

# Voice of Academia

*Academic Series of Universiti Teknologi MARA Kedah*

**VoA**  
Volume 14 Issue 1  
June 2019



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Academic Series of Universiti Teknologi MARA Kedah

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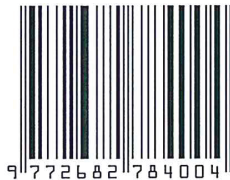
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**e-ISSN: 2682-7840**



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# THE INTERSECTION BETWEEN TRANSFORMATIONAL LEADERSHIP AND EMPLOYEE RETENTION WITHIN SMES IN THE SERVICES SECTOR

Nor Sabrena Norizan<sup>1</sup>, Ramlee Abdul Rahman<sup>2</sup>, Irzan Ismail<sup>3</sup>

Faculty of Business and Management

<sup>1</sup> Universiti Teknologi MARA, Kampus Alor Gajah, Cawangan Melaka, Malaysia

<sup>2</sup> Universiti Teknologi MARA Cawangan Puncak Alam, Malaysia

<sup>3</sup> Universiti Teknologi MARA Cawangan Melaka, Malaysia

## ARTICLE INFO

### Article history:

Received Oktober 2018

Received in revised form

Accepted December 2018

Published June 2019

### Keywords:

Transformational Leadership,  
Employee Retention, SMEs

Corresponding Author:

[norsabrena@uitm.edu.my](mailto:norsabrena@uitm.edu.my)

## ABSTRACT

Many employees leave organization because of the leader. Thus, this study focuses on the intersection between transformational leadership and employee retention within SMEs in the services sector. SMEs in services sector located in Peninsular Malaysia has been chosen as the population due to its largest contribution to Malaysia economic growth. Transformational leadership styles are found to be the determinants of employee's retention success and survival in every organization. Based on the previous study, the determinants of transformational leadership are found to be the factors that significantly influence on employees intention to stay. Analyzing transformational leadership styles on employee retention will give greater understanding on the employee shortage and thus helping the organization to develop potential initiatives to overcome the retention problems in SMEs. Therefore, this study intends to find out the influence of transformational leadership on employee retention within employees who works in SMEs within the services sector. From the past literature, it is found that transformational leadership significantly influences employee retention. Hence, it is hoped that, from the perspective of Malaysia SMEs, the result of this study can embrace transformational leadership as a factor that can help to enhance staff retention in the organization.

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## 1. Introduction

Human capital provides a competitive advantage to the success and survival of most organizations. Employees of a business provide the application of skills and expertise and never been more important that it is today (Sourov, 2019). Human capital is very important because the knowledge that each employee's earn is difficult to find, imitate and replace by the technology (Barney, 1991). However, human capital is at a huge risk for most organizations because it literally leaves the organization every day when the employees go home. Employees are churning through companies at an alarmingly rate; voluntarily leaving one company for another, seeking a path to rapid upward mobility.



A survey conducted by Aon (2017), showed that employee turnover in APAC is the highest in Australia at 12.9 percent, followed by ASEAN 5 consist of Philippines, Vietnam, Thailand, Indonesia and Malaysia (12.8 percent), Singapore (12.7 percent), China (12.5 percent), China (12.5 percent) and Hong Kong (11.8 percent). Malaysia is listed amongst the countries that is struggling with the issues of war on talent. Employee retention has been identified as the major concerned in Human Resource topic areas (Debono, 2018). Thus, business leaders need to take an urgent action to ensure a secure employment relationship is developed before it is gone.

Investing in employees, making them feel important and supporting their career journey are the best investments a business can make. It is found that an increase in employee turnover and employee attrition can cost money to the organization and a low retention rate will significantly affect employee engagement and turnover cost (McDougall, 2018). Thus, a leader's role is becoming highly important as leadership styles are found to significantly influence employees' decision whether to stay or leave the organization (Wakabi, 2016). There are several leadership styles that have been used by previous researcher to study employee intention to stay within their organization. Nevertheless, in this study, transformational leadership style has been chosen as it is found that this type of leadership is highly associated with individual and organizational performance (Shabane, Schultz and Van Hoek, 2017). Therefore, this study intends to investigate the intersection between transformational leadership and employee retention within SMEs in the services sector.

## **2. Literature Review**

### **2.1 Leadership Styles**

Leaders play a major role in employee retention as it affected employee's job performance and satisfaction (Parzinger, Lemon & McDaniel, 2012). There are many definitions developed in defining leadership, but there is still, no real consensus. Leadership is a relationship that influences one person behavior and action towards other people (Wakabi, 2016). Okumbe (1996) and Arham (2014) term leadership as a process of motivating and helping others to work interdependently with each other in achieving organizational goals. It is found that a leader is the one who can help to shape the employee's attitude, motivation and behaviour, establish rewards and punishments (Chitra, 2013). To meet organizational objectives and retain top talent, leaders need to effectively manage their employees.

Leaders use their influence technique to help employees towards achieving targets and to maximize the outcome in the organization. The influence techniques here does not mean that leaders are controlling or having power towards their followers, but leaders have their own strategy that can affect the follower's action and behavior in making decision. Leadership styles are important for increasing organization performance since leaders play greatest roles in achieving organizational strategic goals and encourage employee's motivation (Hashim, Ahmad and Zakaria, 2012). Good leadership is not only essential in directing organization's success but also for their continuity and survival (Van, 2005; Abdul Aziz, Abdullah, Anas and Mahmood, 2013).

Responsibility and accountability for retaining talent need to move out to the front lines and into the hands of leaders. Leaders and their skills in building climate of retention, a culture that speaks to employee in a way that encourage them to stay, will be an organization's best strategies against job turnover. There are numerous approaches that have been used by other scholars to group

leadership styles. In this study, it is believed that transformational leadership can act as an independent variable that affects employees' decision to stay or not within the organization. With the elements of transformational leadership, it can assist the leaders of the SMEs to better manage and plan the elements of talent management towards ensuring their ability in order to sustain employees to stay in their organization.

## **2.2 Transformational Leadership**

The concept of transformational leadership was coined by James MacGregor Burns in 1978 in his study on political leaders, but lately this area has gained currency in organizational psychology as well (Burns, 1978). Burns (1978) defined transformational leadership as a process whereby leaders and followers work interdependently in increasing their level of morale and motivation. Bass (1985) labels the terms transformational leadership as a process where leaders expand and increase the employee enthusiasm. It exists when leaders develop an awareness and agreement of the organization's purpose and mission of the group and then encourage the employees to look further their self-interest to gain advantage for the group.

Sow, Ntamon, Osouha (2016) conducted a research among healthcare providers in the United States and found that transformational leadership has a positive influence towards employees. Transformational leadership style helps the employees to achieve their personal and professional goals. Determining transformational leadership style and its effect on employee retention amongst SMEs in the services sector will give a better knowledge regarding strategy in overcoming high turnover rates in the SMEs industry.

For the purpose of this study, four elements of transformational leadership (Bass and Avolio, 2004; Bass, Jung, Avolio and Berson (2003) will be used as the independent variables in helping the organization to retain its employee as this element found has a significant impact on employee retention. The four elements of transformational leadership consists of idealized influence, inspirational motivation, intellectual stimulation and individual consideration.

### *i. Idealized Influence*

The leader becomes a role model by having a high ethical behavior, instill pride, gain respect and trust (Bass 1999; Bass and Riggio, 2012). Also known as charismatic attribute, it is the central of transformational leadership process and main element of transformational leadership (Bass 1985; Yukl 1989).

### *ii. Inspirational Motivation*

The leader clearly provides a vision that is interesting and inspiring to the followers. Leaders with inspirational motivation require followers with high standards, communicate optimism about future goals and provide meaning for the task given to them (Bass & Avolio 2004). Therefore, followers need to have a strong collective sense of purpose if they are to be motivated to respond. Purpose and meaning give the follower motivation to move forward. The components of visionary produce by the leader are reinforced by their communication skills that make the vision understandable, specific, powerful and engaging. Moreover, followers are willing to spend more effort in the task given to them, be encouraged and optimistic and believe in their future.

### *iii. Intellectual Simulation*

The leader challenge assumptions, risk taker and seek for followers' opinion. This kind of leader stimulate and encourage creativity among the followers (Judge and Piccolo 2004). The leader provides continuous learning and see the unpredicted situation as opportunities to learn new things. The followers seek for explanation, think critically and find better ways to finish their jobs.

### *iv. Individual Consideration*

The leader is very concern about their followers' needs by acting as a mentor or coach to the followers. They provide empathy and support, listen to followers concern and needs and value individual contribution. The followers have a determination to increase their self-development and gain intrinsic motivation in completing their tasks.

## **2.3 Employee Retention**

A highly competitive environment requires organization in all sectors to retain their critical and talent employees in order to gain and retain competitive advantage (Wakabi, 2016). The issues of employee retention have emerged in 1970s and early 1980s as many people have entered organization and stay for a very long time until retiring. There are numerous terms used in describing the concept of retention such as job leaving, intention to leave and job turnover.

Employee retention can be defined as a set of action in which the employees are expected to be part of organization for a maximum of time or after they have settled the job given (Akila, 2012). This can be explained by Michael (2008) who stated that retention of employee is an effort of the organization in ensuring that employee remain in the organization and minimized the reduce job turnover.

Organizations must carefully match the organizations' need and expectations with employees in order for them to retain key talent. Retention is important because of the opportunity costs and recruitment costs it provides when leaving the organization (Pandita and Ray, 2018). When key employees leave an organization, it will have negative impact on existing employee morale, and also for the organization revenues (Vigoda, 2000).

Therefore, a good leader is needed in order to shape the employee's attitudes, motivations and behaviors (Chitra, 2013). Leaders are the important determinants in retaining key potential employees. A weak relationship between leader and employee may the reason for employees leave the organization. A study conducted by Shukla and Sinha (2013) stated that happy employees will make them want to stay for a long time with the organization especially when they have a strong bonding with their leader.

## **2.4 Empirical Review of Transformational Leadership and Employee Retention**

There are increasing numbers of literature focusing on the relationship between transformational leadership and employee retention. Transformational leadership has been stated in the leadership literature to be one of the leadership styles that relates to employee retention. As in previous studies of Alexendrov, Babakus and Yavas (2007) emphasized that, each element of effective transformational leadership style practice by business leaders has a significant influence on

employee retention. Similar results are found in the quantitative study by Hamstra, Yperen, Wisse and Sassenberg (2011) contending that leaders whose controlling, motivating and directing their followers will help to mitigate follower's intention to leave the organization.

### 3. Propositions

Based on the literature, the following propositions are proposed:

- P1** There is a relationship between idealized influence and employee retention
- P2** There is a relationship between inspirational motivation and employee retention
- P3** There is a relationship between intellectual stimulation and employee retention
- P4** There is a relationship between individual consideration and employee retention

### 4. Methodology

This study is designed to investigate the intersection between transformational leadership and employee retention within SMEs in the services sector. The study is a hypothesis testing study, which there will be four hypotheses as proposed above. The correlational study will be done in testing the relationship between variables to see whether a change in one variable may affect the other variable. To meet the research objectives, quantitative approach will be adopted. Quantitative approach will be used to test the proposed hypothesis and to answer the research questions. Before starting to collect quantitative data, past literatures will be gathered regarding the areas of transformational leadership and employee retention. The literature will be related to the formulation of conceptual model, research objectives, research questions and proposed hypotheses. Before the actual data can be collected, a pilot test will be conducted to ensure the clarity and accuracy of the translated questionnaire and to obtain feedback on its format, design, clarity and understanding the ease and time for completion. During the actual data collection, primary data will be collected through the distribution of survey questionnaire to the selected sampling frames. The population of this study will be employees working in the services sector at SMEs located in Peninsular Malaysia. SMEs in Peninsular Malaysia have been selected due to the high percentage of SMEs establishment in Peninsular Malaysia. In the services sector, the focus will be in wholesale and retail trade, food and beverage and accommodation subsector as the value added driven by these subsectors. In this study, probability sampling will be used as a sampling technique. Table of random number will be used in selecting each member of the sample. Moreover, a set of structured questionnaires will be used to collect the data. To measure transformational leadership as independent variables, the Global Transformational Leadership Scale will be used (Carless, Wearing and Mann, 2000). A six-point Likert scale ranging from disagree to strongly agree will be used as the instrument to measure leadership behaviour. Employee retention will be measured by using a model developed by Mobley (1982). This model will be having 3-item measure using a five-point Likert scale. The hypothesis testing will be conducted by using PLS-SEM. It will be testing through the calculation of P value for each path coefficient.

### 5. Expected Result

It is hoped by conducting this study, it can help the leaders of SMEs to better understand the influence of transformational leadership on employee retention more efficiently and effectively. Leaders need to understand that the main reason for the majority of the employees who decide to leave the organization is partly due to the leaders themselves. Besides, the leaders need to keep track of

employee retention as the cost of disengaged and turnover employees are expensive. Higher employee happiness index and retention can be maintained as organizations have gained in understanding the effect of transformational leadership styles towards employee retention.

It is expected that, leaders who are able to instill pride and respect among employees, provide a clear vision to them, allowing employees to instill creativity and attentive to employees' need would have a significant relationship towards employee retention. Those who are able to display these type of behaviours towards employees, would earn their respect and reduce their intention to leave the organization. Thus, it is proposed that organizations can start to hire business leaders with specified characteristics that can help them to ensure increase in employee productivity and performance. Finally, it is anticipated that the result of this study can increase the SMEs awareness regarding the determinants of transformational leadership towards employee retention.

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**e-ISSN: 2682-7840**