986; Brandt, 1986) it is suggested that HRM policies and practices can affect entrepreneurial activities in organizations. In strategic HRM, the main objective was to integrate HR strategies with business strategies. Also, in the previous researches it is proposed that HR functions are affected from business strategies of firms (Schuler, 1989). Therefore if firms select entrepreneurially oriented strategies the role of HR to realize strategic goals becomes very crucial.

The purpose of this study is to investigate the mediator effect of entrepreneurial orientation on the relationship between strategic HRM and firm performance. First of all, depending on previous researches the underlying theory of strategic HRM is given and its relation with firm performance is investigated. Secondly, entrepreneurial orientation and its dimensions are investigated. Thirdly, general associations among SHRM, entrepreneurial orientation and firm performance are discussed and hypotheses are generated. Finally research method and data analysis results are given, conclusions and managerial implications are stated and suggestions for future researches are made.

2. Literature Review And Hypotheses

2.1. Strategic Human Resource Management

The emergence of SHRM is a result of organizations' strategic management tendencies. In today's management practices, all business functions try to link their work methods and practices with firm strategy to achieve higher organizational performance. So, as it is stated by Miles and Snow (1984), SHRM emerges when HR departments try to harmonize their strategies, processes and practices with firm strategies. If you do not observe such a link between HRM and firm strategies, HRM stay as a functional process in the organization.

For companies, strategic human resource management practices can be thought as a tool to achieve competitive advantage. Because strategic human resource management practices are aligned with firm strategy to achieve higher organizational performance (Wright and McMahan, 1992; Jackson and Schuler, 1995). According to Schuler (1992), SHRM is related to effective use of human resources of companies to achieve strategic needs of organizations. According to Wright and McMahan (1992:298), SHRM is "the pattern of planned human resource deployments and activities intended to enable an organization to achieve its goals."

As it is stated by many researchers, SHRM vertically tries to link human resource practices and strategies with the organizations' strategies and strategic management processes. On the other hand, horizontally, it tries to coordinate and harmonize human resource management strategies and practices in itself (Schuler and Jackson, 1987; Guest, 1989; Wright and Snell, 1991; Schuler, 1992). As a result of this organizations and academicians have begun to think HRM in a broader perspective to realize firm strategies and goals. The strategic thinking affected all HRM functions which

called later such as strategic recruitment and selection, strategic planning, strategic training and development, strategic compensation and reward systems, strategic succession and strategic appraisal. All these HR functions and processes tried to integrate with both horizontally HR strategies and vertically business strategies and goals.

Resource based theory is one of the most referred one in SHRM literature. According to Barney (1991), a resource can create sustainable competitive advantage only when it is rare, valuable, inimitable and non-substitutable. According to this view, in order to utilize human capital as a sustained competitive advantage, first of all human resources should add value to the firm. There are a lot of potential workers with different skills, abilities and capabilities and firms try to attract the most talented ones in order to add value to the company. Second, human resources should be rare to create a sustained competitive advantage. All the recruitment and selection programs of organizations which have SHRM practices focus on attracting and hiring the most skilled or talented employees. Third, human resources must be inimitable. Inimitability of human resources is related to people's unique skills, abilities and competencies which are customized for them. And finally, human resources do not have substitutes and this creates a sustained competitive advantage for firms. Technologies, business processes, production processes, products, services, markets, supply advantages, strategies and many different business related sources can be imitable in a way. But human resources do not have any substitutes and this provides a sustainable competitive advantage for companies (Barney, 1991; Wrigt and McMahan, 1992).

2.2. Entrepreneurial Orientation and Dimensions

EO is a concept emerged with the development of strategic management literature and EO is related to firm level entrepreneurial activities and processes (Stevenson and Jarillo, 1990; Lumpkin and Dess, 1996; Wiklund and Shepherd, 2005). Miller (1983) defines EO as firms' innovativeness, proactiveness and risk taking tendencies when they faced with the opportunities in the market. According to Covin and Slevin (1989), EO is a strategic stance of a firm that reflects general competitive orientation of the firm. In another definition, Jennings and Lumpkin (1989) relates EO with entering new markets via providing new services and products above the averages.

In the literature, Miller (1983) defined EO as a three dimensional concept: innovativeness, risk taking propensity and proactiveness. In the later studies, Lumpkin and Dess (1996) added competitive aggressiveness and autonomy dimensions. Although most of the studies used Miller's three dimensions, innovativeness, risk taking propensity and proactiveness (Rauch et al., 2009), in this study in addition to these three dimensions we will also use competitive aggressiveness and autonomy dimensions added by Lumpkin and Dess (1996).

Innovativeness is stated as the most important dimension of EO in different studies (Drucker, 1985; Lumpkin and Dess, 1996) and research results revealed that there is a strong relationship between innovativeness and high performance (Roberts, 1999). According to Lumpkin and Dess (1996: 142), innovativeness reflects "willingness to support creativity and experimentation in introducing new products/services, and novelty, technological leadership and R&D in developing new processes". In today's business environment organizations force themselves to become innovative more than ever before, because the first mover advantage gained with the new products and services offered to the markets create high market share, high sales income and high financial performance (Wiklund, 1999).

Risk taking propensity is defined as the tendency to take risks related to uncertainties in strategic practices of firms (Covin and Slevin, 1989). In most of the studies, risk taking behaviors have been centered in entrepreneurial activities because in order to take advantage of opportunities in the market, trying new things and differentiating a company from its rivals always contains some risk (Hebert and Link, 1988; Morris and Kuratko, 2002).

Proactiveness is related to exploring new opportunities in the markets (Venkatraman, 1989) and proactive firms develop new products and services before their competitors, create new markets to turn and reshape existing balances in favor of the company and forecast future demands and dynamics in the markets (Lumpkin and Dess, 2001). Therefore, proactive firms are expected to become market leader and perform better than their rivals because they can adapt changing conditions faster than others (Hughes and Morgan, 2007).

Competitive aggressiveness is related to firms' direct and extensive competitive entrance to the markets and sectors. Aggressively competitive firms protect their positions in the markets they operate and they perform higher

than their rivals. Because these firms use different methods and practices rather than traditional ones and they exceed their rivals by means of the differentiation they created and the first mover advantages in the markets (Lumpkin and Dess, 1996). Aggressively competitive firms firstly classify their resources at hand, then identify their priorities and achieve sounding outcomes with the optimum use of resources at hand. (Baker and Nelson, 2005; Read and Sarasvathy, 2005).

Autonomy is defined as “independent action by an individual or team aimed at bringing forth a business concept or vision and carrying it through to completion” (Lumpkin and Dess, 2001:431). If managers let their workers to have some level of autonomy, with the independent actions they can influence firms’ strategic decision making practices (Mintzberg, 1994). Autonomy encourages employees to perform on behalf of the company via implementing the best business practices and their novel ideas. Therefore, freedom of employees, their free actions and independent decision making practices are important concepts of autonomy (Lumpkin and Dess, 1996; Voss, Voss and Moorman, 2005).

2.3. Firm Performance

In order to measure firm performance different criteria have been used so far. According to Venkatraman and Ramanujam (1986), firm performance is an indicator of a firm’s capacity to achieve its goals and performance includes both financial and non-financial measures. Financial measures include economic factors and non-financial measures include success indicators such as market share, quality, satisfaction and market effectiveness. On the other hand employees’ contributions to their jobs are very important for the development and success of the organizations. With the talented and skilled employees firms can gain competitive advantage over their rivals. Therefore in this study we used financial performance and employee performance to measure firm performance.

2.4. Development of Hypotheses

The literature investigating the relationship between human resource practices and EO is a new but growing field. In the researches examining the relation between human resource practices and corporate entrepreneurship, it is understood that human resource management is important for corporate entrepreneurial activities (Kuratko et al., 1990; Morris and Jones, 1993; Hayton, 2005; Kaya 2006; Zhang et al. 2009; Messersmith and Wales, 2011).

According to Morris and Jones (1993) there is a relationship between HR practices and entrepreneurial activities. They identified five sets of human resources practices and defined different roles for each practice related to corporate entrepreneurship. In order to facilitate or encourage corporate entrepreneurship HR panning (e.g. formal planning, implicit job analysis, integrative job design, less structured jobs, high employee involvement), recruitment and selection (e.g. external candidate use, broad career paths, less formalized selection, extensive job socialization, open recruitment and selection), training and development (e.g. career oriented long term training, individualized training, high employee participation, developing managerial skills and continuous training), performance appraisal (e.g. effectiveness, long term performance, result oriented performance, innovation and risk criteria in performance, tolerance to failures, effects of project life cycle in appraisals), compensation and reward systems (e.g. long term performance, individual performance, significant financial rewards, merit and incentive-based) are regarded as important tools for organizations (Morris and Jones, 1993: 881).

Hayton (2003) distinguished discretionary HRM practices from traditional ones. Traditional HRM practices are more efficiency oriented and related to matching individual skills with the needs of the organization. But discretionary practices are learning oriented and encourage employee commitment, participation, knowledge sharing and tolerate failures. Therefore it is found that discretionary human resource management practices positively affected entrepreneurial activities and entrepreneurial performance. In another study Messersmith and Wales (2011) found important connection between EO and HRM by investigating the effects of high performance work systems on EO in young, entrepreneurially-oriented, high-technology firms. Kaya (2006) found that human resource practices enhance the effect of EO on firm performance. That means if organizations want to develop their entrepreneurial activities they should give importance to human resource departments and support their practices. In this study we will test the reverse. In other words, we wonder whether firms can enhance the effects of SHRM practices on firm performance by means of EO.

In the literature there are many studies have investigated the relationship between SHRM and performance but the research area examining the mediating effect of EO on the relationship between SHRM and performance is nearly empty. Depending on our review of previous studies investigating the relationship among HRM, EO and performance we developed our hypotheses and research model as below:

H1: Entrepreneurial orientation mediates the relationship between strategic human resource management and financial performance.

H2: Entrepreneurial orientation mediates the relationship between strategic human resource management and employee performance.

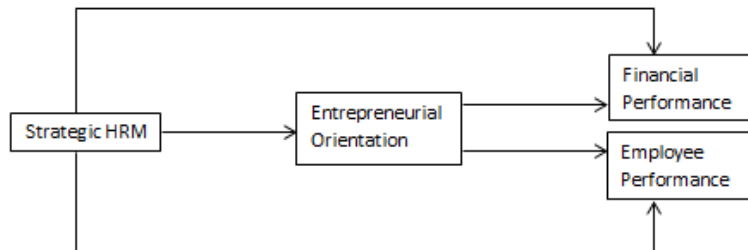


Figure 1. Conceptual Research Model

3. Methodology

3.1. Measurement Instruments

In order to measure research purpose we prepared a questionnaire depending on the scales used in previous studies in the literature. Bartram et al (2007) modified the SHRM index developed by Huselid (1995). In this study we used 13 items SHRM index used by Bartram et al (2007). EO scale adapted from Hughes and Morgan (2007). This scale includes 18 items: 3 items for risk taking, 3 items for innovativeness, 3 items for proactiveness, 3 items for competitive aggressiveness and 6 items for autonomy. Financial performance scale includes 6 items and adapted from Lynch et al. (2000) and Baker and Sinkula (1999). Employee performance scale includes 3 items adapted from Fuentes et al. (2004) and Rahman and Bullock (2004).

3.2. Sample and Data Collection

In order to collect data we used a questionnaire survey. Research data were collected from firms that operate in Istanbul and have human resource departments. We collected 297 valid questionnaires from managerial positions of companies. Data obtained from those 297 questionnaires were analyzed with SPSS and AMOS programs. After collecting the data, statistical analyses provided basic features about respondents. Demographic results indicated that 204 participants were male and 92 participants were female. Most of the participants had less than 5 years of service in the firm and the average age of majority was between 30-39.

3.3. Factor Analyses and Reliabilities

In order to understand the underlying dimensions of the measured variables used in the survey exploratory factor analysis was performed by using principal component analyses extraction method and promax rotation. Kaiser-Meyer-Olkin (KMO) sample adequacy test and Bartlett sphericity tests were applied to test whether the data set is suitable for factor analysis. If KMO value is greater than 0.5 and “p” value is less than 0.05 in Barlett test we can say that data set is adequate for factor analysis (Field, 2009). According to analyses results KMO value is 0,872 and Barlett test result is significant at 0.001 levels. That means our data set is adequate for factor analysis.

In the principal component analysis factor loadings were selected above 0.50 considering the size of the sample (Hair et al 2010). In the factor analysis eigenvalues was set to be higher than 1.00. In SHRM scale questions 4 and 6 loaded below 0.50 and questions 5 and 10 loaded in two different factors. Therefore we took these four items out of

factor analysis. Proactiveness dimension in entrepreneurial orientation scale and related three items are not included in the analyses because this dimension has not been sufficiently understood by participants. The remaining items loaded in predicted factor components according to principal component analyses and factor loadings took values between 0.508 and 0.889.

Factor reliabilities were checked with Cronbach's Alpha values and all values found greater than 0.70 which is the lowest acceptable value. This shows that factors are reliable and have internal consistency. Factor analysis results are given in the table below.

Table 1: Factor Analysis Results

	SHRM	Financial Performance	Employee Performance	Innovativeness	Risk Taking	Competitive Aggressiveness	Autonomy
HR practices are integrated to be consistent with each other	,889						
HR strategies' integration with organisation's strategy	,863						
Matching characteristics of managers to strategic plan	,788						
Identifying necessary managerial characteristics in the long term	,788						
HR personnel are a key influence in setting HR strategy	,699						
Development programmes are designed to support strategic changes	,616						
Modifying compensation systems to encourage managers	,607						
Evaluating key personnel based on their potentials	,553						
Job analyses are based on what the job may entail in the future	,511						
Overall success level in financial terms		,730					
Financial success of new products		,712					
Average net profitability compared to equity		,691					
Net profitability before tax compared to all available resources		,666					
Net revenue achieved from basic operations		,656					
Average annual increase in sales		,643					
Satisfaction level of employees			,810				
Absenteeism rate of employees			,795				
Morale level of employees			,650				
ENTREPRENEURIAL ORIENTATION							
Our business seeks out new ways to do things				,864			
Our business is creative in its methods of operation				,800			
Improvements and innovations in our business				,681			
People are encouraged to take calculated risks with new ideas					,740		
'Risk taker' is considered a positive attribute for people					,705		
Emphasizing on exploration and experimentation for opportunities					,508		
Taking a bold or aggressive approach when competing						,820	
Our business is intensely competitive						,782	
We try to undo and out-manuever the competition as best as we can						,551	
Freedom and independence given to employee to decide on their own							,865
Making and instigating changes while employees perform their tasks							,807
Authority and responsibility given to employees to perform better							,703
Employees are permitted to act and think without interference							,682
Employees are given freedom to communicate without interference							,613
Employees have access to all vital information							,561
Eigenvalues	9,262	2,251	1,032	1,721	1,609	1,349	2,816
Variance Explained	28,067	6,820	3,128	5,215	4,875	4,088	8,534

Notes (i) Principal Component Analysis with Promax Rotation

(ii) KMO =0,872, Bartlett Test; $p < 0.001$

(iii) Total Variance Explained (%): 60,727

Correlation analysis indicates that there is a positive and significant relationship between factor variables. This shows that research variables correlate each other sufficiently and they can be reviewed adequately. Also multicollinearity does not exist in the research variables because correlation levels are less than 0.7 (Hair et al. 2010).

Table 2: Correlation analysis

	1	2	3	4	5	6	7	8	Mean	Std. Dev.
1. SHRM	(0,89)								3,62	0,66
2. Risk Taking	,559***	(0,79)							3,42	0,77
3. Innovativeness	,584***	,616***	(0,84)						3,75	0,73
4. Competitive Aggressiveness	,379***	,323***	,309***	(0,71)					3,79	0,70
5. Autonomy	,429***	,444***	,353***	,251***	(0,81)				3,35	0,70
6. Financial Performance	,179***	,164***	,246***	,256***	,161***	(0,77)			3,52	0,64
7. Employee Performance	,407***	,310***	,381***	,184***	,251***	,244***	(0,71)		3,52	0,78
8. Entrepreneurial Orientation	,667***	,824***	,781***	,633***	,693***	,161***	,251***	(0,82)	3,58	0,53

***; Correlation is significant at the 0.001 level. Cronbach's Alpha () is represented in diagonals

3.4. Test of the Research Model

In order to test research hypotheses path analysis technique which based on the structural equation modelling was used. The results of path model are shown in the table below.

Table 3: Hypothesis Testing

	IV	DV	Standardized Estimates	Indirect Effect ^a		
				Estimate	Confidence Intervals	
					Lower	Upper
Model w/o Mediator	SHRM	→ Financial Performance	0,179**			
	SHRM	→ Employee Performance	0,407***			
Model with Mediator	SHRM	→ Entrepreneurial Orientation	0,667***			
	Entrepreneurial Orientation	→ Financial Performance	0,289***			
	Entrepreneurial Orientation	→ Employee Performance	0,203***			
	SHRM	→ Financial Performance	-0,014 (ns)	0,193**	0,108	0,279
	SHRM	→ Employee Performance	0,272**	0,135**	0,058	0,214

***p<0.001, **p<0.01, a; 5000 Bootstrap Samples, %95 Confidence Interval

According to path analysis results, before including the mediating variable into the analysis SHRM has significant and positive effect on financial performance ($\beta=0,179$; $p<0,01$) and employee performance ($\beta=0,407$; $p<0,01$). After including the mediating variable into the analysis it is shown that the significant effect of SHRM on financial performance disappeared and the significant effect of SHRM on employee performance decreased ($\beta=0,272$; $p<0,01$). According to Baron and Kenny (1986) mediating effects are obvious but on the other hand according to Preacher and Hayes (2004) mediating effects are only controlled.

Bootstrapping is an increasingly preferred method of testing the indirect effect. It is a non-parametric method depends on resampling with replacement that is done in many times. (Preacher and Hayes, 2004; Shrout and Bolger, 2002). In this study, in order to verify mediating effects, indirect effect of SHRM on financial performance and employee performance is examined by using Bootstrapping method at 5000 sample level. Mediating effects are validated because indirect effects ($\beta=0,193$; $p<0,01$ for financial performance; $\beta=0,135$; $p<0,01$ for employee performance) are found significant at 95 percent confidence level.

Depending on the analyses results both H1 and H2 are supported. That means EO has complete mediation effect on the relationship between SHRM and financial performance and partial mediation effect on the relationship between SHRM and employee performance. Related path model results are as shown below.

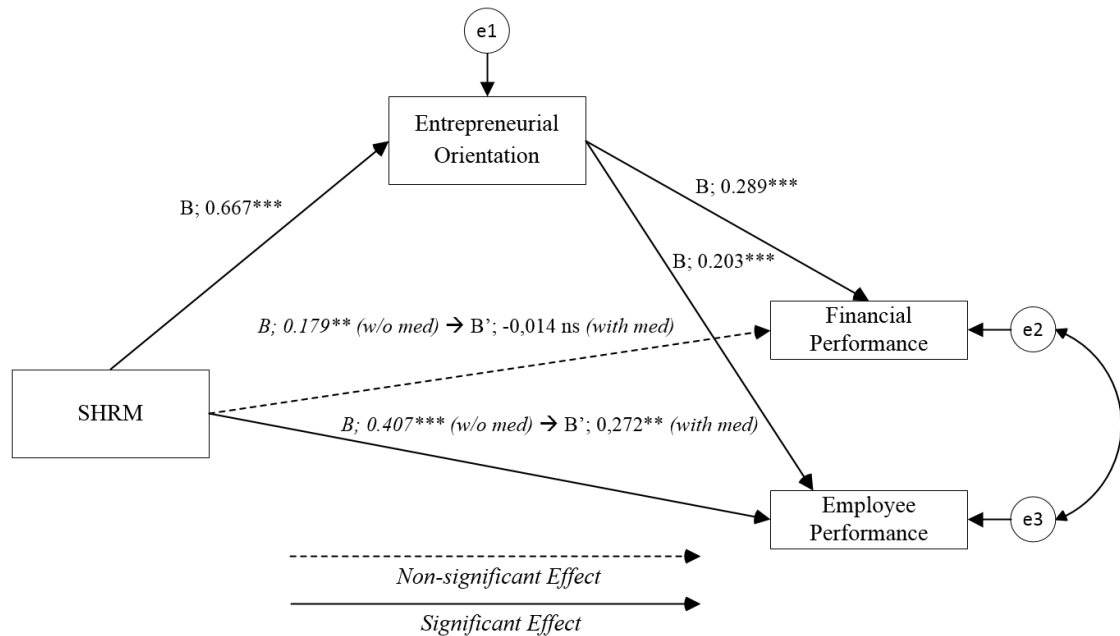


Figure 2: Path Analyses Results ($***p < 0.001$, $**p < 0.01$)

4. Discussion and Conclusion

In this study the role of SHRM and EO on firm performance was investigated. The results indicated that EO has a full mediation role between SHRM and financial performance and partial mediation role between SHRM and employee performance. Although there are many studies examining SHRM - firm performance relation (Wright and McMahon, 1992; Lado and Wilson, 1994; Huselid, 1995; Rogers and Wright, 1998) and human resource management practices – EO relation (Morris and Jones, 1993; Hayton, 2005; Kaya, 2006; Messersmith and Wales, 2011) in the literature, the mediation role of EO between SHRM and firm performance has not been studied deeply.

According to Covin and Slevin (1991), depending on the behavioral model of entrepreneurship, firm level entrepreneurship is becoming more attractive because processes and behaviors are manageable. Firm level activities can be managed with the help of organizational strategies, structures, systems and cultures (Covin and Slevin, 1991). If companies pursue entrepreneurially oriented goals such as being more proactive, encouraging innovativeness and risk taking and competing more aggressively, the strategic HR activities automatically will turn to provide necessary HR support such as human capital, sufficient training programs and competitive compensation and reward systems to company in order to achieve its goals and strategies in the long run. As a result, HR's contribution to firm performance is expected to automatically increase. Depending on the literature and analyses results managers are suggested to determine necessary level of entrepreneurial activities and HR departments can set their roles and activities to meet the need of entrepreneurial goals of organizations. Therefore the positive contribution of HR activities on firm performance can increase.

However, this study has some limitations. First of all, our survey was conducted on firms operating in different industries in Istanbul. For the generalizability of findings, further researches can be conducted in different regions of Turkey and different countries. Also, further researchers can focus on specific sectors in order to show whether any sectoral differences exist in the area. In this study we measured mediator effect of entrepreneurial orientation but further researchers can measure other strategic orientations such as marketing orientation and learning orientation. Our research was designed as a cross sectional study to test the propped relationships among variables. With this design,

we took the perceptions of respondents at a certain point in time. Therefore future researchers can examine relationships on a longitudinal basis.

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