

# JOURNAL OF SMALL BUSINESS **STRATEGY**

## EMPLOYEE RETENTION IN GROWTH-ORIENTED ENTREPRENEURIAL FIRMS: AN EXPLORATORY STUDY

Bruce H. Kemelgor  
University of Louisville  
Bhkeme01@louisville.edu

William R. Meek  
University of Louisville  
bill.meek@louisville.edu

### ABSTRACT

*This study uses a sample of 47 high-growth small firms to examine the understudied topic of employee retention. We found that firms reporting very low annual voluntary turnover (0-2%) rates engaged in creating a positive work environment, provided employees more freedom and flexibility, offered ample employee involvement and opportunities for growth; were clear about the processes associated with compensation and benefits, and frequently communicated with and provided assistance to their employees. Firms reporting turnover higher than 10% for the past year described their retention practices in much diminished frequency and richness along these same dimensions. Given that these firms were all part of a pool of 77 high growth small companies (over \$1 million annual revenue, less than 12 years old and compound annual growth greater than 15%), retention of intellectual capital would be a prime issue. Industry differences among the companies are explored and theoretical and practical implications are discussed.*

### INTRODUCTION

A recent edition of *Entrepreneur* magazine stated that the retention of key employees is the biggest problem facing entrepreneurial companies (*Entrepreneur*, 2006). With today's increasingly competitive global economy, the retention of intellectual capital would appear to be a prime issue for entrepreneurial companies around the world, yet it remains understudied in both the Human Resource (HR) and entrepreneurship literature (Hayton, 2003; Hornsby and Kuratko, 2003). Cardon and Stevens (2004) suggest retention is the most overlooked factor in growth-oriented firms besides organizational culture. As scholars, we are beginning to understand how to hire, pay, and perhaps even motivate workers in small growth-oriented firms. However, there is little theory or data concerning issues of

retention within evolving organizations. Thus, this study seeks answers to the research question: "What HR practices appear to have positive employee retention results among growth-oriented entrepreneurial firms?" This is important because, to date, very few studies look at factors influencing employee retention in entrepreneurial firms, although "few imperatives are more vital to the success of young companies than retaining key personnel" (Baron and Hannan, 2002, 21). Evolutionary economic theory (Nelson and Winter, 1982) and the accompanying work on strategic management of intellectual capital (Winter, 1998) provide a theoretical foundation for the importance of employee retention in young firms. Nelson and Winter's focal point is that organizations and accompanying organizational performance are simply a reflection of deeply engrained

repertoires, norms, and routines. Winter further elaborates that these knowledge processes are the defining characteristics of an organization and these routines are a reflection of how an organization really functions and turns knowledge into organizational memory (Winter, 1998). Organizational memory within a new firm is developed from the constant repetition of activities within an organization and related codifications into rules and procedures that allow for the lessons of experience to be retained and accumulated over time in routines (Nelson and Winter, 1982). Thus, organizational memory and the accompanying routines are often the way in which knowledge is exercised in a firm. Yet, in small, fast-growing firms the organizational memory and routines may not be explicitly codified or recorded, but simply reside in the knowledge structures of the current employees. Therefore, these individuals are often the key resource for valuable ideas to bundle knowledge and resources to create incremental innovations (Ireland and Webb, 2007). Retaining these individuals is a key requirement for maintaining sustainable growth and remaining competitive. The potential loss of organizational memory through employee turnover is a major impediment for newer firms. While voluntary employee turnover is good for established firms because it disrupts the existing patterns of communication and brings new knowledge, it is bad for new firms because individual employees take knowledge with them that is not yet part of the norms and routines of the firm (Aldrich, 1999).

Scholarship focusing on the retention issue to which scant attention has been paid would shed light on what draws and keeps employees engaged as well as what drives their performance (Cardon and Stevens, 2004; Rutherford, Buller, and McMullen, 2003). Another important facet of this research study is its attention to some of the weaknesses of other retention studies. Heneman and Tansky (2002) suggest that simply extending existing retention models from large firms to small emerging firms would not be meaningful, since it has not worked well to extend other HR practices from large firms to small ones (Barber,

Wesson, Roberson, and Taylor, 1999). Instead, we should develop HR theories such as those dealing with retention that are specific to small growth-oriented firms and their strategic practices (Heneman and Tansky, 2002). Further, we follow the suggestion of Heneman and Tansky (2003) to address gaps in the literature by conducting descriptive surveys of practices and developing new data sets that are designed to test specific hypotheses and theory. This article adds to the literature by specifically examining the frequency and extent of retention practices that high-growth entrepreneurial firms utilize.

In following the above prescriptions, it has been noted that in many small emerging firms, founders do not think about HR issues as distinctly different from other issues in the firm, but rather as a flow of interrelated activities that change and fluctuate over time that they deal with concerning their employees (Cardon and Stevens, 2004). We used the most widely used definition of small business – the one specified by the Small Business Administration (e.g., Peterson, Albaum, and Kozmetzky, 1996; Stewart, Watson, Carland, and Carland, 1999) – that generally classifies a firm as small if it has less than 500 employees. In applying the “muddle through” approach, many of these founders/managers probably stumble upon ways to manage and retain personnel that do not fit into our traditional notions about HR. Therefore, data should be gathered concerning what these founders/managers are actually doing and the impact of those activities on employee retention. Aldrich (1999) points out that we know very little about how HR evolves in firms until those firms reach older stages of growth and have become medium or large in size. Looking at both informal as well as formal mechanisms through which small growth-oriented firms manage employee retention issues while continuing to address growth, would provide a more practical and theoretical view focused upon such firms and how their retention practices develop.

Therefore, we first examine what we know about employee retention. Then we summarize relevant retention factors which lead to the creation of testable hypotheses.

Finally, we report results and discuss implications for both theory and practice.

### **The Cost of Poor Employee Retention Practices**

Several studies suggest that the total cost of voluntary employee turnover (i.e., voluntary quits) varies between 150% (Ramlall, 2003) to 250% (Henricks, 2006) of the employee's annual salary. This includes all of the recruitment and training costs, not to mention the public perception of the company, employee morale and productivity, and many other factors. Of course, the more talent a person brings to the company, the more expensive that person is to replace. This may be especially true for high growth entrepreneurial companies where intellectual capital is often *the* competitive advantage (Becker and Gerhart, 1996; Delaney and Huselid, 1996; Hayton, 2003). And the pressure to keep key employees is even greater for small companies because they usually can't offer the same amount of salary, benefits, or opportunities for advancement that are available in large companies (Henricks, 2006).

Losing even one key employee engenders far-reaching consequences and, at the extreme, may jeopardize efforts to attain organizational objectives. Small, growth-oriented firms are especially vulnerable. Frazee (1996) reported on a study of 434 CEOs of fast growth companies and found that 47% said their lack of skilled workers was a barrier to their companies' growth. If we consider that entrepreneurial companies seek to grow and capture market share, employee retention becomes a critical human capital objective.

### **RETENTION FACTORS**

Most employees come to expect salaries and benefits and are therefore not motivated by them (Henricks, 2006; Smither, 2003). Key elements in helping make any company a good place to work include: being treated fairly, flexible hours, opportunities for meaningful contributions, opportunities for growth and skill development, a positive work environment and culture, and frequent management feedback (Arthur, 2001; Dibble, 1999; Glanz, 2002; McKeown, 2002; Rye,

2002). The aforementioned elements thus provided the basis for the construction and development of our survey assessment instrument. As small, growth-oriented organizations evolve and pursue sustainability, many of these key elements appear relevant in providing an attractive work environment. However, Heneman and Tansky (2002) offer evidence suggesting that small firms have strategic human resource issues which are different than those of large firms. Small firms also cannot afford to have a separate human resource department or personnel exclusively devoted to addressing these issues (Cook, 1999), thus leaving responsibility to the owner or manager. Additionally, many small firms do not make explicit formal HR procedures (such as an employee handbook) that are often standard in large organizations (Aldrich and Langton, 1997). With so many challenges associated with managing the business to address human resource issues are often pushed to the end of the priority list or do not appear there at all (MacMahon and Murphy, 1999). We now discuss each of these retention factors and their perceived importance to employee retention within small, growth-oriented firms.

### **Positive Work Environment**

This factor is associated with the organization's culture and practices of valuing employees as an asset, not a cost. Companies that actively promote a positive work environment, and who also value employee contributions while achieving a true work-life balance have been found to be more successful at communicating the idea that their employees are one of their most valuable resources (Hom and Kinicki, 2001; McGrath, 2006; Mitchell, Holtom, Lee, Sablinski, Erez, 2001). Others have suggested the aspects of the workplace as being enjoyable or fun, the organization being a special place to work, and the firm regarded as an employer of choice (Butler and Waldroop, 1999; Kristof, 1996; Saks and Ashforth, 1997). Taken together, these dynamics, if positive, portray a workplace that values its people and their talents. This leads us to the following hypothesis:

**H1:** Companies that display greater characteristics of a positive work environment will have higher employee retention than companies that display fewer characteristics of a positive work environment.

### **Freedom & Flexibility**

In growth-oriented entrepreneurial firms, there is a high dependence upon most employees to be multi-skilled and exhibit some flexibility in both skills and scheduling. Thus, in the recruitment of these employees it becomes necessary to present a realistic job preview that addresses many of the roles they will be expected to fulfill and the level of freedom they will have in conducting these roles. Most people seeking to work in a start-up or small entrepreneurial firm are often attracted to it for these varied role opportunities (Kickul, 2001). In addition, providing opportunities for employees to showcase special talents by working on interesting or meaningful projects is often seen as an essential attraction that small firms can provide (Mitchell et al, 2001). This leads us to the second hypothesis:

**H2:** Companies that offer higher levels of flexibility and freedom will have higher levels of employee retention than companies that offer lower levels of employee flexibility and freedom.

### **Employee Communication & Assistance**

Apparently, one of the most important factors associated with employee commitment to a firm is the extent to which clear and frequent performance feedback is provided. High performing employees are especially interested in receiving frequent, specific feedback (Prewitt, 1999; Smither, 1999). Recent research on employee commitment and the likelihood of staying with the firm indicate a strong positive relationship (Kickul, 2001; Payne and Huffman, 2005). In an entrepreneurial firm, it is likely that the environment is marked by turbulence and changing objectives (Hayton, 2003). Thus, it seems logical to assume that a need exists for clear communication of expectations along with frequent feedback. Finally, adequate help and support to

complete job assignments have consistently been cited as important to job satisfaction. This leads us to the next hypothesis:

**H3:** Companies that provide frequent feedback and clear expectations will have higher levels of employee retention than companies that provide infrequent feedback and unclear expectations.

### **Employee Involvement & Growth**

One of the frequently cited reasons for working in a large company is the clear path for career advancement and growth. Smaller, entrepreneurial companies simply lack varied career ladders. Employees seek to enhance their skills and increase their earning potential, whether the firm is large or small. If the entrepreneurial firm can provide such things as training, mentoring relative to career goals, and growth through employee empowerment the likelihood of their employees remaining loyal is significantly increased (Delaney and Huselid, 1996; Payne and Huffman, 2005). Loyalty, or organizational commitment, is the relative strength of the individual's identification with and involvement in a particular organization (Mak and Sockel, 2001). Individuals exhibiting loyalty are not prone to leave (Mitchell et al, 2001). One aspect of enhancing loyalty is providing the employees a stake in decision-making and the freedom to communicate throughout the organization. Additionally, some people are now setting career paths based on their own values and definitions of success, thus redesigning how they contribute to their prospective organizations on their own terms (McGrath, 2006). This leads us to the fourth hypothesis:

**H4:** Companies that offer greater options for employee involvement and growth will have higher levels of employee retention than companies that offer lower or fewer options for employee involvement and growth.

### **Compensation & Benefits**

A recent article in *Harvard Business Review* discussed the findings of two nationwide studies. The results indicate that of numerous

factors associated with keeping good employees, pay was the least significant factor – money is not a prime motivator (Prewitt, 1999). This is not to suggest that pay, or good benefits are not important – they are. It is just that good pay and benefits are expected and are readily available in our society (Prewitt, 1999). What seems more important than pay or benefits, per se, is awareness of how such rewards are calculated or determined (Mulvey, LeBlanc, Heneman, and McInerney, 2002). Knowledge about compensation and benefit options impact retention. In particular, employees are more likely to remain with an organization when the rewards and actions necessary to earn rewards are well understood (Mitchell et al, 2001; Mulvey et al, 2002). Aside from pay, benefits have become an even more critical factor for retaining good employees (Henricks, 2006), especially for smaller firms. We could envision a scenario where the small, growth-oriented company is sacrificing the costs of benefits that match larger employers and taking the savings to reinvest in growth. This is where stock options frequently are applied in entrepreneurial firms. Imposing a traditional incentive program in an entrepreneurial venture may be the easiest thing to do, but the challenges inherent in working in a start-up or fast growth firm imply a new relational contract. In a new, growth oriented firm, traditional models (of compensation and rewards) are not embedded in a company history. Thus, the possibility exists that alternative views of what is fair and equitable in that context can emerge. This leads to the final hypothesis:

- H5:** Companies that offer well-defined and varied compensation and benefits programs will have higher levels of employee retention than companies with unclear procedures or limited options regarding compensation and benefits.

## **METHODOLOGY**

### **Sample**

The local Chamber of Commerce of a Midwestern (U.S.) city of just over one million people provides support and mentoring for small firms they have

identified as fast-growth. Presently, 77 such firms are part of this portfolio. The firms range in age from just over 18 months to 12 years, with the vast majority between 4 and 8 years in business. These firms have exhibited compound growth rates of at least 15% annually and at least \$1 million in revenue each year. Sample firms were contacted using a multiple method format. A presentation was given at a meeting comprised of founders/CEOs of the fast growth firms announcing the launch of the retention study. The firms were then sent an e-mail inviting participation together with a link to an on-line survey instrument. Following Dillman's (2000) multiple contact approach, all firms were contacted by e-mail after two weeks and asked to participate if the survey had not been completed. After 1 month, firms were then called and the founder/CEO reminded to complete the survey if they had not already done so. Of the 77 companies that were invited to participate, 47 completed the web-based survey, resulting in a response rate of 61%. In almost all cases, company founders or one of the founding team members completed the survey instrument. In the few remaining cases, a CEO who was hired to manage the firm responded to our request.

Based upon the self-report of describing their company in 10 words or less, various industry profiles emerged among these fast-growth companies. Using just the brief descriptions, two senior members of the Chamber of Commerce who had working knowledge of the companies helped the authors sort the responses into industry groups. The five resultant groups are (number of firms in parenthesis): manufacturing (11); biomedical (8); information technology (12); consulting and related services (9); and service (7).

### **Research Instrument**

The survey instrument was designed after conducting relevant literature reviews and an assessment of some existing instruments (e.g., Arthur, 2001; Dibble, 1999; Glanz, 2002). Additional input was derived by holding interviews with three top executives of a world-wide human resource consulting firm. The 21 survey items plus five

additional firm-specific items (age of firm, size of firm, years in operation, respondent's position with the firm, and specification as to the voluntary turnover during the past 12 months) were then compiled and a follow-up evaluation was held through a pilot test of 14 firms owners. The results of this pilot test indicated the items measure the concepts they are intended to measure. Additionally, although none of the previous survey instruments (Arthur, 2001; Dibble, 1999; Glanz, 2002) reported reliability measures, we found reliability levels that were all quite acceptable. The factor we labeled positive work environment had a Cronbach's alpha of .83. The employee freedom and flexibility factor and the employee involvement and growth factors each displayed a Cronbach's alpha of .72 while the employee communication and assistance factor indicated a Cronbach's alpha of .73. Finally, because the compensation and benefits factor included only two items, a measure of reliability was not possible. However, the correlation between the two items (.62) was significant at the .01 level, suggesting a strong relationship between these two items. The 21 survey items were measured using a Likert scale from 1 (not at all), 2 (slightly), 3 (somewhat), 4 (quite a bit), and 5 (significantly).

## **RESULTS**

An analysis of the 47 companies revealed the following information. Thirteen firms exhibited the highest levels of employee retention (lowest turnover) at 0 to 2% annual employee turnover. Another six firms displayed turnover rates of 3-5% annually. Eight firms displayed turnover rates from 6-8% annually. Six firms displayed annual turnover rates of 9-10% and thirteen firms displayed turnover rates greater than 10% annually (the lowest level of retention in our survey). Based on this distribution we chose to compare the 13 companies with the highest retention rate to the 13 companies with the lowest retention rate to determine if significant differences exist between the two groups' retention practices.

T- tests were used to measure whether there was a significant difference between the very high retention group and the very low

retention group. T-tests are a useful tool for understanding whether a difference exists between two groups in social science research. Table 1 provides the t-values and significance levels of all the variables compared in our study. These variables include questions from each of the clusters in our study: creation of a positive work environment, employee freedom and flexibility, employee involvement and growth, employee communication/assistance, and employee compensation and benefits. A total of 21 items comprise this data pool. Five additional items were open-ended responses, seeking input relative to specific employee practices (e.g., how does the company demonstrate it trusts its employees?).

An examination of the t-tests shows that all values are greater than the required score of 1.96 in order to be significant at the .05 alpha level. A closer look shows that all of the variables are significant at the .001 level as well.

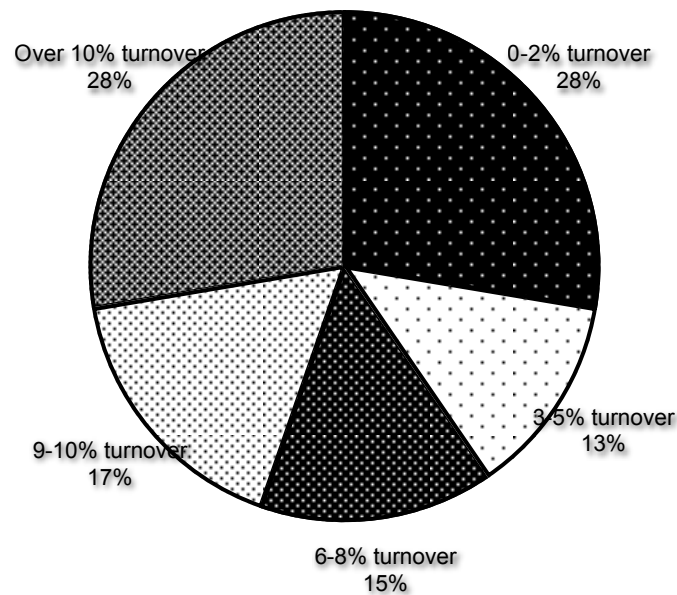
The first hypothesis (H1) predicted a higher level of employee retention for firms that create a more positive work environment. This hypothesis was supported. The six items reflecting a positive work environment were all significant. These items and their associated significance levels and t-scores are presented in Table 1. This implies that there are statistically significant differences in the practices associated with positive work environments in the high retention companies versus the practices in low retention companies.

Hypothesis 2 predicted a higher level of employee retention for firms that offer higher levels of employee flexibility and freedom. This hypothesis was supported. The five items reflecting the level of employee flexibility and freedom were all significant. These items and their associated significance levels and t-scores are presented in Table 1. This implies that there are statistically significant differences in the extent of employee flexibility and freedom in the high retention companies versus the low retention companies.

**Table 1. Factors of retention, T-scores, degrees of freedom (df), and significance levels of highest retention versus lowest retention companies in the sample<sup>1</sup>**

<b>Factors</b>	<b>t-scores</b>	<b>df</b>	<b>Significance</b>
<b>Positive Work Environment (Alpha (<math>\alpha</math>) = .83)</b>			
1. Actively promote positive work environment	35.560	25	.001
2. Insure the workplace is fun and enjoyable	19.000	24	.001
3. Employees know why this is a special company	22.437	24	.001
4. Strive to be an employer of choice	23.645	25	.001
5. Offer a sincere work/life balance	19.403	25	.001
6. Value employee contributions	29.439	25	.001
<b>Employee Freedom &amp; Flexibility (Alpha (<math>\alpha</math>) = .72)</b>			
1. Offer meaningful work for employees	21.755	25	.001
2. Provide freedom to work on/choose interesting projects	15.000	24	.001
3. Opportunity for employees to showcase talents	20.540	25	.001
4. Offer employees flexible work schedules	15.218	25	.001
5. Stock options offered as part of compensation	8.597	25	.001
<b>Employee Involvement and Growth (Alpha (<math>\alpha</math>) = .72)</b>			
1. Encourage using a variety of communication channels	19.114	24	.001
2. Insure employees involved in relevant decision making	27.979	25	.001
3. Help employees develop career goals	13.874	25	.001
4. Employee empowerment/freedom to do job	35.058	25	.001
5. Paths to Promotion are clearly defined	16.481	25	.001
<b>Employee Communication/Assistance (Alpha (<math>\alpha</math>) = .73)</b>			
1. Managers & leaders make work expectations clear	20.482	25	.001
2. Frequency of managers feedback	25.456	24	.001
3. Provide employees adequate help and support	27.933	25	.001
<b>Compensation &amp; Benefits (Correlation = .62**)</b>			
1. Employees understand how compensation is calculated	17.000	24	.001
2. Fair treatment/respect of employees	47.434	25	.001

Figure 1. Annual Turnover of Growth-Oriented Firms



Hypothesis 3 predicted a higher level of employee retention for firms that offer more frequent performance feedback and clear expectations. This hypothesis was supported. The three items reflecting the level of performance management/feedback were all significant. These items and their associated significance levels and t-scores are presented in Table 1. This implies that there are statistically significant differences in the practice of performance management and frequency of feedback in the high retention companies versus the low retention companies.

Hypothesis 4 predicted a higher level of employee retention for firms that offer options for employee involvement and growth. This hypothesis was supported. The five items reflecting the level of employee involvement and growth were all significant. These items and their associated significance levels and t-scores are presented in Table 1. This implies that there are statistically significant differences in employee involvement and growth in the high retention companies versus the low retention companies.

Hypothesis 5 predicted a higher level of employee retention for firms that offer well defined and varied employee compensation and benefits programs. This hypothesis was also supported. The two items reflecting well-defined and varied programs regarding employee compensation and benefits were all significant. These items and their associated significance levels and t-scores are presented in Table 1. This implies that there are statistically significant differences in the level of knowledge about and quality of the employee compensation and benefits in the high retention companies versus the low retention companies. This category also included two items that asked for open-ended responses regarding benefits and perks that are part of the company's practices. Analysis is currently underway to examine specific activities and their effect upon retention within this sample.

#### Industry Differences

Table 2 shows the differences in turnover rates among industries. In analyzing the 47 firms, the authors refrained from making conclusions about industry differences because the sample size for each industry is small. Once the authors have gained a



**Table 2. Industry Breakdown of Turnover Responses**

Annual Turnover %	Consulting				
	Manufacturing	Biomedical Research	Information technology	& Related Services	Service & Other
0-2%	3	2	3	2	3
3-5%	1	2	0	3	0
6-8%	2	0	4	0	1
9-10%	0	3	3	1	1
over 10%	5	1	2	3	2
<b>Total # of firms/industry</b>	<b>11</b>	<b>8</b>	<b>12</b>	<b>9</b>	<b>7</b>
Local Unemployment rate	8.67%	1.36%	3.16%	2.88%	4.24%

substantial number of firms in each industry, positing some potential explanations for industry differences should be feasible. However, we felt it was necessary to briefly discuss the numbers in each industry, including the unemployment rate, to provide some initial clues about the nature of the local industry. The unemployment rate for the entire Metropolitan Statistical Area (MSA) at the time of this study was 5.2%. This was slightly higher than the national unemployment rate of 4.5% at the time. With eleven firms out of 47 in the sample, manufacturing accounted for 23.4% of the total respondents. This industry also had the highest rate of unemployment in our sample at 8.67%. Eight of the 47 firms, or 17.02% in the sample, were in the biomedical research industry. The local unemployment rate in the biotech industry in the MSA was 1.36%, the lowest of all the industries in our sample. The sample also included 12 firms in the Information Technology (IT) industry, representing 25.53% of the sample. Unemployment rate in the IT industry was 3.16%. The consulting and related services industry accounted for nine of the 47 firms or 19.15% of the sample. The unemployment rate in the IT industry was 2.88%. The service industry accounted for seven of the 47 firms in the sample (14.59%) and had an unemployment rate of 4.24%.

**DISCUSSION**

The purpose of this study was to better understand employee retention practices in high-growth entrepreneurial firms. The key research question was – “What HR practices

appear to have positive employee retention results among growth-oriented entrepreneurial firms?”

Our sample provided a useful group of companies to begin exploring answers to this question. Because significant differences between the high retention and low retention groups were found for every single variable used in this study, we can infer that the high retention companies do a better job of promoting a positive work environment, providing employee flexibility and freedom, giving feedback about performance and expectations, ensuring employees understand the compensation process, and providing career development guidance. The results of this study suggest that the companies with the highest level of employee retention use certain employee retention practices to a greater extent than firms with the lowest levels of employee retention.

**Implications for Research**

This study used evolutionary economic theory and the associated work on the strategic management of intellectual capital to build support for the differential effect that using certain practices has on employee retention in growth-oriented entrepreneurial firms. Because support was advanced from this study that increased use of specific human resource practices to have a positive effect on the employee retention levels of growth-oriented firms, the field of human resources and entrepreneurship have moved one more step forward in deciphering the effects of one upon the other.

There are additional insights to be obtained from this data. First, one might argue that some of the variables suggest that companies achieving a good work-life balance for their employees are reaping the rewards in terms of high retention. Hom and Kinicki (2001) report on several studies that reinforce the importance of this issue upon retention. For example, they report that job interference with off-the-job roles activated withdrawal cognitions (Hom and Kinicki, 2001). At least one of the survey questions used in this study implicitly addresses this issue. Contained within the responses, yet not reported here, is an open-ended option asking respondents to describe various ways the companies embrace work-time flexibility. Our item regarding flexible work schedules embraces this as well and the results indicate there is a statistical difference between high retention and low retention firms in this regard.

A second issue to address concerns the role that changes in culture and structure within young firms have upon voluntary separation. Baron, Hannan, and Burton (2001) report that changes in the employment models or blueprints embraced by organizational leaders increase turnover, which in turn affects subsequent performance. It would be interesting to examine how many of these firms have undergone major structural or cultural changes recently, including those encompassing leadership at the top, to discover whether they reside in the high retention or low retention group.

### **Implications for Practice**

The practical implications of this study include the idea that firms who seek to retain their employees need to increase the extent to which they apply the practices outlined in Table 1. This is possible, as witnessed by the much higher annual employee retention rates of the firms in the highest retention group versus the lowest retention group in this sample. It may be possible for growth-oriented firms to increase their retention rates by ensuring that their employees are given the tools, guidance, and feedback necessary to work towards company goals. At the same time, employees need to be given the flexibility and freedom to showcase their special talents, work on

projects that are interesting to them, and be allowed to work toward their own personal career goals. If employees are given this freedom, they will know that the firm they are working for is a special company. Consequently, the firm's reputation as an employer of choice will improve and it may become easier for the firm to hire additional high quality employees to fuel their growth. Also, by decreasing turnover, companies can avoid the excessive costs that correspond with recruitment and training.

Significant implications for growth-oriented firms include these practices reinforcing the strategic implications of individual risk taking and experimentation, employee commitment, shared ownership, communication and learning – all especially important for firms operating in uncertain or dynamic markets (Hayton, 2003). Part of the strategic controls necessary within such firms embrace risks and potential trade-offs (Hayton, 2003), furthering the creation of a true learning organization. As knowledge becomes transferred throughout the organization, the discretionary initiatives and innovative culture essential for growth-oriented firms becomes strategically embedded. Hayton (2003) found that investments in employees are an important success factor for firms seeking to promote innovation and entrepreneurship. We believe that our data further proves the importance of certain practices relating to human capital as being necessary investments by the firm's management to encourage knowledge creation and exchange.

By employing these sound retention practices, firms can avoid the turbulence associated with lowered employee morale and productivity. Additionally, aside from the internal firm dynamics, the public perception of a company with low turnover is less likely to be damaged by dissatisfied former employees. As suggested by evolutionary economic theory (Nelson and Winter, 1982) and research on the strategic management of intellectual capital (Winter, 1998), perhaps the most important aspect for high growth entrepreneurial companies is not only the retention of human capital but also the retention of highly valuable intellectual

capital, which is often *the* competitive advantage.

### **Limitations and Future Research Directions**

We would be remiss if we did not acknowledge the study's shortcomings. The sample only tracked responses from high growth companies in one Midwestern city with a population of approximately one million people. Thus, our sample is not a representative sample of the general population of growth-oriented firms and our generalizability is limited. Additionally, although the sample was well-defined and had a very high response rate, a larger sample size could increase the statistical power of our study. Our future research will include a larger sample size from a more diverse geographic area. As an extension of this study, we plan to obtain responses regarding these retention practices from the employees of a sampling of firms used in this study.

Although the respondents were anonymous, we plan to seek voluntary association with a follow-up study that will provide each firm, data specific to it generated by its employees. The data, collectively, will be used for the follow-up macro-level research. This could help us better understand whether perceptions of HR practices are the same between management and employees, and would provide a more accurate description of whether or not the founders/CEOs were engaged in self-report bias while completing the survey. We could also collect longitudinal data from these same firms to determine whether changes in their retention practices continue to have an impact on their annual retention rate over time. Finally, an interesting comparative study would be between firms that have both a domestic and an international location, and the extent to which firm-specific practices affect retention practices across cultures.

### **REFERENCES**

- Aldrich, H. (1999). *Organizations Evolving*. London: Sage.
- Aldrich, H. & Langton, N. (1997). Human resource management practices and organizational life cycles. *Frontiers of Entrepreneurship Research*. Wellesley, MA: Babson College Center for Entrepreneurship.
- Arthur, D. (2001). *The Employee Recruitment and Retention Handbook*. New York: American Management Association.
- Barber, A.E., Wesson, M.J., Roberson, Q.M., & Taylor, M.S. (1999). A tale of two job markets: Organizational size and its effects on hiring practices and job search behavior. *Personnel Psychology*, 52: 841–867.
- Baron, J.N., Hannan, M., & Burton, M.D. (2001). Labor pains: Change in organizational models and employee turnover in young, high-tech firms. *American Journal of Sociology*, 106(4): 960–1013.
- Baron, J.N. & Hannan, M. (2002). Organizational blueprints for success in high-tech start-ups: Lessons from the Stanford project on emerging companies. *California Management Review*, 44(3): 8–36.
- Becker, B. & Gerhart, B. (1996). The impact of human resource management on organizational performance: Progress and prospects. *Academy of Management Journal*, 39(4): 779–801.
- Butler, T. & Waldroop, J. (1999) Job Sculpting: The Art of Retaining Your Best People. *Harvard Business Review*, 77(5): 101–109.
- Cardon, M.S. & Stevens, C.E. (2004). Managing human resources in small organizations: What do we know? *Human Resource Management Review*, 14: 295–323.
- Cook, M.F. (1999). *Outsourcing Human Resource Functions*. New York: American Management Association.
- Delaney, J.T. and Huselid, M.A. (1996). The impact of human resource management practices on perceptions of organizational performance. *Academy of Management Journal*, 39(4): 949–969.

- Dibble, S. (1999). *Keeping Your Valuable Employees: Retention Strategies for Your Most Important Resource*. New York: Wiley.
- Dillman, D. (2000). *Mail and Internet surveys: The Tailored Design Method*. New York: Wiley.
- Entrepreneur magazine (2006). Entrepreneurial Challenges Survey. January, 2006.
- Frazer, V. (1996). Skilled workers are in short supply. *Personnel Journal*, 75(11): 23–26.
- Glanz, B.P. (2002). *Handle with care: Motivating and Retaining Your Employees*. New York: McGraw-Hill.
- Hayton, J.C. (2003). Strategic human capital management in SME's: An empirical study of entrepreneurial performance. *Human Resources Management*, 42(4): 375–391.
- Heneman, R.L. & Tansky, J.W. (2002). Human resource management models for entrepreneurial opportunity: Existing knowledge and new directions. In: Katz, J. and Welbourne, T. (eds). *Managing people in entrepreneurial organizations*. Amsterdam: JAI Press.
- Henricks, Mark (2006). Are you afraid your key employees are ready to walk? Here's what you can do to hold on to your most valuable players. *Entrepreneur* 1 April 2006, 84.
- Hom, P.W. & Kinicki, A.J. (2001). Towards a greater understanding of how dissatisfaction drives employee turnover. *Academy of Management Journal*, 44(5): 975–987.
- Hornsby, J.S. & Kuratko, D.F. (2003). Human resource management in U.S. small businesses: A replication and extension. *Journal of Developmental Entrepreneurship*, 8(1): 73–92.
- Ireland, R.E. & Webb, J.W. (2007) Strategic entrepreneurship: Creating competitive advantage through streams of innovation. *Business Horizons*, 50(3): 49–59.
- Kaplan, S. & Henderson, R. (2006). Employee incentive systems: Why, and When, They are so hard to change. *Knowledge @ Wharton*. Retrieved 6/5/06 <http://knowledge.wharton.upenn.edu>.
- Kickul, J. (2001). Promises made, promises broken: An exploration of employee attraction and retention practices in small business. *Journal of Small Business Management*, 39(4): 320–335.
- Kristof, A.L. (1996). Person-Organization Fit: An Integrative Review of Its Conceptualizations, Measurement, & Implications. *Personnel Psychology*, 49(1): 1–49.
- MacMahon, J. & Murphy, E. (1999). Managerial effectiveness in small enterprises: Implications for HRD. *Journal of European Industrial Training*, 23(1): 25–35.
- Mak, B.L. & Sockel, H. (2001). A confirmatory factor analysis of I.S. employee motivation and retention. *Information & Management*, 38: 265–276.
- McKeown, J.L. (2002). *Retaining Top Employees*. New York: McGraw-Hill.
- Mcgrath, M. (2006). Plateauing: Redefining Success at Work. *Knowledge @ Wharton*, October 20, 2006. Retrieved 9/5/07. <http://knowledge.wharton.upenn.edu>.
- Mitchell, T.R., Holtom, B.C., Lee, T.W., Sablynski, C.J., & Erez, M. (2001). Why people stay: Using job embeddedness to predict voluntary turnover. *Academy of Management Journal*, 44(6): 1102–1122.
- Mulvey, P.W., LeBlanc, P.V., Heneman, R.L., & McInerney, M. (2002). Study find that knowledge of pay process can beat out amount of pay in employee retention, organizational effectiveness. *Journal of Organizational Excellence*, 21(4): 29–32.
- Payne, S.C. & Huffman, A.H. (2005). A longitudinal examination of the influence of mentoring on organizational commitment and turnover. *The Academy of Management Journal*, 48(1): 158–168.

- Peterson, R.A., Albaum, G., & Kozmetsky, G. (1986). The public's definition of small business. *Journal of Small Business Management*, 24(3): 63–68.
- Prewitt, E. (1999). How to keep your company's star employees. *Harvard Management Update*, August, 3–4.
- Ramlall, S. (2003). Managing employee retention as a strategy for increasing organizational competitiveness. *Applied H.R.M. Research*, 8(2): 63–72.
- Rutherford, M.W., Buller, P. F., & McMullen, P.R. (2003). Human resource management problems over the life cycle of small to medium-sized firms. *Human Resource Management*, 42(4): 321–335.
- Rye, D. (2002). *Attracting and Rewarding Outstanding Employees*. Santa Monica, CA: Entrepreneur Press.
- Saari, L. & Judge, T. (2004). Employee attitudes and job satisfaction. *Human Resource Management*. 43(4): 395–407.
- Saks, A.M. & Ashforth, B.E. (1997). Organizational socialization: Making sense of the past and present as a prologue for the future. *Journal of Vocational Behavior*, 51(2): 234–279.
- Smither, L. (2003). Managing employee life cycles to improve retention. *Leadership and Management in Engineering*, January, 19–23.
- Stewart, W.H., Watson, W., Carland, J.C., & Carland, J.W. (1999). A proclivity for entrepreneurship: A comparison of entrepreneurs, small business owners, and corporate managers. *Journal of Business Venturing*, 14(2): 189–214.
- Tanksy, J.W. & Heneman, R. (2003). Guest editor's note: Introduction to the special issue on human resource management in SMEs: A call for more research. *Human Resource Management*, 42(4): 299–302.
- Winter, S. (1998). Knowledge and Competence as Strategic Assets. In: David A. Klein (Ed). *The Strategic Management of Intellectual Capital*. New York: Butterworth-Heinemann, 165–168.

**Bruce H. Kemelgor** is an associate professor of management and entrepreneurship at the University of Louisville. He is also the director of their Small Business Institute and is president of the national association. His research interests include opportunity recognition, entrepreneurial competence, and person-role fit in organizations.

**William R. Meek** is an Entrepreneurship PhD candidate at the University of Louisville. His research interests include nascent entrepreneurship, career motivation and expectations, and human resource problems in entrepreneurial firms.

Reproduced with permission of the copyright owner. Further reproduction prohibited without permission.