Critical Analysis of the Performance Management System (PMS) in SMEs of Karachi

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Abstract: In the midst of global financial slump SMEs of developing & developed economies appear to be a center of gravity for researchers and management practitioners and advent of globalization exaggerate its role indeed. In this situation only hundred percent exploitation of financial, human and technological potential of SMEs make certain the competitiveness and growth possibilities. Relatively little research has been conducted on performance management system in Pakistani SMEs. This study is more focused headed for investigating the PMS implementation and post implementation effects in small firms. Performance Management (PM) is a process for establishing a shared understanding about what needs to be achieved. It is an approach to managing people that increases the level of personal performance and business success. Any organization with suitable performance management system increase employer conviction that it has the right people in the right place at the right time. Performance management must consist of two basic components one is talent exploitation and preservation and second is performance feedback mechanism. In an organizational perspective one thing is quiet evident that maturity of employer-employee relationship depends upon employee job satisfaction and performance and conceptually job satisfaction and performance is directly proportional to each other. The dominant findings indicate that, SMEs in Pakistan are generally less likely to adopt ‘formal’ PMS practices, including setting goals, monitoring performance and performance evaluation practices. Similarly, they have not formulated ‘formal’ HR policy and human resource departments usually pursue traditional means of basic HR functions such as employee recruitment, training and compensation. However, from statistical results of textile sector small and medium enterprises exposed that employees do not have a clear understanding of what performance management system aim to achieve similarly big number of employees consider that performance appraisal is not aligned with organizational goals it has no functionality in employee career planning or progression.

Key words: Performance Management System, SMEs, setting goals, monitoring performance, and performance evaluation practices.

INTRODUCTION

1.1. Background of Study:
The strategic vision of organization in knowledge economy is more employees focused and skill deficiency in the labor pool makes it more vulnerable. At macro economic level contribution of SME sector is twofold one towards alleviation of poverty at bottom line and second economic prosperity at top line. Profound literature review has confirmed contradictory definitions of SME from different authors. According to Verhees and Meulenberg (2004) SME is run and controlled directly by its owner and Carson et al., (1995) has explained that small firm is an entrepreneurial activity and normally based upon entrepreneurship. Employee size of small firm should be in between 20 and 99 employees, while medium to large firms employ over 100 workers (Wiesner and McDonald 2001). Kandula (2007) defined that “…performance management is a process of designing and executing motivational strategies, interventions and drivers with an objective to transform the raw potential of human resource into performance”. Kaplan, (1996) and Mazzarol (2003) state that, any organization with suitable performance management system increase employer conviction that it has the right people in the right place at the right time. PMS is a systematic approach to managing people that increases the level of personal performance and business success and performance management is a process for establishing a shared understanding about what needs to be achieved. However, performance management must consist of two basic components one is talent exploitation and preservation and second is performance feedback.
mechanism (Vance 2006). Tangen (2005) discern that a successful PMS mechanism should maintain, and perform organizational activities. Karami A., et al., (2008) suggested that human resource intellectual competence decides competitive advantage of the organization and (Karami A., et al., 2008; Sanger (1998) and Ashton (1997) have anticipated that in presence of financial based performance management system could not handle complex and turbulent work conditions and may not promising to craft best possible decisions in relation to resource allocation. As for as performance management is concerned Hudson et al. (2001) found that the majority of the SMEs did not have a formal feedback mechanism. Mazzarol (2003) observed that the main reason behind ineptness of SME sector is because of traditional methods of employee performance management system normally pursue financial outputs and customer growth. Therefore, we have identified the real problem Pakistan SME sector is facing and in the same course relatively little research has been conducted so far on performance management system in Pakistani SMEs. This study is more focused headed for investigating the PMS implementation and post implementation effects in small firms. The dominant findings indicate that, SMEs in Pakistan are generally less likely to adopt ‘formal’ PMS practices, including setting goals, monitoring performance and performance evaluation practices.

1.2. Problem Statement:

It is identified that good performance management must consist of two basic components one is talent exploitation and preservation and second is performance feedback mechanism. SMEs in Pakistan are generally less likely to adopt ‘formal’ PMS practices, including setting goals, monitoring performance and performance evaluation practices.

1.3. Research Objectives:

- To explore the formal PMS practices in SMEs.
- To determine the setting goal mechanism in SMEs.
- To examine the formal performance monitoring and evaluation mechanism in SMEs.
- To identify the PMS post implementation effects on SMEs functionality
- To explore the barriers towards the implementation of PMS in SMEs

1.4. Significance of the Study:

The undeniable urge to conduct this research was stirred while attending 3rd SME conference held on August 8, 2009 at Karachi. The number of presenters unanimously agreed upon the issue that, today’s utmost challenge of Pakistan SME sector is “Effectiveness of Human Resources Functionality”. In this scenario Pakistan SME sector expands its significance for future researchers, consultants, analysts, policy makers and private owners of SMEs.

1.5. Research Methodology:

1.5.1. Research Design:

This research activity has been carried out by applying both qualitative and quantitative research approaches. Data was collected from primary and secondary source. The secondary data consists of by looking different published and online research journals, newspapers, magazines, internet, and reports.

1.5.2. Population:

Due to limited time horizon we have selected Textile sector SMEs located in Karachi. Bhutta et al., (2007), reported that 20,550 firms are operational in ten districts i-e, Karachi, Lahore, Faisalabad, Multan, Hyderabad, Sialkot, Gujrat, Shiekhupura, Gujranwala and Quetta. Whereas, in Karachi total 4,777 SMEs are operational and this number is 23.2% of total number of firms located in ten districts. In addition, according to ten districts sector wise breakup 6,932 (6,932/20,550 * 100 = 33.7%) firms are operational in Textile sector. For our research we have intended to take 12 textile firms located in Karachi district those meet the criteria of SME definition i-e; SMEs are up to 250 employees having up to Rs. 25 Million paid up capital and Rs. 250 Million annual sales. The entire firms would be selected from Chambers Listings, Jamal’s Yellow Pages, Stock Exchange Listings and Textile Directory of Pakistan (Bhutta et al., 2007).

1.5.3. Sample Size:

A total 225 questionnaires were distributed in 12 SMEs and 153 respondents have returned the questionnaire whereas, due to incomplete information 11 questionnaire have been rejected. Hence response rate remained (142/225 * 100 = 63%).
1.5.4. Sampling Technique:
It was decided to use convenience sampling technique by keeping in view that in Karachi, total 4,777 SMEs are operational and it is difficult to cover all of them. Therefore, 12 SMEs from textile sector have been selected that voluntarily offered support in data collection. All those respondents who voluntarily offered their concern are considered as the part of the sample.

1.5.5. Tools for Analysis:
In order to analyze the data quantitatively (SPSS 10.0, E-Views 3.1 and Microsoft Excel) was used. Descriptive Statistics, Correlation and Covariance, and Multiple-Regression Analyses were carried out.

2.0. Literature Review & Theoretical Framework:
2.1. Statistics on Pakistan SME Sector:
The SMEs considered as the engine for economy and in the midst of financial slump and economic downturn SMEs played a critical responsibility in sustained momentum. SMEs have given cushion and lessen the effect of economic meltdown and it is an immense resource for economic endurance for developing countries such as Taiwan, Hong Kong, Singapore, Korea and Philippine. We are looking forward the SME sector for future research since numbers showed in Economic Survey of Pakistan that approximately 3.2 million SMEs are operating in the country and it occupies 77 percent share in industrial employment with value addition share of 28 percent only. SMEs add more than 30 percent to GDP, 24 percent to national manufacturing exports, and account for the employment of more than 21 million people. In addition, 5 or less people are working in 87 percent SMEs and 10 or less people are working in 98 percent SMEs. Bhutta et al. (2007) has given horror picture of the financial performance of SMEs that showed negative trend on Y-o-Y basis and research activity conducted at ten districts pointed out that sale of 71 percent units from total population either to be declined or remained stagnant in coming years. Pakistan is sixth densely populated country and its population reaches to 173.5 millions according to latest survey. The Y-o-Y cumulative GDP growth is 6-8 percent since 2004. Inflation remained at 10-25 percent since 2005 due to this poverty rate is constantly uplifting. International Labor Organization projected that economically active population in Pakistan is projected to increase from 63 million in 2008 to 93 million in 2020. In recent years surge in unemployment is sky rocketing. Slow moving economy, law and order situation and terrorism in the region completely derailed economic activity.

2.2. Categorization of Pakistan SME Sector versus Rest of the World:
In US small-sized business is defined as those with fewer than 100 and medium-sized business often refers to those with fewer than 500 employees while categorization of EU is different for small business with less than 50 employees and for medium business this is fewer than 250 employees. However, in Asia Pacific employees break up is 300 or between (300-500) employees for manufacturing and 20 (20-50) for services. There is strong consensus offered on characterization of Pakistan SME sector and various presenters of 3rd SME Conference hold this view that in Pakistan SMEs are up to 250 employees, up to Rs. 25 paid up capital and up to Rs. 250 Million in Sales (Ehsan Elahi 2009).

2.3. SMEs Adoptability of Performance Management System:
Plethora of work has been embarked on PMS applicability and literature review showed that SME sector of Pakistan lacks efficiency and traditionally employee competence and performance have been measured with financial outputs, customer growth, employee learning and satisfaction (Kaplan, 1996 and Mazzarol 2003) quoted that small business lacks satisfactory mechanism to guarantee the efficient management of human resources and according to the Fraza (1998) rapidly developing SMEs are coping with problem of talent hunting and retaining. Number of researchers also stipulates that SMEs does not have proper system to make certain the proficient management of human resources (Tim Mazzarol, 2003; Rigby and Lawlor 2001 and Fraza, 1998). We believe that PMS acquirement promptly eradicate considerable bottleneck that seems complementary in way of business growth. Huselid (1995) and Arthur (1992) argue that all types and sizes of corporations are being coupled with increases in employee and organizational performance. Moreover Rigby and Lawlor (2001) and Delahaye and Smith (1987) enlighten that rising global and domestic competition particularly in area of employee career growth and advancement and performance management is prerequisite. SME sector of Pakistan lacks employee competitiveness and post knowledge economy organizational setup necessitates appropriate system for employee talent exploitation and performance feedback mechanism. Beside this fact that globalization creates opportunities for SMEs it also generates plentiful challenges and threats to
become active players in the global market. It is observed that SMEs in Pakistan are still pursuing the traditional dichotomy and we thought that performance management system designed for increase employees’ performance and organizational productivity.

2.4. PMS Foundation – Theoretical Ground:
Kandula (2007) theorize that,” The fundamental structure of performance management is drawn from basic principles of well-established motivational theories”. In other words we precisely conclude that PMS is an output of motivational and learning theoretical framework and according to Kandula (2007) without complete understanding to the motivational and learning theories no performance management system could ever be successful.

2.5. PMS as a Tool for Employee Goal Setting:
Vance (2006) emphasized that an effective PMS should play strategic role and it aligns individual and team goal with the organization’s goals and an efficient PMS should support single employee and group of employees with organization’s goals. In continuation of Vance (2006) argument Risher, (2003) articulates that the unsurpassed performance management systems are business plans with clear vision and organized strategies designed for managing and organizing work and rewarding top performers. Furthermore, Vance (2006), Huselid (1995) and Arthur (1992) suggested that PMS entails a set of routine, constant human resource actions usually conceded out by managers and supervisors relative to their subordinates in order to increase productivity and maintain employee performance toward the achievement of desired performance objectives.

2.8. PMS as a Tool for Formal Performance Monitoring and Evaluation Mechanism:
It is observed that employee performance and organizational productivity positively be enhanced with implementation of regular performance feedback mechanism, and execution of formal performance appraisal / management system (Vance 2006; Fisher et al., 2003; and Anthony et al., 2002). In addition activities including regular performance feedback, monitoring, and formal performance evaluation system are normally designed for encouraging best possible employee output, motivation, and development. However, formal performance monitoring and evaluation mechanism is a recurring process and may possibly be apply at both individual employees at all employment levels in different locations (EBY et al., 2005; Greenhaus, Callanan, & Godshalk, 2000). Schweiger and Summers (1994) states that, employee evaluation aimed at improved employee future performance and Appelbaum et al (2008b) affirms that PMS is a systematic approach in which employee performance is reviewed in course of time. In addition according to the Bellak (1984); Skenes and Kleiner (2003) assertion three factors i-e; required level of knowledge to do the job, problem solving judgment level and allocated responsibilities should be considered while evaluating a job.

3.0. Data Analysis and Findings:
3.1.1. PMS Adoptability in SMEs of Karachi:
Figure 3.1 is the graphical representation of PMS adoptability in SMEs of our investigated organizations. Statistics of twelve textile SMEs (small and medium enterprises) reveal that large number of employees do not have a clear understanding of what PMS performance reviews aim to achieve. Similarly, 66% respondents reported that appraisals do not focus on achieving organizational goals whereas, 64% have been refuted from its use in any type of employee career planning. In contrast only 10% employees are engaged in setting their own goals and 51% did not agree. As for as, performance monitoring and evaluation mechanism is concerned only 9% respondents thought that it exists while 58% denied. It is also evident that only 6% employees are getting performance feedback from managers and supervisors. It is also exposed that pay and performance in most of the SMEs are not closely connected and 64% respondent has given contradictory answers and 64% consider that managers and supervisors need extensive training to ensure appraisal work in place.

3.1.2. Employee Perception about PMS:
Survey results of eight textile SMEs concerning employee perception and their experience about performance management system discovered that 68% employees believe that overall PMS performance reviews are a useful initiative. However, only 36% employees perceived that performance reviews have caused great deal of fear among employees whereas, 31% thought that PMS performance reviews are used to intimidate and control employees. Similarly, 63% respondents of the view that PMS performance reviews are an effective way to evaluate the performance of individuals.

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3.2. Reliability Analysis:

3.2.1. Overall Reliability - Scale Cronbach Alpha:
The overall reliability analysis was measured by using SPSS 10.0. The calculated Cronbach Alpha value .9703 for 142 numbers of cases and for 5 numbers of items imply that existing questions already in use are the reliable measurement scales for examining the performance management system in SMEs.

3.2.2. Reliability Analysis - Scale Split-Half:
An alternative way of computing the reliability is Split-Half scale via the Spearman-Brown and Guttman Split-half coefficient. In this method some of scale are divided into two halves and for perfectly reliable scale two halves must be perfectly correlated i-e; $r = 1$. Split half reliability values (i-e; .92 and .96) are greater than .85 exposed that scale used for survey is highly reliable.

3.3. Quantitative Analysis
3.3.1. Descriptive Statistics:
Table 3.5 is output of SPSS 10.0 that shows the basic features of the variables used in a study in form of Mean, Median, Standard Deviation, Skewness and Kurtosis. It is exposed that performance monitoring has maximum mean value i.e.; 4.29 whilst 3.90 is the minimum mean value of setting individual goals on a Likert Scale 1-5 (i.e.; strongly agree, agree, neutral, disagree and strongly disagree). Consequently maximum mean value implies that textile SMEs has implemented performance monitoring and employees perceived it in the organization and in contrast minimum mean value can be interpreted as employees does not involve in goal setting. The estimated standard deviation values show the dispersion from mean value of the variables. The lowest value of SD = 1.19 have highest mean value i.e.; 4.29 and for highest SD = 1.41 contains lowest mean value i.e.; 3.90. The detailed SD value of each parameter encompasses that which of the outlier greatly inflates the range. Fig 3.3 shows the Histogram and Normal Curve Distribution. We have observed that the distribution is concentrated on the right side and for this data set distribution is said to be negatively skewed or left-skewed. The data set does not have normal distribution it is observed that data set is showing high value of kurtosis tends to have a discrete peak near the mean and it declines quite rapidly, and has profound tails.

3.3.2. Correlation Matrix
A table 3.6 shows the correlation between five variables in order to describe the degree of relationship between variables. The E-views 3.1 output suggests that at 1% significance level highest correlation is found between performance evaluation and performance monitoring. In contrast PMS adoptability is found least correlated with other variables.
3.4. Multiple Regression Analysis:

The generated regression equation (as shown in Table 3.7a) i.e.; 
\[ Y_5 = 1.638 + 1.152Y_1 + 0.456Y_2 - 0.802Y_3 - 0.022Y_4 \]
by taking PMS Adoptability as Dependent Variable shows that, at 95% confidence interval 
\[ Y_1 = \text{Setting Individual Goal has the largest coefficient value (i.e; 1.152) contributes more to PMS Adoptability as Dependent Variable.} \]

The generated regression equation (as shown in Table 3.8a) i.e.; 
\[ Y_1 = -0.676 + 0.349Y_2 + 0.149Y_3 + 0.249Y_4 + 0.0282Y_5 \]
by taking Setting Individual Goals as Dependent Variable shows that, at 95% confidence interval 
\[ Y_2 = \text{Setting Organizational Goal has the largest coefficient value (i.e; 0.349) contributes more to Setting Individual Goals as Dependent Variable.} \]

The generated regression equation (as shown in Table 3.9a) i.e.; 
\[ Y_2 = -0.197 + 0.112Y_1 + 0.329Y_3 + 0.535Y_4 + 0.0365 \]
by taking Setting Organizational Goals as Dependent Variable shows that, at 95% confidence interval 
\[ Y_4 = \text{Performance Evaluation has the largest coefficient value (i.e; 0.535) contributes more to Setting Organizational Goals as Dependent Variable.} \]

The generated regression equation (as shown in Table 3.10a) i.e.; 
\[ Y_3 = 0.716 + 0.11Y_1 + 0.751Y_2 + 0.229Y_4 - 0.145Y_5 \]
by taking Performance Monitoring as a Dependent Variable shows that, at 95% confidence interval 
\[ Y_2 = \text{Setting Organizational Goals has the largest coefficient value (i.e; 0.751) contributes more to Performance Monitoring as Dependent Variable.} \]

The generated regression equation i.e.; 
\[ Y_4 = 0.06767 + 0.112Y_1 + 0.745Y_2 + 0.139 - 0.002Y_5 \]
by taking Performance Evaluation as Dependent Variable shows that at 95% confidence interval 
\[ Y_2 = \text{Setting Organizational Goal has the largest coefficient value (i.e; 0.745) contributes more to Performance Evaluation as Dependent Variable.} \]

4.0. Conclusion & Recommendation:

1. Through qualitative data analysis it is concluded that Pakistani SMEs have not formulate ‘formal’ HR policy and human resource departments usually pursue traditional means of basic HR functions such as employee recruitment, training and compensation. However, from statistical results of textile sector small and medium enterprises exposed that employees do not have a clear understanding of what performance management system aim to achieve. Similarly big number of employees consider that performance appraisal is not aligned with organizational goals it has no functionality in employee career planning or progression. In contrast, we also came to know that employees are eager to have PMS in their respective organizations and they thought that it would be a positive initiative.

2. Furthermore, neither managers used to provide performance feedback regularly nor employees are used to participate into the performance evaluation.

3. Minimum mean value implies that textile sector SMEs has implemented performance monitoring system and managers give performance feedback regularly. Whereas, from minimum mean value we found that neither population involved in setting own goals nor job goals are to be fixed in the beginning of the year.

4. The variable setting individual goals has shown the immense dispersion from mean value while performance monitoring has low dispersion.

5. It is observed that the distribution is concentrated on the right side and this particular distribution is said to be negatively skewed or left-skewed. In addition, data set is showing high kurtosis tends to have a discrete peak near the mean and it declines quite rapidly, and has profound tails.

6. At 1% significance level highest correlation is found between performance evaluation and performance monitoring. In contrast PMS adoptability is found least correlated with other variables.

7. Multiple Regression Analysis by taking PMS Adoptability, Setting Individual Goals, Setting Organizational Goals, Performance Monitoring and Performance Evaluation as Dependent Variable revealed that,
Setting Individual Goal has the largest coefficient value contributes more to PMS Adoptability
Setting Organizational Goal has the largest coefficient value contributes more to Setting Individual Goals
Performance Evaluation has the largest coefficient value contributes more to Setting Organizational Goals
Setting Organizational Goals has the largest coefficient value contributes more to Performance Monitoring.
Setting Organizational Goal has the largest coefficient value contributes more to Performance Evaluation as Dependent Variable

The survey finding on our tested parameters further reveals that,
- The SMEs does not have ‘formal’ HR policy
- The SMEs does not have ‘formal’ performance management system
- At present there is no planned organizational and individual goal setting practice
- There is no ‘formal’ performance monitoring and evaluation mechanism subsists.
- Career progression and salary rise is not performance based
- Training should be given to managers to design and execute appraisal process
- Managers are not trained to apply appraisal process

We have following recommendations based on our survey results in order to strengthening the SME sector from human resources development point of view;
- ‘Formal’ HR policy should be formulated for human resource development
- ‘Formal’ performance management system should be design and implemented
- Employees should be participate in goal setting process
- Pay raises, promotions, etc should be closely tied to performance appraisal
- ‘Formal’ performance monitoring and evaluation mechanism in SMEs should be applied
- Employees should be motivated to provide input to the performance evaluation process
- Performance data should be used in career planning
- Training should be given to managers to design and execute appraisal process
- Awareness should be created to SME owners to formulate their own HR policy and to adopt prevailing HR principals through conferences, seminars and workshops.
- There is need to encourage HR practitioners and policy makers to participate in SMEs human resource development process
- SMEDA and Chambers of commerce should play its role in creation of HR policies for employee development.
- Government should provide support SMEs to promote their HR effectiveness and efficiency

5.0. Area of Further Research:
During research, it has been observed that there is more than enough vacuum present for future researchers and Pakistani SME sector requires further scholarly contributions that will look at the effectiveness of SME policy towards human resource development. However, in the context of Pakistan SME sector, significance for future research seem to be growing and as for as our research is concerned we are inviting researchers for replication. Since our used variables can be reproduced and replicate in other small and medium enterprises located in different cities.

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