

# Impact of Transactional Leadership Style on Business Performance of SMEs in Tanzania

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*This study is based on a field survey research conducted in Tanzania between February and July 2015 focusing into CEOs (Chief Executive Officers) of SMEs (small and medium enterprises). The study covered 60 % of all regions in Tanzania including Dar es Salaam, Pwani, Iringa, Morogoro, Dodoma, Mbeya, Tabora, Kigoma, Ruvuma, Rukwa, Mwanza, Arusha and Mara, Singida, Tanga, Kilimanjaro, Mara and Simiyu. Purposive sampling was used to prepare a sample of 100 respondents based on their availability and willingness to participate in the study after introductory telephone conversations meant to create conducive environment for mailed questionnaires. However 60 questionnaires only qualified for further analysis while the rest were discarded for various reasons. This is a quantitative study which attempts to determine the relationship between transactional leadership style and business performance of small and Medium Enterprises in Tanzania. The study aims at firstly, determining the strength and direction of the correlation between transactional leadership style and business performance of SMEs in Tanzania. Secondly, the study determines the significance of the correlation between transactional leadership style and business performance of SMEs in Tanzania. Thirdly, the study determines the extent to which transactional leadership style predicts performance variations of SMEs in Tanzania and fourth, it determines the significance of transactional leadership style as a predictor. Data was analyzed quantitatively using Pearson product moment correlation and simple regression by SPSS. This study found existence of significant and moderate positive correlation between transactional leadership style and business performance of SMEs in Tanzania. Moreover, transactional leadership style was found to be a significant moderate predictor of business performance of SMEs in Tanzania.*

**Key words:** Business Performance, Business success, Firm Performance, Organizational Performance, Transactional Leadership Style and Small and Medium Enterprises

## INTRODUCTION

Role of leadership in business firms has long not been recognized in Tanzania. Neither policy makers nor researchers have shown any serious interest in leadership development and related researches, until recently when Mgeni, 2015 and Mgeni&Nayak, 2015 researched on the link between entrepreneurial leadership style and business performance of SMEs in Tanzania. Much emphasis has been in management under the expense of business leadership, as a result less is known about leadership role in the business performance of various firms in Tanzania. It is not surprising to note that, there is no school or institution which offers any business leadership program while almost every academic institution has a management training program, (Olomi, 2006). Tanzania is experiencing very poor performance of SMEs sector despite good business environment created by the government to attract investors. For example 3 out of every 5 SMEs' startups fail within a period of less than 5 years of its establishment (Mfaume, and Leonard, (2004)). Moreover, the surviving firms are stagnant in growth and contribute very little to the national economy (Dalberg, 2011). Poor performance of SMEs sector is of big concern because 95% of all businesses in Tanzania are SMEs thus its underperformance shakes the entire economy (Madatta, 2011). According to Zheltoukhova, and Suckley, (2014), failure of SMEs in early stages of its life cycle and stagnancy indicate poor business performance associated with leadership factor. Studies elsewhere

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have found a strong and significant correlation between certain leadership styles and business performance of SMEs (Udoh&Agu, 2012). Moreover existing literature found consistently that, leadership is a predictor of business performance of SMEs. Nevertheless, to the time this study was done, no study was found to have covered anything on the relation between transactional leadership style and business performance of SMEs in Tanzania. This study therefore aims at determining the relationship between transactional leadership style and business performance of SMEs in Tanzania.

## CONCEPTUALIZATION OF KEY TERMS

### Transactional Leadership Style

The distinction between transactional leadership and other styles in the full range leadership model such as transformational and passive avoidant leadership styles is well established in the existing literature (Heuvel, 2010). However there are various definitions given on this concept which in principal they are not contradictory as they appear to be, rather they are different view points of the same idea. Tosi, (1982), has defined transactional leadership style as the set of behavior which highly concentrates on implementing strategies, improving hierarchical structure, and rewarding employee performance and exhibit active management by exception behavior to correct mistakes so that they can devote significant contribution to improve organizational performance. Likewise, Rukmani, (2010), considered transactional leadership to be the type of leadership where the leaders dedicate most of their time and effort to explain about what is required from followers and expected compensation upon completion of these requirements. It is called a transaction because it involves transactions between leaders and followers (Bass 1990, Khan I-Harn, 2001 and Arham, (2014). The transactional leadership style is based on maintenance of the status quo in the sense that it does not allow flexibility in the organization (Khan, 2013). This is unique because other leadership styles such as transformational

leadership are more innovative and flexible which often challenge the organizational regimes by rewarding those who go beyond the organizational performance's norms (Udoh and Agu, 2012). Transactional leadership seeks to lead the organization in accordance with the established rules and regulation in which any attempt to deviate is not tolerated (İşcan, et al., 2014). Transactional leadership is thus conceptualized as the exchange relationship between leaders and their followers (Burns, 1978). In transactional leadership, relationship between the leader and follower, is based on contingent reward (Howell & Avolio, 1993 and Fernandes&Awamleh, 2013).

### Business Performance

There has been a debate among researchers on what business performance is all about (Dess&Robinson, 1984 and Barney, 1997). The main agenda has been what is the meaning of the concept, how do we call it and how can we possibly measure it. The fact that, Business performance is a multidimensional concept has made things difficult for researchers to arrive into consensus on what business performance is all about (Hansen & Wernerfelt, 1989 and Wiklund & Shepherd, 2005). Performance is probably the most researched theme in management sciences (Venkatraman, & Ramanujam, 1986).

Most of the studies reviewed, suggested no difference in the use of performance related terms such as; business performance, firm performance and organizational performance. For example studies like Hansen & Wernerfelt, 1989; Richard, 2000; Vithessonthi, & Thounrungrroje, 2011; Ahmad, 2012 and Santos & Brito, 2012 used the term firm performance and organizational performance interchangeably to mean increase in organizational output resulting from improved input and efficient process in the organizational system. Likewise studies like; Yang, (2008), Aziz, et al., (2013) a, Arshad, & Rasli, 2013, and Arief, Thoyb & Sudiro, 2013 used the term business performance and Organizational performance to mean the same thing

as those who used the term firm performance, On the other hand, Javier, (2002) as cited by Abu-Jarad, Yusof&Nikbin,(2010), associates, business performance with the famous 3Es (economy, efficiency, and effectiveness) of a certain program or activity. One thing seems to be common among all studies when trying to conceptualize performance in the organizational context. Almost all such studies take into consideration, what brings about organizational output than just looking at it as a complete set in itself. In other words, performance is considered to be more of a system involving input, process and output than just the outcome of the organizational functioning(Wu, 2009). Along this line of thinking, Daft (2000), defined organizational performance as the organization's ability to attain its goals by using resources in an efficient and effective manner. Likewise, Armstrong & Baron, 1998 and Ahmad, 2012, defined performance of the organization as a strategic and integrated approach to delivering sustained success to organizations by improving the performance of the people who work in them and by developing the capabilities of teams and individual contributors. Moreover, Steers, (1982) and Maalu, (2013), defined firm performance as efficiencies and effectiveness in terms of utilization of resources as well as the accomplishment of its goals. The same positions are shared by other studies such as Dess& Robinson, (1984)and Ricardo( 2001). Existing literature, reported existence of complications in measuring multidimensional performance due to its complexity (İşcan et al., 2014)). Likewise this study focuses into organizational output for simplicity and clarity although terms like business performance, organizational performance and firm performance are considered to be the same thus are used interchangeably.

#### Small and Medium Enterprise (SMEs)

Small and Medium Enterprises (SMEs) conceptualization has been controversial and often misleading in developing countries resulting into serious impediments in the development of the

particular sector (Gibson &van der Vaart, 2008).There has been a hot debate among researchers and entrepreneurial practitioners as to whether it really matters to take SMEs' conceptualization into serious consideration when thinking of how to improve SMEs in the developing countries. According to Gibson &van der Vaart, (2008), the meaning you attach to SMEs have a lot to do with the performance of SMEs sector in the particular country.

For example if any misconception of SMEs happens, it can lead to misallocation of donor spending for private sector development, contribution of the sector to the economy will be mislead statistically and it may cause policy distortion in setting development priorities. On that ground Gibson and Van der Vaart, (2008) defined SMEs by formulae criterion as an attempt to develop a universally accepted meaning of SMEs. However, some studies suggested that, defining SMEs, in the socio-cultural context is more appropriate than any attempt to come up with a universal definition, mainly because, SMEs tend to differ from one cultural setting to the other (Hamisi, 2011). Literature suggests multiple criteria of defining firms in relation to Small and Medium Enterprises (SMEs) worldwide ((URT, 2003, Mgeni&Nayak, 2015). Capital investment and size of the firm are the most used criteria in international classification of firms. Each country has its own criteria used to define SMEs for policy planning purposes (Mgeni, 2015). In Tanzania, for example the term SMEs is used to mean micro, small and medium enterprises, sometimes referred as micro, small and medium enterprise (URT, 2003).However, SMEs' working definition by the Tanzanian entrepreneurial policy excludes micro firms because in most cases their impacts in business are insignificant. Commonly used yardsticks in the conceptualization of SMEs in Tanzania include; total number of employees, total investment and sales turnover.in Tanzania's context SMEs are the one with 5 to 99 employees and capital investment of between 2500 to 400,000 US dollars approximately (URT, 2003). This study will use the Tanzanian definition of

SMEs as shown in table 1, because the study will focus on Tanzania's context.

Table A1: types of Firms in Tanzania		
Category	Employee	Capital Investment In Machinery (USD) as per October 2015
Micro enterprise	1-4	Up to 2500
Small enterprise	5-49	Above 2500 to 100,000
Medium enterprise	50-99	Above 100,000 to 400,000
Large enterprises	100+	Above 400,000

Source: URT, 2003

## LITERATURE REVIEW

### Transactional Leadership Style and Business Performance of SMEs

There are many factors associated with business performance of SMEs (Udoh&Agu, 2012). Leadership is said to be the leading factor in influencing organizational performance (Mahdinezhad, et al., 2013). In other words, leaders' performance is one of the important pointers when assessing organizational performance (Wall et al., 2004). Different styles of leadership can influence organizational performance or effectiveness in different ways (Nahavandi, 2002 and Ali, et al., 2014). Transactional leadership for example is important for managing organizations, but it may not be the best style for leading all types of organizations(Kuhnert & Lewis, 1987 and Khan, Ghouri&Awang, 2013). In this study we focus into determining the relation between transactional leadership style and business performance of SMEs in Tanzania. Transactional leadership is about guiding or motivating their followers in the direction of established goals by clarifying the role and task requirements (Robbins, 2003 and Politis, 2004). Although no study was found to have covered this topic in Tanzania, Previous studies elsewhere have found a variety of findings on the link between transactional leadership and business performance

of SMEs. Literature suggests similarity of findings in studies done on the same industry and geographical location (Koech&Namusonge, 2012).For example Rosian&Rosli, (2012) from Malaysia found a significant moderate positive correlation between transactional leadership and business performance of SMEs. These findings were consistent with other works from Malaysia done in the same industry such as; Arham, Muenjohn& Boucher, (2012); Aziz, et al., (2013a) and Arshad&Rasli, (2013). However, under certain circumstances, studies done in the same industry had similar findings irrespective of its geographical location as for the case of Obiwuru, et al., (2013) who reported similar findings as that of Malaysia when he did a study on the same industry in Nigeria. On the other hand, Voon, et al., (2011) researching on multi industrial SMEs in Malaysia found a significant negative correlation between transactional leadership and business performance. Likewise Yanney, 2014, did similar study in Ghana and reported similar findings. However most of these findings have been challenged for not taking into consideration moderating factors like size of the firm which might have brought different set results.

Despite mounting critics to the findings of previous studies for not taking moderators into consideration, literature suggests absence of much difference of the relation between transactional leadership style and business performance on the basis of firm size as for the case of SMEs and corporate firms. For example; Koech&Namusonge, (2012) and Ali & Ibrahim, (2014), conducted a study similar to that of Arham, Muenjohn& Boucher, (2012), in the corporate sector and found a significant moderate positive correlation between transactional leadership style and business performance, a result similar to that of SMEs. The similarity of findings irrespective of the size of the firm confirms the findings advanced by Kipesha, (2013), that, in Tanzania's context, size of the firm has a negative correlation with business performance. Studies done elsewhere found similar results irrespective of the nature of industry covered (Amato &Burson, 2007). However it is also true that



there are some studies which have found a positive correlation between firm size and organizational performance (Majumdar,(1997); Vijayakumar and Tamizhselvan, (2010); Pervan and Visic,(2012). As literature suggests, it is important to note that moderating factors like firm size are contextual thus its application in the organizational performance researches should not be generalized.

Generally it can be concluded that, previous works on the impact of transformational leadership style on business performance of SMEshave reported two main findings: Firstly, existence of significant and moderate positive correlation between transactional leadership and business performance. Secondly, transactional leadership is a moderate predictor of business performance variations in SMEs. Since no previous study within our scope of literature search was found to have researched on the impact of transactional leadership style on business performance of SMEs in Tanzania, this study attempts to bridge that knowledge gap.

RESEARCH HYPOTHESES

This study attempted to determine the relationship between transactional leadership style and business performance of SMEs. Two hypotheses drawn from literature review were tested. The hypotheses which were tested by this study included:

H1. There is a significant moderate positive correlation between transactional leadership style and business performance of SMEs in Tanzania.

H2. Transactional leadership style is a significantandmoderate predictor of business performance variations of SME in Tanzania.

RESEARCH DESIGN

Research Methodology

Research survey by mailed questionnaires and telephone interviews were used to collect data from CEOs of 100 SMEs in Tanzania sampled purposively

to suit the context of this study. Respondents were selected because they happened to be at the right time and place which could allow them willingly to participate in the study as per researcher's schedule. Telephone interviews were done to identify the right respondents and solicit email addresses for mailed questionnaires because most of SMEs listed in various authorities had no email addressesgiven instead were provided with receptionist phone numbers. In other words telephone interviews did not cover any technical questions because were meant to prepare more conducive environment for mailed questionnaires. Moreover; survey by mailed questionnaires was found necessary due to scattered nature of SMEs in Tanzania which could otherwise cause loss of time and financial resources(Wilcock, 2014).

Research Method

This study used Quantitative method in which two hypotheses were tested using quantitative statistical tools starting with Pearson product moment correlation followed by simple regression by SPSS. This method was chosen because it is one of the well establishedphenomena(Wilcock, 2014).. Pearson product moment correlation was used to test the strength, direction and significance of the correlation between transactional leadership style and business performance of SMEs while simple regression was used to test the significance and prediction strength of transactional leadership style on business performance variations in SMEs.

Validity and Reliability of the Instruments

This study used two questionnaires namely, Transactional leadership questionnaire (TRLQ) adopted from Multifactor Leadership Questionnaire (MLQ) developed by Bass &Avolio, (2004) and outcome based business performance questionnaire (OBPQ) adopted from Multidimensional Business performance questionnaire (MBPQ) developed by Wu, 2009. TRLQ and OBPQ are standard questionnaires widely used by previous studies and proven to be valid and reliable.Cronbach's Alpha

test was used to test internal consistence of items with each of the two questionnaires well known as reliability while construct validity of TRLQ and OBPQ were tested by Factor Analysis (FA). Since TRLQ and OBPQ were not originally meant for Tanzanian context thus it was found inevitable for this study to employ validity and reliability confirmatory test. The aim was to make TRLQ and OBPQ applicable in Tanzania's context as it is well established in the existing literature that, the applicability of leadership and performance tools is usually affected by contextual factors (Wong, et al., 2012). Both questionnaires were confirmed to be valid and reliable. Table 2 and 3 summarizes the reliability output for the two tools where as FA output is not reported in tables due to space limitation.

Table A2: Transactional leadership style reliability output

Reliability Statistics		
Cronbach's Alpha	Cronbach's Alpha Based on Standardized Items	N of Items
.906	.904	2

As shown in Table 2,Cronbach's Alpha (CR) for Transactional Leadership Questionnaire (TRLQ) was found to be 0.906 thus confirmed the tool to be highly reliable for this type of study in Tanzania's context. Likewise, as shown in table 3, OBPQ's CR was found to be 0.762, which implies good reliability for the particular tool in Tanzania's context. More over both questionnaires loaded highly in the FA test thus were retained.Construct validity under FA test showed that the two items for TRLQ were extracted under a single factor with as high loading as 0.87 and 0.79 forContingent rewards (CR) and Active Management by objectives (MBE-A) respectively

Table A3: Business performance Reliability output

Reliability Statistics		
Cronbach's Alpha	Cronbach's Alpha Based on Standardized Items	N of Items
.762	.704	9

MEASURES

Transactional leadership style Measures.

Transactional leadership style is widely researched thus its measures are also well established. This study used Avolio, (2004)'s version of transactional leadership style measures which consist of two items namely;Contingent rewards (CR) andActive Management by objectives (MBE-A) (Chan I-Harn, A.,2001). Both two items were rated on a five-points Likert scale ranging from 0 (not at all) to 4 (frequently,if not always).

Business Performance Measures

Despite of being one of the widely researched phenomena in organizational management studies, Business performance measures have remained controversial among researchers and policy makers (Yang, 2007, 2008).Some studies have considered organizational inputs such as human and financial resource to be indicators of business performance in the particular organization(Dess& Robinson, 1984; Ricardo 2001and Maalu, 2013). On the other hand, others measured business performance in terms of the process involved in the transformation of inputs into organizational outputs while many capitalized on organizational output measures such as Profitability; Gross profit Return on asset (ROA), Return on investment (ROI), Return on equity (ROE), Revenue growth, Market share and stock price for financial business performance of SMEs ( FSDT). There are few studies such as Wu 2009 which have attempted to use a multidimensional performance measures which combines organizational, input, process and output indicators. This study adopted an outcome or result based business performance measures developed by Wu, 2009 as part of multidimensional business performance questionnaire. Outcome based performance measure consists of 8 items namely; Growth in market shares, Quality of products and services offered, Growth of returns on assets (ROA), Growth of return on investment (ROI), Growth of

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return in equity (ROE), Growth of return on sales, Growth on exports and Growth in the size of the firm. Outcome based business performance questionnaire was measured by 5 point Likert scale ranging from 1 to 5; 1(very poor to 5 (very good) based on the respondent assessment

## FINDINGS AND DISCUSSION

This study tested two hypotheses using Pearson product moment correlation and simple regression. The findings are presented in sequence starting with the first hypothesis followed by the second hypothesis.

### H1. There is a significant moderate positive correlation between transactional leadership style and business performance of SMEs in Tanzania.

The first Hypothesis was tested by using Pearson product moment correlation by SPSS 16.0 software. According to Lane (2007) Pearson correlation coefficient can be interpreted as weak, moderate and strong as indicated in table 4. 0, implies no association, 0.10 to 0.30 implies weak correlation, 0.31 to 0.50 and 0.51 to 1.00 for moderate and strong correlation respectively.

Table A4: Interpretation of Pearson correlation coefficient		
Strength of Correlation	Positive correlation	Negative correlation
No correlation	0	0
Small or Weak	.10 to .30	-.10 to -.30
Medium or Moderate	.31 to .50	-.31 to -.50
Large or Strong	.51 to 1.00	-.51 to -1.00

Source: Adopted from Lane, 2007

Pearson product moment correlation output in table 5, shows that, there is a moderate positive correlation between transactional leadership style and business performance of SMEs in Tanzania. The Pearson correlation coefficient is 0.409 which is a moderate positive correlation when 1 is taken as a perfect positive correlation as shown in table 4. Pearson

product moment correlation found significant correlation between transactional leadership and business performance of SMEs in Tanzania. As shown in table 4, the p-value is 0.000, which is below 0.01, level of significance (2 tails), thus the hypothesis is supported. Based on these findings it can be concluded that, there is a significant and moderate positive correlation between transactional leadership and business performance of SMEs in Tanzania.

### H2. Transactional leadership style is a significant moderate predictor of business performance variations in SME in Tanzania

Simple regression by SPSS was used to test the second hypothesis, which aimed at determining the extent to which transactional leadership style predict business performance variations of SMEs in Tanzania. Transactional leadership was regressed against business performance as a dependent variable and its results are presented in table 6 and 7.

Second hypothesis basically tested the regression model represented by table 6. The regression model tested is thus summarized as  $BP = 1.682 + 0.409(TRLs)$

Where BP is business performance

TRLs is transactional leadership style

Coefficient table (table 6) further shows that, at 95% level of confidence, p value of the regression model is 0.000, which is potentially less than 0.05 and thus significant; this implies that, there is a big possibility that the population slope is significantly different from zero therefore the regression model is capable in predicting variations of the dependent variable.

As indicated in table 7, Coefficient of determination ( $R^2$ ) for the regression model,  $BP = 1.682 + 0.409(TRLs)$ , was found to be 0.341, implying that transactional leadership style can predict 34% of the variations in business performance of SMEs Tanzania. According to Lane, (2007), the interpretation of the coefficient of determination ( $R^2$ ) is that; 0.10 to 0.30 implies weak prediction, 0.31 to

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0.50 suggest moderate prediction and 0.51 to 1.00 implies strong OR perfect prediction. Based on this interpretation we conclude that, transactional leadership style is a moderate predictor of business performance of SMEs in Tanzania. However  $R^2$  does not give us any picture as to whether the transactional leadership style is significant and thus a useful predictor of business performance variations, unless we include ANOVA regression output

Table 8 shows the significance of the predictor in the regression model,  $BP = 1.682 + 0.409(TRLs)$ . As it has been found in table 7 that, transactional leadership style is a moderate predictor of business performance of SMEs in Tanzania; table 8 found the

P-value of the predictor in the regression model to be 0.000, which is basically less than 0.05, significance level. If we put it in different words, it can be concluded that transactional leadership style is a significant predictor of business performance of SMEs in Tanzania.

Since the regression model,  $BP = 1.682 + 0.409(TRLs)$ , has been found to have moderate and significant predictor of business performance variations of SMEs in Tanzania, hypothesis two is thus well supported. We have sufficient evidence to conclude that, Transactional leadership style is a significant moderate predictor of business performance of SMEs in Tanzania.

Table A5: Correlation between transactional leadership style and business performance of SMEs in Tanzania

Correlations			
		Transactional Leadership Style	Business Performance
Transactional Leadership Style	Pearson Correlation	1	.409**
	Sig. (2-tailed)		.000
	N	60	60
Business Performance	Pearson Correlation	.409**	1
	Sig. (2-tailed)	.000	
	N	60	60

\*\* Correlation is significant at the 0.01 level (2-tailed).

Source: Authors based on data collected by mailed questionnaires between February and April 201

Table A6: Regression model

Coefficients <sup>a</sup>								
Model		Un standardized Coefficients		Standardized Coefficients	t	Sig.	95% Confidence Interval for B	
		B	Std. Error	Beta			Lower Bound	Upper Bound
1	(Constant)	1.682	.224		7.524	.000	1.234	2.129
	Transactional Leadership Style	.409	.053	.416	5.855	.000	.269	.549

a. Dependent Variable: Business Performance

Source: Authors based on data collected by mailed questionnaires between February and April 2015



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Table A7: Coefficient of determination (R<sup>2</sup>)

Model Summary <sup>b</sup>

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.409 <sup>a</sup>	.341	.336	.327

a. Predictors: (Constant), Transactional Leadership Style

b. Dependent Variable: Business Performance

Source: Authors based on data collected by mailed questionnaires between February and April 2015

Table A8: Significance of the predictor

ANOVA <sup>b</sup>

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	6.259	1	6.259	34.277	.000 <sup>a</sup>
	Residual	10.591	58	.183		
	Total	16.850	59			

a. Predictors: (Constant), Transactional Leadership Style

b. Dependent Variable: Business Performance

CONCLUSION

Based on the findings made by this study, four main conclusions are drawn; firstly, this study found a moderate positive correlation between transactional leadership style and business performance of SMEs in Tanzania. Secondly, the correlation between transactional leadership and business performance of SMEs is found to be significant. Thirdly, transactional leadership style is found to be a moderate predictor of business performance variations of SMEs in Tanzania. Fourthly, Transactional leadership style was found to be a significant predictor of business performance variations in SMEs. These findings are consistent with previous studies elsewhere such as Arham, Muenjohn& Boucher, (2012); Rosian&Rosli, (2012), Aziz, et al., (2013) and Arshad & Rasli, (2013). Since this study took SMEs as a whole sector, further studies are invited to conduct similar studies in specific industries such as agribusiness, and microfinance related SMEs, to shed more light on the

link between transactional leadership style and Business performance of SMEs from specific industries point of view. However, we are of the expectation that, this study will be of big help to researchers, policy makers, business leaders and other stake holders interested with the development of entrepreneurial sector in Tanzania and elsewhere.

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