

# The Impact of Transformation Leadership on the Performance of Small and Medium Enterprises in United Arab Emirates

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## Abstract

In today's business world, Small and Medium Enterprises (SMEs) are the source of development in the national economy. The globalization and the tough competition in the domestic and international markets motivate SMEs to adopt transformational leadership in their mission because of the significant traits of those leaders such as idealized influence, inspirational motivation, intellectual stimulation, and individualized consideration. In recent decades, the United Arab Emirates (UAE) focused on SMEs to achieve economic growth. Transformational leaders have the ability to foster the performance of SMEs. But adopting transformational leadership is not an easy task and require in-depth analysis to recognize the necessary factors that ease the adoption of transformational leadership by SMEs. Hence, the aim of this study is to examine the impact of transformational leadership on business performance of SMEs. Quantitative methods have been used to measure and evaluate this relationship. The respondents are the executive managers of SMEs working in various sector like information and communication, manufacturing, education, financial and insurance, professional scientific and technical. The sample of 441 SMEs was specified for the data analysis. The empirical results revealed that transformational leadership has a significant effect on SME performance. Thereby, SMEs should emphasize on the reality that transformational leaders are the pillar of success in a country rely on innovation and technology to develop all sectors and faces of life. Moreover, SMEs should focus on those leaders who have the personal characteristics such as idealized influence, inspirational motivation, intellectual stimulation, and individualized consideration to foster the organizational performance in the domestic market.

**Keywords:** *Transformational Leadership, Business Performance, Small and Medium Enterprises (SMEs)*

## 1 Introduction

Small and Medium Enterprises (SMEs) are the source of growth in the national economy in the business world (Abdul-Mohsin 2020). Small and medium-sized enterprises (SMEs) have become significant assets for a wide number of countries, and they represent a dynamic component of the global economy (Ali et al. 2021). This is a result of globalization and fierce rivalry in domestic markets. To boost company performance, SMEs must be able to make a substantial difference by implementing innovative business models and relying on employees' ingenuity. While the dynamic business climate has increased competition for SMEs, SMEs' leaders should focus on creativity and innovation to improve company and achieve productivity growth (Qalati et al. 2020). The UAE is making significant efforts and investments to strengthen its innovation capabilities across its many institutions in order to address the requirements of its population (Abdulqader and Al Marri 2020). As a result, SMEs must be innovative in all aspects of their operations in order to meet the needs of customers who are becoming increasingly sophisticated in their choices of products and services (Fitriati et al. 2020; Gherghina et al. 2020). Furthermore, in today's competitive market, small businesses should concentrate on success elements that attract clients. However, without a transformational leader with the personal attributes to inspire staff innovation and motivate people to be creative, high levels of performance may be impossible to accomplish (Lopes et al. 2017).

As a result, in order to compete with client demand, a SME must deal with creative concerns and innovative solutions to the complicated challenges that every firm may confront (Liao and Tsai 2019). In such a case, a SME should use transformational leadership, which is based on the creativity of its employees, who are the intellectual assets of any organization (Mishra et al. 2018). Globally, SMEs account for more than 90% of all enterprises; this proportion accounts for a significant amount of the gross domestic product (GDP) of many developing countries (Ogundana et al. 2017). Whereas the UAE is one of the fastest developing countries, the government in this country must focus on the competitive advantages provided by SMEs, allowing them to access larger markets and allowing for their growth and sustainability (Dutot et al. 2014), as well as improve globalization of SMEs and support various types of mechanisms, such as knowledge sharing, collaboration, and innovation (Costa et al. 2020). By depending on innovative methods and successful leadership styles, SMEs may be able to get a competitive advantage in the market (Cao and Yu 2019). As a result, it is critical to investigate the factors that promote SME performance, such as leadership, innovation, and creativity (Halim et al. 2019). SMEs may have limited resources, but in this day and age, they have a fantastic opportunity to use innovation and tools such as social media as free platforms to improve their company. Numerous studies have demonstrated that innovation has a favorable impact on the success of SMEs (Ahmad et al. 2019).

Understanding the complexities of SMEs, their operations, and the challenges that CEOs encounter on a daily basis is crucial. In addition, rather of fighting with larger-scale competitors, SMEs partner with them. Indeed, there are several examples of how tiny enterprises may help larger businesses achieve considerable cost reductions and income that would otherwise be impossible. Furthermore, the issues of SMEs in the UAE business climate, particularly those linked with transformational leadership, must be investigated. The purpose of this research is to investigate the performance and leadership of SMEs in the UAE by surveying employees from various levels of SMEs.

## **2 Methodology**

This study utilized quantitative methods and regression analysis to test relationship between transformational leadership and business performance. The focus on SMEs in specific sectors, such as information and communication, education, manufacturing, financial, insurance, professional scientific and technical institutions. The total number of active SMEs working in these fields in Abu Dhabi = 11023. The population is executive and general managers. Stratified random sampling technique is used to sample a heterogeneous population. The data instrument is questionnaire. Out of the 500 questionnaires distributed to the study sample, 441 valid copies have been considered for the analysis.

## **3 Literature Review**

### **3.1 Small and medium-sized enterprises**

Small and medium-sized enterprises (SMEs) are seen as a significant engine of economic growth in terms of both employment and GDP (Edinburgh Group 2013). According to Tripathi (2019), SMEs contribute up to 60% of total employment and 40% of national income (GDP) in emerging nations, and this figure will rise if the informal sector is included. In addition, the World Bank anticipates that 600 million workers would be needed over the next 15 years, primarily in Asia and Sub-Saharan Africa. In many countries throughout the world, SMEs now account for a sizable portion of present employment and future growth opportunities. SMEs are a source of inspiration for potential entrepreneurs, providing employment for many creative people as well as a platform for testing new concepts and ideas (Abdullah 2018). To emphasize the importance of SMEs in job development, the World Bank (2015) estimated that 600 million jobs will be needed over the next 15 years, with SMEs accounting for the majority of jobs in emerging nations. In the 18 OECD countries, SMEs account for 63 percent of total jobs, with major enterprises accounting for the remaining 37 percent (International Labor Office 2015). As a result, SMEs are viewed as one of the most essential weapons for combatting poverty in many nations around the world. As a result, the World Bank, local governments, and other international relief groups have prioritized delivering targeted support to SMEs worldwide (Abdullah 2018). In 2012, for example, the 20 million European SMEs employed more than 86 million people (66.5%) and created 57.6 percent of the gross value added generated by the private and non-financial sectors (European Commission 2013). There is no universally accepted definition of a small business (Jones et al. 2013). Several definitions have been proposed. These definitions are frequently linked to the level of economic activity and development in the country (Brunswicker and Vanhaverbeke 2015). Some researchers examined capital assets, while others examined labor skills and turnover rates, the firm's legal status or mode of production, the number of employees, ownership, or industry sector (Cheng 2014). However, because SMEs are reluctant to disclose their revenue and profit, most academics define SME primarily on the number of employees (AlSharji et al. 2018). SME are businesses with earnings, property, or fewer than a specific number of employees (Zhou 2015). Each country has its own definition of what makes a small and medium-sized enterprise (SME).

In the UAE, SMEs are the foundation of the economy, and their success is critical to fostering economic progress (Hamdan 2019). The trading segment accounts for 47% of the overall value-add generated by the SME sector (Dubai SME 2015). According to a recent report in 2019 by the Dubai SME department, the contribution of SMEs to the economy in Dubai province is approximately 50 percent of Dubai's GDP, while SMEs contribute 52 percent of the total workforce. SMEs in Dubai also represent 99.2 percent of the total number of businesses in the entire territory of the UAE. As a result, study into the primary factors influencing the performance of SMEs in the UAE has expanded in recent years (Abdul Quddus 2019). Small and medium-sized enterprises (SMEs) in the UAE are categorised into three groups based on their industry of operation: commerce, manufacturing, and utility. For a business to be classified as a SME, many standards must be met. Manufacturing firms frequently have larger yearly revenue and staff counts than the ordinary trade or service organization. A small manufacturing firm has the same turnover rate as a large corporation but employs more people (10-100), but a small service firm employs fewer people (6-50) and has a lower turnover barrier of AED20 million. The medium-sized manufacturing industry employs up to 250 people and has a revenue of up to AED250 million. A medium-sized trade firm that employs 51-200 people and has a revenue of up to AED200 million meets the same criteria as a medium-sized service company that employs 51-200 people and has a revenue of up to AED200 million. All firms with fewer than ten employees or where the entrepreneur is the sole employee fall into the lowest category, micro enterprises. Because the aim of this study is the Abu Dhabi SMEs market, the SMEs definitions of Abu Dhabi are necessary to illustrate. A micro business in Abu Dhabi has fewer than five employees, whereas a small business has more than five but fewer than 19 employees. According to a regulation passed by the Abu Dhabi Executive Council, a medium-sized enterprise has 20 or more employees but less than 49. The Abu Dhabi SME definition, on the other hand, is more precise and differentiates between three categories: trading, manufacturing, and services. In the trading sector, for example, a micro business has nine or fewer employees and a turnover of AED 9 million or less. A micro SME in manufacturing, on the other hand, is one with 20 or fewer people with a turnover of less than AED 10 million. A micro business in the services sector is defined as one with 10 or less employees and a turnover of less than AED 3 million. The UAE SMEs criteria and the number of employees in each classification are shown in Table 1.

Table 1: Number of employees according to SME classification in Abu Dhabi

<b>Firm size</b>	<b>Trading sector</b>	<b>Manufacturing sector</b>	<b>Services Sector</b>
Micro	< 9 employees	< 20 employees	< 10 employees
Small	< 50 employees	< 100 employees	< 100 employees
Medium	< 250 employees	< 250 employees	< 250 employees

Investing in infrastructure and human resources can give SMEs a competitive advantage and greater performance; but, these elements will inevitably generate decreasing returns. The introduction of new technology and non-technological innovations is a critical source of SMEs' sustainability, competitive advantage, and efficiency (Price et al. 2013). Those with higher rates of innovation, according to Fagerberg et al. (2004), have higher rates of growth and income than countries with lower rates of innovation. As a result, studies of innovation, particularly in the context of SMEs, are crucial due to the unique set of processes and resources possessed by SMEs, as well as their roles in innovation adoption that result in enterprise sustainability and efficiency, as well as national growth (Anderson & Eshima 2011). Another significant component of this study is that it provides empirical support for path-dependence models, which have been often criticized for lacking empirical data (Abdullah 2018).

### 3.2 Transformational leadership.

Transformational leadership is based on innovation and teamwork in two ways: first, it can boost employee motivation (intrinsic) by stimulating creativity, which is the primary key to innovation (Shin and Zhou 2003), and second, it provides intellectual stimulation, encouraging employees to think "outside the box" (Elkins and Keller 2003). The world is changing and evolving at a breakneck pace. Change and change occur at such a rapid pace that firms that can keep up can continue to operate, while those that cannot keep up withdraw from commercial life and fail in business (Awaru 2015). As a result, ongoing innovation and development at all organizational levels are critical (Yilmaz and Comez 2020). A true leader should now be able to enhance followers' performance, instill confidence, make work vision plain and simple, and then direct them to achieve the vision and organizational goals (Chawla and Lenka 2015). As a result, the work of the transformative leader requires more than simply encouraging people. It suggests that the leader must be there and ready to convince and direct individuals before they can attain their objectives (Bass and Riggio 2006). A transformative leader inspires others to accomplish amazing results (Azizah 2016). Bass and Avolio (1997) established the widely accepted principle of transformational leadership, which consists of four behaviors performed by the leader. The interaction of these four elements motivates followers' professional traits. These four elements of transformational leadership or

transformational leader conduct are thus the structures in this study that characterize transformational leadership. The researchers proposed that organizational leaders pay close attention to the four components of transformational leadership style (idealized influences, intellectual stimulation, individualized consideration, and inspiring motivation) (Eyamba 2020). The idealized impact is the leader's ability to generate pride, faith, and respect (Sladjana 2017). Transformational leadership is a component of change, and idealized power consists of idealized attributes and idealized acts (Budur and Demir 2019). Transformational leadership is based on inspiring people and motivating them through transformative communication abilities that position the leader as an icon who inspires the followers (Prabowo et al. 2018). The degree to which a leader articulates a vision that is engaging and inspiring to personnel is referred to as inspirational motivation.

A transformational leader is even more concerned with individualized considerations (i.e., leaders are concerned with the desires of their followers and have training to assist them flourish in a collaborative work environment) (Prabowo et al. 2018). Leaders, on the other hand, inspire followers to think for themselves by fostering innovation and originality (Al-Sada et al., 2017). Furthermore, the other characteristics of a transformational leader are idealized influence and inspirational motives; with these characteristics, a leader's future objectives for the organization are always expressed, desirable, and concrete (Buil et al. 2019). To put it another way, such leaders are strong-willed, insistent, and consistently stress the attainment of their goal (Mohammed et al. 2020), as well as take on individual tasks and responsibilities, and demonstrate high ethical standards and actions in winning followers' trust (Summers 2015). According to Qistina and Khashini (2017) and Eyamba (2020), leadership elements such as idealized influence, inspirational motivation, customized concern, and intellectual stimulation turn and motivate followers. Previously, several research offered empirical data on the main qualities of transformational leadership. These four aspects of transformational leadership are discussed further below.

### **3.2.1 Idealized influence**

The idealized influence is the ability of the leader to elicit pride, faith and respect (Sladjana 2017). Transformational leadership is a part of transition and idealized power comprises idealized qualities and idealized actions (Budur and Demir 2019). The most evident idealized attributes of a leader are, among other aspects, inspiring the honor and pride of followers and their commitment to organization interests (Ali et al. 2020). Transformational leaders have certain traits, which influence the followers, such as praise, integrity, respect, and trust (Maskurochman et al. 2020).

### **3.2.2 Inspirational motivation**

Transformational leadership is built on inspiring people and motivation through transformative communication skills that present the leader as an icon which motivate the followers (Prabowo et al. 2018). Inspirational motivation is the degree to which a leader articulates the vision that is appealing and inspirational to employees. When transformational improvements are required in the organization, the leader shall inspire followers to embrace new values and make changes in doing the work continuously. Accordingly, transformation leaders can then act in a special way to inspire their followers (Boamah et al. 2017).

### **3.2.3 Intellectual stimulation**

The intellectual stimulation is the behavior of the leaders who develop the employees' ability and inclination to think about problems in a new way (Sladjana 2017). Caspi and Roccas (2013) figured out that intellectual stimulation achieves leaders with groundbreaking artistic judgment already in the hands of the followers by implementing fresh techniques with a new perspective (Bass and Riggio 2006). The basic feature of intellectual stimulation of transformational leaders is enabling the followers to solve problems associated with the work; those leaders appear to be more knowledgeable regarding the dealing with work challenges.

### **3.2.4 Individualized consideration**

Individual consideration refers to paying attention to each employee, or dealing with his/her specific problems. This trait indicates the degree in which a leader considers individual problems and listens to them as well as provides support individually to fulfil followers' requirements (Bass and Avolio 1994). It is the behavior of the leader considering every individual as a part of the team, valued them, showing support to them.

Bass and Riggio (2006) concluded that individualized consideration is an essential element in transformational leadership in which the leaders provide employees with a clear picture or vision of the future inspire them and provide them with the necessary support and help in their facing the challenges of change. Thereby increasing employees' commitment to execute tasks more efficiently (Suifan and Al-Janini 2017; Sladjana 2017).

### 3.3 SME Performance

The extent to which an organization has completed all of its major actions in order to achieve its vision and mission. It is determined by sales growth, profitability, and market share (Fitriati et al. 2020). In academic literature, the term "performance" refers to the outcomes of a company's business actions. The concept of performance has multiple interpretations due to its all-encompassing character and tremendous popularity as a normal speech phrase (Inta and Irina 2017). Business performance is a crucial variable of interest to management scholars across the board, as businesses may only achieve and expand at the expense of productivity (Bhola 2015). According to Wheelen and Hunger (2010), business performance demonstrates how an organization combines material and immaterial resources to fulfill its objectives. It is the climax of an organization's work. Many business scholars used financial variables to assess performance (Al-Matari et al. 2014; Bianchi 2015). While profitability is one of the most important markers of a company's performance (Qistina and Devi 2017). Business performance is a multidimensional variable with multiple explanatory aspects or metrics (Yunoh and Ali 2015; Maduekwe and Kamala 2016; Mishra and Misra 2017; Claudiu et al. 2019).

In principle, the concept of performance lies at the heart of strategic management, and empirically, most strategy studies use the construct of business performance to investigate various strategy content and process difficulties. The importance of performance in management is obvious from the numerous prescriptions for performance enhancement. According to a review of the literature, business performance can be judged when a company achieves their goals with few resources, indicating an efficacy in employing organizational resources to achieve targeted profits. In this regard, Almatrooshi et al. (2016) proposed that an organization's performance is related to the effectiveness of all organizational functions in relation to its objectives. However, inability to manage organizational resources may have an impact on corporate performance and, in the end, lead to business collapse. A business failure could be caused by a number of things. Inability to generate long-term business planning, ineffective advertising/promotional strategy, lack of technological innovation, lack of managerial experience, skills, and training, failure to generate an online business plan, lack of experience in the product line, lack of marketing knowledge, and an ineffective online store are all factors that can lead to business failure and poor performance (Tsai 2015).

SMEs' business performance may be judged in two ways: business growth and company profitability. These two characteristics are frequently used as a broad indicator of SMEs' organizational success in the UAE. These two aspects are discussed further below. Profitability is the amount of profit or money that a company can earn with its restricted resources. The bulk of organizations exist to improve profitability (Azhar and Ahmad 2019). All management and planning efforts are aimed at increasing profitability (West 2018). Firms that are more profitable can theoretically readily expand their size of operation through internal funding. However, the financing process is not as straightforward as it appears. The performance of SMEs can be understood quantitatively using metrics such as profitability (Claudiu et al. 2019). As a result, in order to boost the company's performance even further, the management should develop a strategy for expanding profitability while focusing on productivity and industry affiliation (Farah and Nina 2016). The second dimension is business expansion. The literature on growth as a measure of company performance has shown conflicting conclusions. Firms expand in a variety of ways, and the growth pattern of a firm is related to its age, size, and industry. According to Delmar et al. (2003), one probable explanation is that researchers employ diverse metrics of growth and that growth is heterogeneous in nature. Growing SMEs have been identified as the economic backbone. Governments in all developing countries are emphasizing the expansion of SMEs in many areas in order to acquire the status of developed or high-income nations (Shehnaz and Sulaiman 2017). According to the findings of several studies, financial capital acquired by SMEs has a favorable impact on business growth. Access to financial resources is more important for company expansion during economic recovery (Ullah 2020; Cowling et al. 2018). SME public incentives have a favorable impact on sales and production growth, particularly for small enterprises (Bann et al. 2014).

## 4 Results and Discussion

Transformational leadership is vital in the development of performance in SME context (Knezovi and Drki 2021). Several empirical research has shown that transformational leadership improves organizational performance (Cheng 2014; Ebrahimi et al. 2016; Ariyani and Hidayati 2018), while others have confirmed that transformational leadership results in broader change among SMEs by improving their performance (Flanigan et al. 2017; Nungky et al. 2020). A review of the research reveals that transformational leadership is associated with SME performance from a variety of perspectives, owing to its good effects on individuals (Tareq 2016). As a result, transformational leadership has received a lot of attention in the literature on performance development. In other words, it is proposed that transformational leadership has a direct impact on SME performance; this premise is supported by past research discussed in the following sections. Based on empirical data and previous research findings. This research assumes that transformative leadership and SME performance are related. This association suggests that

transformational leadership has a direct and significant impact on SME performance. According to this assumption, this study will examine the following hypothesis statement:

***“Transformational leadership has a significance effect on SME business performance”***

To justify the hypotheses of this study, the Critical Ratio (C.R) is applied to validate each hypothesis as well as determining significance level of unstandardized regression coefficients (Hair et al. 2010). The following two principles are used to validate the hypotheses (accept or reject) (Chen et al. 2010; Byrne 2013). However, if  $C.R \geq 1.96$ , a hypothesis is true, otherwise the hypothesis will be rejected and accept the null-hypothesis. The estimate path coefficient for a particular relationship should be significant at 0.05 cut-off point (Gao et al. 2008). Accordingly, the degree of association between transformational leadership and SME performance will be considered acceptable if  $C.R \geq 1.96$  and  $Sig. \leq 0.05$ . Therefore, the relationships between these two constructs are not based on probability but on statistical evidence (Garson 2007). The analysis of regression analysis reveal that the direct relationships between these two constructs (transformational leadership & SME performance) is significant and positive. Based on this results, it is concluded this hypothesis is accepted and not rejected. While, the opposites hypotheses are rejected (Null-Hypotheses).

## 5 Conclusions

The result of this study will help the general managers and executive managers in SMEs located in Abu Dhabi to understand why the traits of transformational leaders (i.e. idealized influence, inspirational motivation, intellectual stimulation, and individualized consideration) have a direct impact on fostering the business growth and profitability of small and medium business projects. Through in-depth literature review, this study found empirical evidences supporting the significant relationships between the transformational leadership, SME performance. Several theoretical contributions to the topic of transformational leadership in particular and organizational performance has been achieved in this research. It seems that the potential for innovation lies within reach of business managers, also it is assumed in this research that transformation leaders always encourage the adoption of followers to adopt innovation in all activities in the work and marketing. Whereas the financial resources are not enough to achieve growth in the market and sustainable profitability, the role of leaders could make a dramatic change to the organizational performance.

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