

# HUMAN RESOURCE PRACTICES AND ORGANIZATIONAL PERFORMANCE LINK: A THEORETICAL REVIEW

*Subash Chandra Pattnaik,*

Ph.D. Scholar,  
Department of Business Administration,  
Utkal University, Vani Vihar,  
Bhubaneswar, Odisha, India

*Rashmita Sahoo,*

Asst. Professor,  
Department of Business Administration,  
Utkal University, Vani Vihar,  
Bhubaneswar, Odisha, India

## ABSTRACT

*Relationship between HR practices and organizational performance is one of the leading themes of research for quite some time. Though a large number of researches have been conducted to investigate the relationship, very few researches have been conducted in India in its dynamically evolving HRM scenario. It is, therefore, desirable that for further research to be conducted, a theoretical review should be made as a guideline for future researchers. This paper, therefore, an attempt to present a literature review of the researches conducted so far in the area and exploring the direction in which future research should take place.*

**Keywords:** *HR practices, organizational performance, literature review, system view.*

### Introduction:

HRM has, of late, emerged as an essential factor for sustained competitive advantage. Previous researchers have highlighted that organizations could develop sustained competitive advantage through management of scarce and valuable resources (Barney, 1991). HR enables organizations to achieve optimization of resources and continuous improvement in effectiveness (Wernerfelt, 1984). An organization takes time to nurture and develop human capital in the form of knowledge, skills, abilities, motivation, attitude and interpersonal relationships, which makes it difficult for competitors to imitate (Becker & Gerhart, 1996). Pfeffer (1994) stressed that HR has been vital for a firm's sustained performance. In a knowledge economy, HR has been recognized as a strategic tool, essential to organizational profitability and sustainability. This realization has led to the new role of HR managers as strategic partners in formulating and implementing organizational strategy (Myloni et al, 2004). Organizations are proactively pursuing HR practices to capitalize on the strength of this vital asset for sustained competitive advantage in knowledge economies (Jackson & Schuler, 2000; Mac Duffie, 1995).

### HR Practices and Organizational Performance Link:

Impact of HR practices on firm performance has been a leading theme of research in the past decades and the results of extensive empirical investigations by previous researchers have been encouraging, indicating a positive association between the two (Dyer and Reeves 1995; Huselid 1995; Becker and Gerhart 1996; Guest 1997; Becker & Huselid, 1998; Harel and Tzafrir, 1999; Appelbaum et al 2000; Guest et al, 2000a, 2000b, 2000c; Boselie, 2002). However, all extant research has been conducted on the operations of domestic firms in the developed countries but limited research has been done to examine the relationship of HR practices and performance in the developing countries, especially in the Indian sub-continent. Prior studies have validated the link between HR practices and organizational performance in the USA and European countries (Boselie et al., 2001; Hoque, 1999), Asia (Bjorkmand & Xiucheng, 2002; Ngo et al., 1998). To add more validity to this growing stream of research, more studies in varied settings and particularly in the developing economies need to be conducted. Table 1 lists out chronologically studies conducted by various researchers in various countries to explore the link between HR practices and organizational performance.

**Impact of select HR Practices:*****Compensation Practices and Organizational Performance:***

Compensation refers to all forms of payment made to employees by their employer as a result of their employment relationship (Dessler, 2003). It motivates employees to behave in ways they desire. Compensation refers to all monetary payments and all commodities used instead of money to reward employees. Compensation practices contribute to competitive advantage by promoting more productive and skilled workforce (Pfeffer, 1995). Huselid (1995) asserts that the compensation system is recognized as employee merit and it is widely linked with firm outcomes. In regulating human action, money can have instrumental or symbolic motivational properties (Stajkovic & Luthans, 2001). Money can provide outcomes that satisfy physiological or psychological needs in instrumental form. In addition, money also generates social comparison information in symbolic form.

The expectancy theory suggests that rewards that can be understood as a form of direct and indirect compensation packages have potential to influence employee work motivation. Thang (2004) suggests that compensation and reward can be powerful tools for getting efforts from the employees to fulfil the organizational goals. Leonard (1990) said that the companies following long-term incentive plans gets more increase in return on equity than those that ignore such plans.

Authors have reported positive influence of compensation on organizational commitment (Lawler & Jenkins, 1992) while others have shown no significant influences (Shore & Barksdale, 1998). However, results generally show that compensation has a strong and significant relationship with both organizational commitment and also normative commitment in particular.

Previous researchers have reported positive correlation between compensation practices and employee performance. Shahzad et al (2008) have shown in their research results that there is a positive relationship of compensation practices with the performance of university teachers of Pakistan. Ferguson and Parsons (1992) proposed that compensation strategy is part of the whole organizational strategy and it could help the organization acquire competitive advantage. McNally (1992) emphasized that compensation not only should attract and retain talents, but also motivate employees to attain organizational goals. For this reason, compensation structure should be a strategic tool, which should be integrated with organizational strategy to help the organization attain its strategic goals.

Frye (2004) examined the relationship between equity-based compensation and performance and found positive relationship between the two. He argued that for human capital intensive firms

compensation plays a crucial role in 'attracting and retaining highly skilled employees'.

Incentive pay plans positively and substantially affect performance of workers if combined with innovative work practices like flexible job design, employee participation in problem-solving teams, training to provide workers with multiple skills, extensive screening and communication and employment security (Ichniowski et al, 1997). High performance work practices including compensation have a statistically significant relationship with employee outcomes and corporate financial performance (Huselid, 1995).

***Performance Appraisal and Organizational Performance:***

Performance management systems manage and align all the organization, resources in order to achieve the highest possible performance. Williams (2002) argued that performance management involve determining the strategic objective, establish team goals, plan of performance developed, Analyze the performance (by using appraisal system) identified need of development and Assign rewards.

Researches from Schraeder, Becton & Portis, 2007 also identified that the method of personnel appraisal also goes a long way in determining the success and competitive positioning of an organization. Prowse & Prowse (2009) argued that there are many methods of appraisal that can be adopted ranging from comparing one person's performance with another, evaluating performance against set of traits to appraising the workers performance against the objectives of the organization (Mansor, 2011).

***Training Practices and Organizational Performance:***

Training and development is a process meant to provide both new and existing employees the knowledge and skills they need to do their current job as well prepare them for changes on the job and also future job demands (Dessler, 2003). Previous researchers have found a positive relationship between training and development practices and organizational commitment and organizational performance (Pare et al, 2000) while some have found no significant correlation (Shore & Barksdale, 1998).

Training and development may be related to firm performance in many ways. Firstly, training programmes increase the firm specificity of employee skills, which, it turn, increases employee productivity and reduces job dissatisfaction that results in employee turnover (Huselid, 1995). Secondly, training and developing internal personnel reduces the cost and risk of selecting, hiring, and internalizing people from external labour markets, which again increases employee productivity and reduces turnover. Training and development like job security requires a certain degree of reciprocity: A company that train and

develop systematically its employees advocate them that their market value develops more favourably than in other firms. This increases employees' productivity, commitment, and lowers turnover.

Past researchers have examined the growth strategies in the retail sector and suggested that modern retailers should place more emphasis on the policies and practices that could contribute to staff retention, rather than on the immediacy of recruitment and selection. Zhu (2004) reviewed the changes in the area of human resource development in Japan and observed that some companies and industries have shifted towards a more strategic approach that emphasizes the impact of effective learning at both individual and organizational levels on long-term organizational competitiveness. Huselid (1995) found that the education and development of employees have a significant effect both upon the personnel productivity and the short-term and long-term indicators of organizational performance.

Michie and Quinn (2001) investigated the relationships between UK firms' use of flexible work practices and corporate performance and suggested that low levels of training are negatively correlated with corporate performance.

#### Conclusion:

A survey of the extant literature indicates that a lot of research has been done to examine the relationship between HR practices and organizational performance. But, very limited research has been conducted in Indian in its changing context. Hence, more research has to be conducted in order to explore this relationship in Indian context.

#### References:

- Appelbaum E., Baile T., Berg, P. & Kallenberg, A. L. (2000). *Manufacturing Advantage: Why High Performance Work Systems Pay Off*. Ithaca: Cornell University Press
- Barney, J. (1991). Firm resources and sustained competitive advantage. *Journal of Management*, 17, 99-120
- Becker, B. & Gerhart, B. (1996). The impact of human resources management on organizational performance: Progress and prospects. *Academy of Management Journal*, 39, 779-801
- Becker, B.E. & Huselid, M.A. (1998). High performance work systems and firm performance: A synthesis of research and managerial implications. *Research in Personnel and Human Resource Management*, 16, 53-101
- Björkman, I. & Xiucheng, F. (2002). Human resource management and performance of western firms in China. *International Journal of Human Resource Management*, 13, 853-64
- Boselie, P. (2002). *Human resource management, work systems and performance: A theoretical-empirical Approach*. Tinbergen Institute Rotterdam, Thela Thesis Research Series, no.274, Erasmus University Rotterdam
- Boselie, P., Paauwe, J. & Jansen, P. (2001). Human resource management and performance: Lessons from the Netherlands. *International Journal of Human Resource Management*, 12(7), 1107-1125
- Dessler, G. (2003). *Human Resource Management*. Delhi: Pearson Education Asia
- Dyer, L. & Reeves, T. (1995). Human resource strategies and firm performance: What do we know and where do we need to go? *International Journal of Human Resource Management*, 6, 656-70
- Ferguson, W. J. & Parsons, J.F.C. (1992). *Compensation Strategies*. Mortgage Banking, 52(8), 47-53
- Frye, M. B. (2004). Equity-based compensation for employees: Firm performance and determinants. *The Journal of Financial Research*, 27(1), 31-54
- Guest, D. (1997). Human resource management and performance: A review and research agenda. *The International Journal of Human Resource Management*, 8(3), 263-76
- Guest, D.E., Michie, J., Sheehan, M. & Conway, N. (2000a). *Employment Relations, HRM, and Business Performance: An Analysis of 1998 Workplace Employee Relations Survey*. London: CIPD.
- Guest, D.E., Michie, J., Sheehan, M. & Conway, N. (2000b). Getting inside the HRM-performance relationship. Paper presented at the Academy of Management Conference, Toronto
- Guest, D.E., Michie, J., Sheehan, M., Conway, N. & Metochi, M. (2000C). *Effective people management: First findings from the future of work-study*. London: CIPD
- Harel, G.H. & Tzafirir, S.S. (1999). The effect of human resource management practices on the perceptions of organizational and market performance of the firm. *Human Resource Management*, 38(3), 185-200
- Hoque, K. (1999). Human resource management and performance in the UK hotel industry. *British Journal of Industrial Relations*, 37, 419-43
- Huselid, M.A. (1995). The impact of human resource management practices on turnover, productivity, and corporate

- financial performance. *Academy of Management Journal*, 38(3), 635–672
- Ichniowski, C., Shaw, K. & Prenunshi, G. (1997). The effect of human resources practices on productivity: A study of steel finishing lines. *American Economic Review*, 87, 291–313
- Jackson, S. E. & Schuler, R. S. (2000). *Managing human resource—A partnership perspective*. London: Southern Western College Publishing
- Lawler, E.E., & Jenkins, G.D. (1992). *Strategic Reward Systems*. In M.D. Dunnette & L.M. Hough (Eds.), *Handbook of Industrial & Organizational Psychology* (2nd Ed). Palo Alto, CA: Consulting Psychologist Press, Inc.
- Leonard, J. S. (1990). Executive pay and firm performance. *Industrial and Labor Relations Review*, 43, S13-29.
- MacDuffie, J.P. (1995). Human resource bundles and manufacturing performance: Organizational logic and flexible production systems in the world auto industry. *Industrial and Labor Relations Review*, 48, 197-221.
- Mansor, N. A. (2011). Determinants of performance management system in South East Asia. *Interdisciplinary Journal of Contemporary Research in Business*, 3(2), 43–56.
- McNally, K.A. (1992). Compensation as a strategic tool. *HRM Magazine*, 37(7), 59-66
- Michie, J. & Sheehan-Quinn, M. (2001). Labour market flexibility, human resource management and corporate performance. *British Journal of Management*, 12(4), 287-306
- Myloni, B., Harzing, A.W.K. & Mirza, H. (2004). Host country specific factors and the transfer of human resource management practices in multinational companies. *International Journal of Manpower*, 25(6), 518 – 534
- Ngo, H.Y., Daniel, T., Chung-Ming, L. & Siu-yun, L. (1998). Human resource practices and firm performance of multinational corporations: Influences of country origin. *International Journal of Human Resource Management*, 9, 632–52
- Pare, G., Tremblay, M., & Montreal, H. (2007). The influence of high-involvement human resources practices, procedural justice, organizational commitment, and citizenship behaviors on information technology professionals' turnover intentions. *Group & Organization Management*, 32(3), 326–357.
- Pfeffer, J. (1994). *Competitive advantage through people: Unleashing the power of the work force*. Boston: Harvard Business School Press
- Pfeffer, J. (1995). Producing sustainable competitive advantage through effective management of people. *Academy of Management Executive*, 9, 55-69.
- Prowse, P., & Prowse, J. (2009). The dilemma of performance appraisal. *Journal of Measuring Business Excellence*, 13(4), 69–77.
- Schraeder, M. Becton, J., & Portis, R. (2007). A critical examination of performance appraisals. *The Journal for Quality and Participation*, 21(1), 20–25.
- Shahzad, K., Bashir, S. & Ramay, M.I. (2008). Impact of HR practices on the perceive performance of university teachers in Pakistan. *International Review of Business Research*, 4(2), 302-315
- Shore, L. M., & Barksdale, K. (1998). Examining degree of balance and level of obligation in the employment relationship: A social exchange approach. *Journal of Organizational Behaviour*, 19, 731–744.
- Stajovic, A.D. & Luthans, F. (2001). Differential effects of incentive motivators on work performance. *Academy of Management Journal*, 11, 580-591
- Thang, L.C. (2004). *Managing human resources in Vietnam: An empirical study of an economy in transition*, School of Management, Asian Institute of Technology, Thailand
- Wernerfelt, B. (1984). A resource-based view of the firm. *Strategic Management Journal*, 5, 171-180.
- Williams, R.S. (2002). *Managing Employee Performance*. London, Thomson Learning.
- Zhu, Y. (2004). Responding to the challenges of globalization: Human resource development in Japan. *Journal of World Business*, 39, 337–348.

Table 01

SI No	Researcher(s)	Place of study	Year of Study
1	Lee and Chee	Korea	1996
2	Ngo et al	Hong Kong	1998
3	Morishima	Japan	1998
4	Ichniowski and Shaw	USA and Japan	1999
5	Harel and Tzafrir	Israel	1999
6	Bartel	Canada	2000
7	Bae and Lawler	Korea	2000
8	Chang and Chen	Taiwan	2002
9	Bjorkmanin and Xiucheng	China	2002
10	Paul and Anantharaman	India	2003
11	Sing	India	2003
12	Bae et al	Pacific Rim	2003
13	Guthrie	New Zealand	2003
14	Sang	Taiwan and Cambodia	2005
15	Katou and Bedhwar	Greece	2006
16	Tessema and Soeters	Eritrea	2006
17	Tsai	Taiwan	2006
18	Zheng et al	China	2006
19	Rizov and Croucher	Europe	2008
20	Beh and Loo	Malaysia	2013
23	Amin, Ismail, Rasid and Selemani	audi Arabia and Malaysia	2014
21	Aguta and Balcioglu	Turkey	2015
22	Singh and Kassa	Ethiopia	2016

\*\*\*\*\*