

Leadership and Organisational Performance: An Investigating of SMEs in Malaysia

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Abstract: Leadership is one of the essential elements within organisation. Even though much effort has been attributed to investigate many issues related to leadership, the results are mixed and inconclusive. Also, in Malaysia, debate is still going to identify the form of leadership that best suited with Malaysian leaders. Due to this, this research attempts to explore the impact of transformational and transactional leadership behaviours on organisational performance of SMEs in Malaysia. These leadership behaviours are selected due to its being the most current and widely form of leadership behaviours. SMEs are chosen as target population because its significant contribution to Malaysia's economic well-being. Quantitative and qualitative data are used to answer research questions. Empirical data is analysed by using Structural Equation Modelling. Qualitative data was collected through unstructured interviews. This study found that leaders of SMEs in Malaysia demonstrate behaviours that exemplify both transformational and transactional leadership. Empirically, transformational leadership was found to have a significant relationship with growth and profitability and these relationships were stronger than those found with transactional leadership. The originality of this paper lies in it being the first to examine the leadership behaviours of Malaysian SMEs from a quantitative and qualitative perspective.

Key words: Transformational leadership • Transactional leadership Organisational performance • SMEs • Malaysia

INTRODUCTION

SMEs contribute significantly to the growth and development of the economy in Malaysia. As reported, about 99% of total business establishments in Malaysia is under the category of SMEs. They represent up to 31% of country's Gross Domestic Product (GDP). 56% of total employment in the country is provided by this sector and it contributes 19% to the total exports [1]. The numbers facilitate infrastructural development, growth and economic acceleration for developing prosperous Malaysia [2]. Even though substantial amount of funds are always offered and granted by the government, the

contributions from this sector within Malaysian economy are still below to other lower as compared to other developed or developing countries with regard to the GDP and exports [1].

Practitioners, researchers, educators and policy-makers are having huge interest with the topic of performance of small and medium sized enterprises (SMEs). The characteristics and determinants of performance of SMEs have been and will always be a focus of debate [3]. Due to the unique constraints and limitations faced by SME's (such as having a limited number of employees, insufficient financial resources, lack of educational background and experience, lack

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of managerial expertise, among many others), efforts are continuously being made to understand how the performance of SMEs could be developed and further enhanced. These efforts are important since this sector of economy has been recognised as one of the important engines of growth for a country's economy [4,5].

There is still a lack of understanding about leadership in small businesses [6]. However, to stimulate change in the economy, the importance of entrepreneurship is recognised [7]. The literature also suggests that very little effort has been made to examine leaders and the leadership behaviours adopted in SMEs [8]. Thus, the approach that has been the focus of this paper is to examine the impact on performance of SMEs in Malaysia of the behaviours of leaders, through the collection of quantitative and qualitative data. Effective displays of leadership by leaders of organisation provide a sound strategic direction and encourage motivation amongst members [9]. This is needed to improve and sustain organisational performance and will allow entrepreneurs, who are the owners and managers of SME's in Malaysia, to better equip themselves to be more competitive in the future.

The purpose of the current study is to examine the impact of transformational leadership and transactional leadership on organisational performance. It is acknowledged that there are many efforts attributed to study transformational and transactional leadership, however a much integrated effort is needed to study the impact of such leadership behaviours on the performance of a more generalised population. Besides, a recent literature review shows that very little effort has been made to examine leaders in relation to the leadership behaviour adopted in SMEs [8,9]. Specifically, the following research questions are going to be addressed. 1) To what extent does transformational and transactional leadership have an impact on organisational performance of SMEs? 2) Does transformational leadership have a stronger effect on organisational performance than transactional leadership?

Practically, the outcomes of this study will benefit government related agencies like SME Corporation Malaysia. The results may identify whether certain forms of leadership behaviour are resources and capabilities needed by organisation to ensure sustainable performance [10,11]. Thus, a more robust and specific training program could be initiated by SME Corporation

Malaysia to foster and develop the right leadership attributes among entrepreneurs who are owners and managers of SME's.

Literature Review: Every organisation needs sound and effective leadership. Recognizing its importance, organisations are starting to focus on developing effective leaders within their organisations [9]. Many previous studies on leadership emphasised on its effects towards satisfaction [12,13] or follower's individual performance [13] rather than firm performance. But, [14] argued that, the most important effects of leadership behaviours are towards organisational performance [15,16].

The importance of leadership also has received interests among researchers in entrepreneurship field. Several researchers [17,18] have recognised leadership as important and valuable organisational resource. The success of new ventures are being associated with the practice of effective leadership. There were others who suggest that lack of and poor leadership among common factors of failures of small businesses [19,20].

Transformational Leadership: A transactional leader "pursues a cost-benefit economic exchange to meet subordinates' current material and psychic needs in return for "contracted" services rendered by the subordinate" [21]. Leaders who are transactional will give direction and motivate employees through goals setting and clarifying task requirements [22]. Put simply, it is an agreed reciprocal process between a leader and followers in order to achieve goals of organisation. Most transactional leaders are found to be risk averse and perform well in a stable and predictable condition [23].

Different from transactional leadership, transformational leadership is characterized by a person's ability to engage and create a connection between themselves and their staff. A leader raises the level of motivation of followers and brings about significant change in the organisation [24,25]. This type of leader is "attentive to the needs and motives of followers and tries to help followers reach their full potential" [25]. Transformational leadership involves leaders generate awareness and acceptance of the purpose and mission of the organisation and help their employees to look beyond their own self-interest for the benefit of the group [21,23].

“Transformational leaders have the ability to lead changes in an organisation’s vision, strategy and culture as well as promote innovation in product and technologies” [25]. For the purpose of this research, transactional and transformational leadership theory will be used as the framework through which leadership will be studied, since these leadership approaches are the most commonly used by researchers interested in comparing the approaches adopted by leaders [26].

Key Dimensions of Transformational Leadership:

There are four dimensions of transformational leadership. These are idealized influence, inspirational motivation, intellectual stimulation and individualized consideration. In terms of *idealised influence*, the leader provides vision and sense of mission, instils pride and develops respect and trust among employees [23,27]. *Inspirational leaders* communicate high expectations and use symbols to focus effort and convey important purposes to employees in simple ways, about what needs to be done [12,23,28]. *Intellectual stimulation* involves leaders encouraging intelligence, rationality and careful problem solving [23,27]. The *Individualised consideration* aspect of transformational leadership means leaders provide personal attention and treat each employee individually [23,27].

Key Dimensions of Transactional Leadership: There are three dimensions of transactional leadership. These are contingent reward, management-by-exception (active) and management-by-exception (passive). Contingent reward refers to leaders providing followers with rewards for effort. Leaders promise rewards for excellent performance, acknowledge accomplishments and punish poor performance [23,12]. In the management-by-exception (active) mode, leaders act as monitors and search and watch for deviations from rules and standards and take corrective actions [23,12]. In the management-by-exception (passive) mode, leaders only intervene when procedures are not followed and standards are not met [23,12].

Organisational Performance: Organizational performance is one of the most important dependent variables for most management research [29]. [30] confirm that growth, profitability and efficiency are the most commonly form of performance measures used in the entrepreneurship literature.

Transformational Leadership, Transactional Leadership and Organisational Performance:

To date, there have been many efforts undertaken by scholars and researchers to acknowledge and assess the relationship between transformational and various organisational performance measures. Many evidences suggest that these two are correlated positively [31]. Others have identified that transformational leadership is correlated with innovation [32], supervisory assessments of managerial performance [33] and effectiveness [12,34].

Regarding transactional leadership, [14] has initiated a study to investigate the impact of leadership on organisational performance and found that Russian managers who practiced transactional leadership behaviour have positive impacts on organisational performance as well as innovation. In a military setting which is characterised as organisation operating in an unstable environment, [35] concluded that platoon leaders who demonstrated transactional leadership characteristics increase the performance of the platoon members. [36] also reported a positive relationship between transactional leadership and business performance of SMEs in Taiwan.

Generally, in examining the effects of transformational and transactional leadership on measures of organisational performance, most of the findings reported that transformational leadership is more effective than transactional leadership [37,38]. [14] found that transformational leadership directly and positively impacted organisational performance of Russian companies above and beyond the impact of transactional leadership. [39] also suggest that transformational leadership has a stronger positive relationship with followers’ psychological empowerment and organizational identification than transactional leadership. But recently, a study by [40] suggested the opposite. Their results of small-scale organisations in Nigeria indicated that performance is highly positively affected by transactional leadership behaviour, but insignificantly affected by transformational leadership behaviour of leaders.

Due to mixed results from literature described above, three hypotheses were proposed:

- H1: Transformational leadership has significant and positive relationship to organisational performance.
- H2: Transactional leadership has significant and positive relationship to organisational performance.

H3: Transformational leadership has greater impact on organisational performance than transactional leadership has.

due to their expertise and knowledge with regards to their own establishments and understanding of the direction of the organisation.

MATERIALS AND METHODS

This study employed a combination of quantitative and qualitative approaches to data collections and analyses. Quantitative data is collected to test the proposed hypotheses of this study. Qualitative data is collected to confirm and to expand on the understanding obtained from the quantitative findings. To test research hypotheses, data were gathered from 395 Malaysian-owned SMEs operating in the manufacturing and services industry. To test and verify research hypotheses, structural equation modelling (SEM) was used. There were two approaches to the recruitment strategy. First, a list of enterprises was obtained from the SME Corporation Malaysia. From this list, 1000 firms were selected in equal proportion from manufacturing and services industries. These two industries were chosen because they are the main industries that contribute significantly to the development of economy in Malaysia [1]. The second approach involved distributing 700 questionnaires through several agencies (eg. SME Corp. Malaysia and Malaysian Institute of Management) that provide and conduct specific training and seminars for entrepreneurs in Malaysia. The response rate generated was 23%.

The instruments for leadership behaviours were adopted from the Multifactor Leadership Questionnaire (MLQ) by [41]. [42] have tested its validity. The instrument was measured on five-point Likert scales that ranged from 0=*Not at all* to 4=*Frequently, if not Always*. Growth and profitability were used to represent organisational performance in this study. The instruments of these dimensions were adopted from [32] To standardize the scaling format of the research instruments, all items for organisational performance were also measured on five-point Likert scales ranged from 0=*Strongly Disagree* to 4=*Strongly Agree*.

Of the 395 surveys returned, 42 respondents agreed to participate in an interview. However, only nine interviews were conducted to confirm and further explore findings from quantitative data. The semi-structured interviews were employed since it involves an in-depth examination of the respondents and the topics [43]. The owner or the top level managers are chosen as subjects

RESULTS AND DISCUSSIONS

Cronbach's alpha coefficients for leadership behaviours earned a high coefficient of 0.860. At the dimension level, the values for Cronbach's alpha for transformational and transactional leadership were 0.87 and 0.61 respectively. Cronbach's alpha coefficient for organisational performance was 0.80. All variables achieved 0.70 or above indicating an acceptable statistic testing level [44] except for transactional leadership dimension. [45,46] also suggested that a value of above 0.6 is still an acceptable value for internal consistency.

Demographic of Participants: For the quantitative survey, the total number of respondents retained for the remaining analysis was 395 (N = 395). 206 respondents were from the manufacturing industry, representing 52.2% while the remaining 189 respondents came from the service industry, representing 47.8% of the sample. 45.8% of the respondents (n = 181) were the owners of the firms and the remaining 54.2% were the top managers (n = 214). The majority of the respondents were relatively young, aged between 31 and 40, representing 44.8% (n = 177). In terms of gender, there were 247 male respondents, representing 62.5% while the 148 female respondents represented 37.5%. Most of the respondents had at least a Degree (Bachelor), representing 45.6% (n = 180). The majority of the respondents (52.7%; n = 208) employed between five and 19 employees; 105 respondents (26.6%) employed between 20 and 50 employees; 53 respondents (13.4%) employed between 51 and 150 employees; 24 respondents (6.1%) employed fewer than five employees; and only five respondents (1.3%) employed more than 150 employees.

Leadership Behaviours: Referring to Table 1, the mean score for total leadership behaviours was 2.69 (SD=.39). Between the two form of leadership behaviours, transformational leadership scored higher mean at 2.90 (SD =.47), than the mean score for transactional leadership 2.33 (SD =.37). This results exemplify that the respondents in this study perceived that they practiced and displayed transformational leadership behaviours more frequently than transactional leadership behaviours.

Table 1: Means and Standard Deviation for Leadership Behaviours (N=395)

Measures	Mean	SD
Transformational Leadership	2.90	.47
Idealised influence	2.90	.51
Individualised Consideration	2.73	.58
Intellectual Stimulation	2.84	.64
Inspirational Motivation	3.13	.57
Transactional Leadership	2.33	.37
Contingent Reward	2.94	.57
Management-by-exception (Active)	2.78	.56
Management-by-exception (Passive)	1.26	.73
Total Leadership Behaviours	2.69	.39

Table 2: Themes for Transformational Leadership

Themes	Codes	Respondents									# of resp
		1	2	3	4	5	6	7	8	9	
Idealised Influence	inspire employees	x	x		x		x	x	x	x	8
	have respect on me		x					X			
	stress on trust					x		X			
Individualised Consideration	coaching	x	x	x		x		x		5	
	one-on-one			x							
Inspirational Motivation	motivating employees		x		X	x	X	x		8	
	employees willing to put more effort		x								
	provide direction			x	x		X	x	x		
Intellectual Stimulation	encourage intelligence	x	x							3	
	instil critical thinking						X				

Table 3: Themes for Transactional Leadership

Themes	Codes	Respondents									# of res
		1	2	3	4	5	6	7	8	9	
Contingent Reward	acknowledged accomplishment	x	x	x							4
	punishment for poor performance								x		
Mgmt-by-Exception (Active)	close monitoring		x		x		x		x	5	
	take corrective actions						x	x			
Mgmt-by-Exception (Passive)	interfere only when needed				x	x				2	

The outcomes of the quantitative study indicate that leaders of SMEs in Malaysia perceived themselves to be more transformational than transactional. The results from the interviews also showed support when majority respondents referred more often to transformational rather than transactional leadership attributes. Table 2 and Table 3 indicates the frequency of themes and codes used for leadership behaviours that appeared after the analysis of data from the interview.

Goodness-of-fit Statistics, Construct Reliability and Validity: The outcomes of the final measurement models for each of the variables were derived from the Exploratory Factor Analysis (EFA) and Confirmatory Factor Analysis (CFA). The final results produced were much improved than their initial measurement models. The comparisons are summarised in Table 2. Construct reliability and validity were then examined. The results are presented in Table 3.

Results from Table 2 indicated that the final measurement models for each of the variables derived from the EFA and CFA processes produced much better results than their initial measurement models. Results from Table 3 demonstrated that all values for construct reliability were above the threshold value of 0.6 as recommended by Bagozzi and Yi [47]. Data also demonstrated convergent and discriminant validity. Convergence validity is defined when the AVE value for each factor is greater than 0.4 [47]. Discriminant validity is defined when the AVE for each factor is greater than the average shared squared variance (ASV) [46].

Table 4: Goodness-of-fit Comparison between Initial and Final Measurement Models

	RMSEA	GFI	CFI	AGFI
Transformational Leadership	0.071 (0.092)	0.976 (0.837)	0.958 (0.782)	0.934 (0.917)
Transactional Leadership	0.080 (0.075)	0.963 (0.952)	0.910 (0.880)	0.917 (0.917)
EO	0.053 (0.095)	0.991 (0.920)	0.981 (0.791)	0.957 (0.871)
OP	0.082 (0.154)	0.992 (0.896)	0.984 (0.796)	0.943 (0.804)

Note: Numbers in parentheses were fit statistics from initial measurement models

Leadership Behaviours and Organisational Performance: To examine the relationship between leadership behaviours and organisational performance and to answer the hypotheses proposed in this study, the following path model was developed. The final path model (Figure 1) between leadership-organisational performance

Table 5: Construct Reliability and Validity

Construct	Factors	Construct Reliability	Average Variance Extracted	Average Shared Variance
Transformational Leadership	Idealised Influence	0.65	0.48	0.17
	Intellectual Stimulation	0.69	0.43	0.30
	Inspirational Motivation	0.68	0.42	0.35
Transactional Leadership	Contingent Reward	0.66	0.40	0.16
	Management-by-exception (active)	0.73	0.51	0.10
	Management-by-exception (passive)	0.74	0.49	0.07
Organisational Performance	Growth	0.69	0.54	0.52
	Profitability	0.66	0.40	0.52

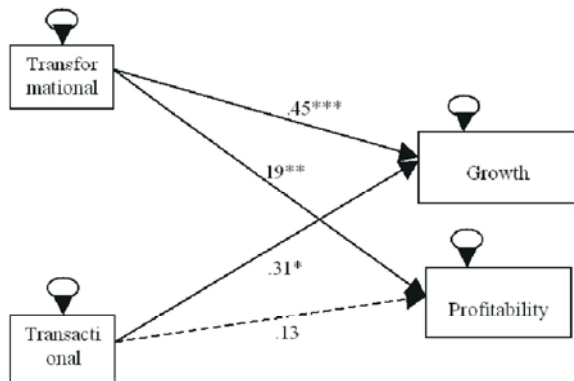


Fig. 1: Path Analysis of Direct Model between Leadership and Organisational Performance

Note: Dashed arrow denotes nonsignificant relationship

* $p < .05$. ** $p < .01$. *** $p < .001$

Goodness of fit statistics: GFI=.905, AGFI=.855, RMSEA=.091, CMIN=4.288

relationships fits the data well and majority of the indices have achieved satisfactory level of goodness-of-fit statistics. The fit indices of the model are as follows: $\chi^2=338.741$, $df=79$, $\chi^2/df=4.288$, RMSEA=.091, GFI=.905, AGFI=.855.

Based on the results shown in Figure 1, transformational leadership has a significantly positive relationship towards growth ($\beta=.45$, $p=.000$) and also profitability ($\beta=.19$, $p < .01$) and thus H1 is supported.

On the other hand, transactional leadership only has a significantly positive relationship towards growth ($\beta=.31$, $p < .05$). The path between transactional and profitability is positive but not significant ($\beta=.13$, $p > .05$). Therefore, H2 is only partially supported.

Also, the results presented conclude that transformational leadership has a greater impact on the performance of SMEs than transactional leadership has. Higher path coefficients are found between transformational leadership than the path coefficients

between transactional leadership towards growth and profitability performance of SMEs. Hence H3 is supported.

Based on responses and remarks from interview data, it can be determined that leadership behaviours described by them are similar to what is described in the literature as transformational and transactional leadership [27,28]. To summarise, the outcomes of the quantitative study indicated that leaders of SMEs in Malaysia are prone to be more transformational than transactional. Interviews conducted also revealed that most of the respondents referred more often to transformational rather than transactional leadership attributes.

DISCUSSION

Based on the means distribution between the two types of leadership behaviours and their respective attributes, transformational leadership is reported to have higher means ($M=2.90$) as compared to transactional leadership ($M=2.33$). These findings were quite similar to what had been found in a study by Avolio & Bass [41]. They found that the mean for transformational leadership ($M = 2.85$) was higher than the mean for transactional leadership ($M = 2.27$). The results of the study being reported here indicate that leaders of SMEs in Malaysia perceive themselves practicing the behaviours and attributes of transformational leadership. On the other hand, they believe that they only sometimes display the behaviours and attributes of transactional leadership. It shows that when it comes to leadership, leaders of SMEs in Malaysia perceived themselves to be more transformational (as compared to transactional) leaders. It is seemed that leaders of SMEs in Malaysia like to consider themselves to be transformational when they are dealing with organisational problems or issue with employees. They believe that to lead the organisation, they do not necessarily have to focus on finding mistakes of employees or providing contingent reward and

exercising punishment for poor performance. They see themselves, rather as someone who focuses on developing trust among employees in order to earn more respect from them, providing assistance in dealing with old problems or issues, giving more individual attention and communicating high expectation. These are the attributes of transformational leaders.

At the factor level of transformational leadership, an interesting finding was observed. Compared to the western countries, this study established that inspirational motivation has the highest mean of the four transformational leadership attributes at $M = 3.13$, followed by idealised influence, intellectual stimulation and individualised consideration, respectively. Much Western research i.e. [48] has found that idealised or charismatic influence is considered to be the key element of transformational leadership. But in the context of SMEs in Malaysia, inspirational motivation is perceived to be the key attribute of transformational leadership. [49] also reported a similar finding in another non-Western context study in Iran. Based on data gathered from personnel in private manufacturing companies in Qom, successful companies scored the highest mean for inspirational motivation, followed by idealised influence, intellectual stimulation and individualised consideration.

This evidence of inspirational motivation having the highest mean of all the attributes of transformational leadership suggests that leaders of SMEs in Malaysia believe that, in steering the organisation to success, communicating high expectations to employees and using the simplest way to convey purposes to employees are the most important qualities of a leader. They believe that creating trust for mutual respect comes second. They also believe that encouraging critical thinking by their employees is more important than providing individual attention to employees. Perhaps it is due to the size of their organisation (which in this study consisted of more small than medium-sized organisations) that the attribute of inspirational motivation is considered to be important for ensuring good organisational performance. Leaders are expected to understand how to communicate high expectations and to show how to achieve good outcomes. Several respondents admitted that because of having employees with minimum or no qualifications, they need to be motivational leaders. They believe that leaders who can do this will motivate employees to perform beyond what is normally expected from them.

On a different note, the low mean score of individualised consideration indicates that leaders of SMEs in Malaysia need to practise more of this

behaviour. Transformational leadership is concerned with developing employees' capabilities and capacities [49]. Therefore, paying close attention to the different needs of individual employees and spending time in teaching and coaching could develop the skills and capabilities of their employees to enhance organisational performance.

Possibly, Malaysia being characterised as having a collectivist culture influences the perception of leaders in Malaysia of the importance of providing individual attention [5,10,11,16]. A collectivist society, as described by [50], gives priority to group goals over individual goals. In his book *Culture's Consequences*, [50] said that a collectivist society fosters strong relationships where every member of a group takes responsibility for fellow members. Employer–employee relationships are perceived in moral terms (like a family link) and employment and promotion take account of the employee's in-group [50]. This is quite the opposite to the individualist culture of Western countries. The people in an individualist society give primary importance to their own interests and their immediate family.

Therefore, in the context of SMEs in Malaysia, leaders do not see the need to address employees' needs individually. They see their employees as being the entire team and workforce in their organisation. Employee growth and development are addressed in groups to ensure that the goals of the organisation are communicated to all members of the organisation. This might explained the removal of individualised consideration from the final measurement model.

Thus, this study supports the view that that the owners/top managers of SMEs are more transformational than transactional. It means that within the context of SMEs in Malaysia, leaders perceive themselves as acting and displaying more often the behaviours of transformational leadership. They also believe they demonstrate transactional leadership behaviours but to a lesser extent than they practice transformational leadership behaviours.

Limitations and Future Research: There are several limitations with this study. First, it relied upon self-reported data from single respondents. All measures on leadership behaviour and organisational performance were evaluated by either the owners or the top managers of SMEs in Malaysia. The respondents may have exaggerated their evaluation of their leadership behaviour and also their organisational performance. According to a recent review of literature, self-assessment of leadership behaviour tends to be more inflated than other sources

[51]. Thus, the findings must be interpreted in the light of this limitation, even though the Harman's one-factor test showed that common method bias was not an issue in this study. Second, this study adopted subjective measures. [52] argued that the use of subjective performance measures might encourage performance evaluation bias but the results of this study were tested for that bias and there did not seem to be a problem. Third, the cross-sectional design used in this study only provides a snapshot view of the researched phenomena where data on all measures were collected at the same time. Thus, causal inferences could not be drawn from this research. The use of longitudinal data would provide a remedy for this limitation when data on independent variables and dependent variables are measured at two or more points in time. It is also recommended that future research to consider exploring leadership of SME leaders from employees' perspective. A comparative study of effective leadership between the results obtained from the leaders themselves and employees' perception might produce a better understanding of how performance of SMEs could be further improved.

CONCLUSION

More studies need to be done to study leadership and its impact on organisational performance [8]. SMEs' performance in Malaysia could be well improved through an understanding of leadership behaviours of the leaders. Perhaps, by aligning the right leadership behaviours of leaders of SMEs with those known to result in higher organisational performance could further strengthen entrepreneurship development in the country. Thus, it is strongly suggested that leadership does matter to Malaysian SMEs. Success of the firm is attributed to the leadership behaviours of leaders and they should practice more transformational than transactional leadership behaviours.

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