Transformational Leadership, Organizational Reward Systems and Performance of Telecommunication Firms in Kenya

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Abstract

Purpose *– The purpose of this study was to investigate the moderating effect of organizational reward systems on the relationship between transformational leadership and firm performance.The empirical study employed a questionnaire approach. The Sample for the study was drawn from a population of 404 Telecommunication firms registered under the Communications Authority of Kenya (CAK) as at June 2014. Regression analysis was used to test the hypotheses in a sample of 202 firms. The findings suggest that Transformational leadership has a direct and significant effect on firm performance. In addition, organizational reward systems have no significant moderating effect on overall firm performance and financial firm performance. However, the moderating effect of reward systems on the relationship between transformational leadership and nonfinancial firm performance is significant.*

Keywords: Transformational Leadership, Reward systems, Performance, Telecommunication Firms

1. Introduction

Transformational leaders have been characterized as possessing attributes of idealized influence, inspirational motivation, Intellectual Stimulation and individualized consideration (Bass, 1985). These attributes are argued to influence the performance of a firm in many ways, leading to greater effectiveness and outcomes (Avolio & Howell, 1992; Arnold et al., 2001; Bass *et al.*, 2003; Hetland and Sandal 2003; Yammarino & Bass 1990; Wofford *et al.*, 2001; Walumbwa & Muchiri, 2012). Transformational leadership style has gained a strong base with several studies conducted over many years, and it is still more studied than other leadership styles. However, it is surprising that few studies have empirically established strong evidence to support its connection with firm performance. For example, Tosiet al. (2004), Waldman *et al.* (2001), Agleet al. (2006) and Ensley *et al.* (2006) failed to find any connection between transformational leadership and firm performance. Ling *et al.* (2008) found a significant connection in a sample of less complex, small, privately held firms. Similarly, Pedraja-Rejaset al. (2006) found that transformational leadership has a positive impact on performance in a sample of small firms. Hmieleski's (2006) found no evidence to support a positive main effect of chief executive officer transformational leadership on firm performance. Ling et al.(2008) argue that the weak relationship found in prior studies between transformational leadership and performance may be a consequence of using data from large firms where organizational complexity is a major obstacle to establishing this link. This research aims to add on to existing empirical work which has tried to establish a relationship between transformational leadership and firm performance.Organizational rewards refer to the basis upon which rewards are distributed to two or more individuals in organizations (e.g. Wageman & Baker, 1997).Research findings suggest that Organizational rewards play a crucial role in attracting new employees, eliciting good work performance and maintaining employee commitment and engagement (Day et al., 2014; Kerrin & Oliver, 2002; Tomaževič et al., 2014). A number of researchers have found that transformational leadership and rewards offered by an organization are individually positively associated with a number of employee behavioral variables such as satisfaction with their jobs, their overall work situation and their productivity (Brown& Dodd, 1999, Bass, 1990a, Hater & Bass, 1988,).

Muchiri et al (2012) concluded that by practicing aspects of transformational leadership such as articulating clear standards and expectations for performance and showing recognition to work unit members for goal achievements, work unit leaders may establish a foundation that later leads to higher performance outcomes. Furthermore, promoting aspects of social processes of transformational leadership such as communication, enhancing adaptability and resolving uncertainties may lead to greater clarification and subsequent higher performance outcomes. The positive effects of transformational leadership on employee attitudes and organizational outcomes through rewards as reported in a number of studies are however contradicted by Yammarino et al. (1998) who found no relationship between transformational leadership, organizational rewards and objective organizational outcomes.This study aims to determine whether rewards offered by an organization have an effect on the relationship between transformational leadership and firm performance.

2. Literature review and Hypotheses Development

This section reviews the literature to identify the relevant practices comprising Transformational leadership, rewards offered by organizations and firm performance. Hypotheses are then developed based on the literature that has been reviewed.

2.1 Transformational Leadership and Firm Performance

Bass (1985) identifies four dimensions of transformational leadership. They include idealized influence inspirational motivation, intellectual stimulation, and individualized consideration (Dionne et al., 2004). Idealized influence emphasizes trust, values, and ethics. Inspirational motivation consists of leaders providing meaning and challenge to followers' work and using inspiring messages to arouse emotions. Intellectual stimulation challenges old assumptions, beliefs, and traditions, and encourages new ways of thinking. Individualized consideration refers to leaders who consider the needs, abilities, and goals of followers and provide coaching and mentoring. Meta-analytic evidence has shown that transformational leadership has strong positive relationships with not only leader effectiveness but also follower satisfaction with leaders, job satisfaction, organizational commitment, and job performance (DeGroot et al., 2000; Judge & Piccolo, 2004; Lowe et al., 1996). Transformational leadership has been found to be closely associated with a range of organizational outcomes pertaining to the individual followers' creativity (Gumusluoglu & Ilsev, 2009; Shin & Zhou, 2003), satisfaction and performance (Vecchio et al., 2008). Based on the above literature review, we can propose the following hypothesis

H1.Transformational leadership has a significant effect on Firm Performance

2.2 Transformational Leadership, Organizational Rewards and Firm Performance

Firm performance has been viewed in many different aspects and connotations depending on application e.g. McCann (2004) and Firer (2003) viewed it in terms of efficiency and effectiveness in converting inputs into outputs. Norton & Kaplan (1987) viewed it in terms of balanced scorecard (Innovation, learning and internal processes). Richard et al. (2009) viewed firm performance as encompassing three specific areas of firm outcomes; financial performance (profits, return on assets, return on investment); product market performance (sales, market share) and shareholder return (total shareholder return, economic value added etc).Studies have reported positive effects of transformational leadership on employee attitudes and organizational outcomes through reward systems. For example, Combs et al.'s (2006) Meta analysis which included 92 studies showed a link between three sets of influential HR practices and firm performance. The practices include those that increase employee skills, empower employees, improve motivation as well as pay and reward practices. Thompson (2000) found that practices that build skills, motivation and ability, including share ownership schemes, broad bands, competence based pay, and team rewards were associated with higher organizational performance in the aerospace sector. In addition, Muchiri et al (2012) found that certain aspects of transformational leadership such as articulating clear standards and expectations for performance and showing recognition to work unit members for goal achievements may establish a foundation that later leads to higher performance outcomes. Thompson (2000) found that practices that build skills, motivation and ability, including share ownership schemes, broad-bands, competence-based pay, and team rewards were associated with higher organizational performance in the aerospace sector. Similarly, in a study of 25 customer service organizations, Brown and West (2005) reported links between employee engagement and customer service performance, with employees influenced by reward practices such as variable pay and recognition awards.

The effect of transformational leadership on firm performance as moderated by organizational rewards has been confirmed by a number of studies. The current study sought to extend this line of research to determine whether organizational rewards have a moderating effect on firm performance. This study unlike previous ones will focus on organizational rewards classified as monetary, developmental and recognition rewards. This classification was derived through extensive review of literature. In view of prior empirical evidence on the connection between rewards and firm Performance, the following hypothesis was proposed.;

H2: The relationship between transformational leadership and firm performance is moderated by organizational rewards.

3. Research methodology

3.1 Data collection and sample

The empirical study employed a questionnaire approach designed to collect data for testing the validity of the model and research hypotheses. Variables in the questionnaire include background information, Transformational Leadership, reward systems and firm performance. All of the independent and dependent variables were assessed via five-point Likert-type scales. The sample for this study was drawn from a population of the 404 Telecommunication firms listed in the Communications Authority of Kenya (CAK) register as at June 2014. A random stratified sampling method was used to select 202 firms representing each of the six Tiers. Questionnaires were distributed to all the available sampled firms. Follow-up e-mails and phone calls were done after two weeks. Out of the 202 firms that the study targeted, valid data was available from 160 firms representing a success rate of 79.2%, which was considered acceptable.

Survey measures

Five-point Likert scales with anchors of "not at all" (1) and "a very great extent" (5) were used to measure transformational leadership. A total of 18 items on transformational leadership were adopted from Bass (1985) Multi Leadership Questionnaire (MLQ) measuring the behavioral components of individualized consideration, intellectual stimulation, inspirational motivation, and Idealized influence. An example of a sample item included for individualized consideration is, "Recognizes differences among employee in their strengths and weaknesses, likes and dislikes". Judge and Piccolo (2004) reported an average correlation of 0.93 after correction for unreliability among the four transformational leadership dimensions. Accordingly, and consistent with prior studies (for examples, Judge and Piccolo, 2004; Piccolo & Colquitt, 2006; Wang & Rode, 2010; Wang & Walumbwa, 2007), the approach of these studies was adopted in combining the four sub-dimensions of transformational leadership into a single transformational leadership factor. To measure organizational rewards systems and firm performance, this study relied on instruments developed in other related studies, as well as concepts generated from appropriate literature. Organizational rewards questionnaire was developed with number of questionnaire items derived from Nick Bontis (2006). Each statement was rated using a five point Likert scale ranging from strongly agree (5) to strongly disagree (1). Firm performance was measured using statements derived from both financial and non financial measurements which were derived from reviewed literature. Financial measurements included gross profit, return on shareholder equity and growth in market share. Non financial measures included innovation and customer satisfaction and retention. The questionnaire statements were rated based on a 5-point Likert scale from strongly disagree (1) to strongly agree (5). The study adopted a Cronbach alpha coefficient of 0.7 as the minimum acceptable measure of reliability. Hair et al. (1998) stated that a value of 0.70 and higher is often "considered the criterion for internally consistent established factors". Results indicated the variables had alpha coefficient ranging from 0.83 for reward systems, 0.95 for Transformational Leadership and 0.96 for firm performance. Demographic data about the firms was collected which included the number of years in operation, number of employees, scope of operations and ownership structure. The size of the firm was measured in terms of the number of employees who are currently employed by the telecommunication firms. The results show that majority of telecommunication firms (60%) had more than 100 employees. This implies that most of the telecommunication firms in Kenya fall under the category of medium and large Enterprises as per the government of Kenya guideline (GOK 2005). Results on ownership structure indicated that majority of the telecommunication firms (55%) were fully locally owned. Results further show that majority (60%) of telecommunication firms had been in operation for 11- 20 years. only 24 firms were older than 30 years.

Analysis and Discussion of Results

The first objective of the study was to establish the effect of transformational leadership on the performance of telecommunication firms in Kenya. Transformational leadership was operational zed using Bass (1985) attributes namely Idealized Influence, Inspirational motivation, Intellectual stimulation and individualized consideration. To test therelationship between Transformational Leadership and Performance of telecommunication firms in Kenya, the following hypothesis was formulated;

H1: Transformational leadership has a significant effect on Firm Performance

A simple regression analysis was performed to test this hypothesis. The results show that **t**he model summary revealed that 73% of the variation on firm performance can be explained by transformational leadership while the remaining percentage can be explained by other factors which are not present in the model. The models goodness of fit indicates that there is a significant relationship between transformational leadership and firm performance, F = 417.672, $p\leq 0.05$. There is a positive and significant relationship between transformational leadership and firm performance ($\beta = 0.852$, $p\leq 0.05$). This implies that a unit change in transformational leadership increases firms' performance by 0.852 units. The results are indicated in table**3.1**

Table 3.1 Regression Results on the Relationship between Transformational Leadership and Firm Performance

Model summary					
R	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**	**Durbin-Watson**	
.85	0.73	0.72	0.053	1.93	
ANOVA					
	Sum of Squares	**df**	**Mean Square**	**F**	**Sig.**
Regression	115.361	1	115.361	417.672	.000
Residual	43.639	158	0.276		
Total	**159**	**159**			
Coefficients					
	Un-standardized Coefficients		**Standardized Coefficients**		
	B	**Std. Error**	**Beta**	**t**	**Sig.**
(Constant)	1.12E-17	0.042		.00	1
Transformational Leadership	0.852	0.042	0.852	20.437	.00
a. Dependent Variable: Firm PerformancePredictor variable : Transformational Leadership					

Table 3.2: Regression Results for moderating effect of reward systems on the Relationship between Transformational leadership and Firm Performance

Model		**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**	**Change Statistics**				
						R Square Change	**F Change**	**df1**	**df2**	**Sig. F Change**
	1	.795[a]	0.633	0.63	0.608	0.633	272.117	1	158	0
	2	.875[b]	0.765	0.762	0.48782	0.132	88.437	1	157	0
	3	.875[c]	0.765	0.761	0.48918	0	0.133	1	156	0.716
a Predictors: (Constant), Transformational Leadership										
b. Predictors: (Constant), Transformational Leadership , Rewards										
b Predictors: (Constant), Transformational Leadership, Reward TL*RS										

The second objective was to establish the moderating effect organizational rewards on the relationship between transformational leadership and firm performance. Organizational rewards were operationalized through developmental, recognition and monetary rewards. The following hypothesis was formulated;

H2: **Organizational Rewards have a moderating effect on the relationship transformational leadership and firm performance**

A three-step stepwise regression analysis was used to test this hypothesis asproposed by Baron and Kenny (1986). Step 1: Dependent variable was regressed on the independent variable. Step 2: Moderating variable was added to the regression equation. Step 3: The interaction term (between independent and moderator variable) was added to the regression equation. All the variables comprising transformational leadership, reward systems and the interaction term were entered in the regression model. To confirm moderation, the interaction term should be significant ($p<0.05$). From the resultsintable 3.2, transformational leadership alone accounts for 63% of the variance on firm performance (adjusted $R^2=0.630$, F=272.117). In step 2, the results show that rewards and transformational leadership account for 76.2 % (adjusted $R^2=0.762$, F=88.437) of change in firm performance. In step 3, a product of rewards and transformational leadership (transformational leadership*reward systems) were added into the model to determine the effect of rewards on the relationship between transformational leadership and firm performance. The interaction term accounted for 76.1% of the variation in financial performance. The results in step 3 showed that when interaction term was entered into the model, the variance of firm performance barely changed. The movement was very slight from 0.762 to 0.761 and the F-ratio decreased from 88.437 to 0.133. Analysis of variance (ANOVA) was then undertaken to determine the significance of the overall regression models. The results are presented in Table 3.3

Table 3.3 Results of Analysis of Variance (ANOVA) for the Moderating effect of reward systems on the Relationship between transformational leadership and Firm Performance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	100.593	1	100.593	272.117	.000[a]
	Residual	58.407	158	.370		
	Total	159.000	159			
2	Regression	121.638	2	60.819	255.572	.000[b]
	Residual	37.362	157	.238		
	Total	159.000	159			
3	Regression	121.670	3	40.557	169.485	.000[c]
	Residual	37.330	156	.239		
	Total	159.000	159			
a. Predictors: (Constant), Transformational Leadership						
b. Predictors: (Constant), Transformational Leadership , Rewards						
c. Predictors: (Constant), Transformational Leadership , Rewards , TL*RS						

Table 3.4 Results of Regression Coefficients for the Moderating effect of reward systems on the Relationship between transformational leadership and firm Performance

Model		**Unstandardized Coefficients**		**Standardized Coefficients**	**t**	**Sig.**
		B	**Std. Error**	**Beta**		
1	(Constant)	1.522E-16	.048		.000	1.000
	Transformational Leadership	.795	.048	.795	16.496	.000
2	(Constant)	1.602E-16	.039		.000	1.000
	Transformational Leadership	.689	.040	.689	17.104	.000
	Reward system	.379	.040	.379	9.404	.000
3	(Constant)	-.005	.041		-.125	.901
	Transformational Leadership	.688	.041	.688	16.935	.000
	Reward system	.380	.041	.380	9.369	.000
	TL*RS	.018	.051	.014	.365	.716
a. Dependent Variable: Firm Performance						

The results of the analysis of variance presented in Table 3.3 show a statistical significance for the direct effect of transformational leadership on firm financial performance (F= 272.117, $p<0.05$). At step 2, the model of transformational leadership and firm performance was statistically significant F=255.572, $p<0.05$). In step 3, the overall model was statistically significant (F=169.485, $p<0.05$). Regression coefficients results for the test of hypothesis are presented in Table 3.4

As shown in Table 3.4, the regression coefficient was significant at all the three steps of the analysis. The effect of interaction term between transformational leadership and rewards on firm performance was insignificant. (B= 0.014, t=.365, p>0.05), implying that for every unit change in interaction between transformational leadership and organizational rewards, there is a corresponding decrease in firm performance.

Discussion and conclusions

This study has several important findings. First, the results demonstrated that Transformational leadership is positively related to firm performance.This was inconsistent with the findings of Tosiet al. (2004), Ling et al. (2008), Waldman et al. (2001), Agleet al. (2006) and Ensley et al. (2006),who found a very weak connection between transformational leadership and firm performance in a sample of small firms. The findings were also inconsistent with Pedraja-Rejaset al. (2006) who found that transformational leadership has a positive impact on performance in a sample of small firms. The findings were however consistent with O'Reganet al. (2005)who found that firms with transformational leadership had a significant correlation with performance.This study established that majority of the surveyed firms (60%) fall under the category of medium and large Enterprises (SMES). The study therefore recommends that future research should focus on the role of organizational contextual factors on the hypothesized relationship. The results provided insufficient evidence to conclusively support the hypothesis that organizational rewards moderate the relationship between transformational leadership and firm performance. Further research is needed to determine whether various contextual factors such as size, environmental uncertainties and competitiveness may have moderated the findings of this study.A number of researchfindings reported hererevealed that effectively managed rewards have a positive influence on employee motivation, retention and performance (Rumpel & Medcof, 2006).Organizational rewards and procedures help to motivate employees to achieve the vision and goals of the organization.The results offer both theoretical and managerial implications that are useful for researchers and for practicing managers of firms in designing organizational rewards and formulating human resources policies that are supportive of firm performance.

Practical Implications

The results from this study contribute to body of knowledge in Transformational leadership theory as well as reward systems and organizational performance, by identifying possible links among the three variables. The results suggest that companies where leaders demonstrate transformational leadership attributes of idealized influence, inspirational motivation, individualized consideration and intellectual stimulation will positively impact firm performance. Although prior studies indicated that effective organizational rewards contribute to creating value for organizations, leading to improved performance, this study was not able to find sufficient evidence to confirm this. Further research is therefore recommended.

Limitations and recommendation for future research

There are several limitations in this study. First, the time sequence of the association between the variables could not be concluded given that cross-sectional data were used. A future study is suggested to conduct a longitudinal research design to present the evidence of causation which cannot be achieved through cross-sectional designs. Second, this study was limited to telecommunication firms in Kenya. Hence the findings and conclusions drawn from this research are representative of the Kenyan context only. Generalization of the final results should therefore be considered with caution.Thirdly, the regression analysis employed in the study focused on the combined effect of transformational leadership as well as organizational rewards on firm performance without isolating the individual attributes of each of the variables of the study. Future research may therefore focus on the effect each of the sub-constructs of the variables in this study. Future research may also categorize firm measures performance into financial and non financial measures to study a similar relationship.

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