

## Analyzing the Impact of Transactional and Transformational Leadership Styles on Employee Performance: Empirical Evidence from MSMEs

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### Abstract

Business leaders have crucial functions and duties for optimising the performance of employees as they integrate the practices of utilising human and other resources in the organisation. They are considered indispensable for giving employees the right guidance and emotional commitment to make the best possible contribution at the workplace. The ability to adopt leadership styles that are effective in managing changes and new developments in the business is made possible by paying attention to the scope and complexity of the problems in an appropriate manner. Despite the fact that various leadership philosophies might have varying effects on how their employees behave, the business leaders must explore appropriate leadership styles for a sustainable business. It must give special heed to the effective leadership styles that will enhance employee performance. As a result, this study investigates how leadership styles can have different effects on employee performance in a changing business environment after the economic disruptions of COVID 19. The empirical findings suggest that employee performance is positive associated with transactional and transformational leadership styles. These leadership styles have positive impacts on the performance of employees. However, transactional leadership has a stronger positive impact on employee performance of Micro, Small, and Medium Enterprises (MSMEs) in Manipur.

**Keywords:** Leaders, Leadership Style, Transactional Leadership, Transformational Leadership, Employee Performance, MSMEs, Manipur.

### 1. Introduction

Leadership is an essential element in determining and establishing the visions, missions, objectives, and strategies to meet those objectives in an organisation (Xu and Wang, 2008). With the upcoming problems in the world economy, leadership has grown to be an essential component of every successful organisational

transformation. Organizations should evaluate their leadership styles to succeed and remain competitive in the market (Alqatawenh, 2018). Any organisation should anticipate to adopt the appropriate leadership style as leadership styles may have different effects on employee behaviour and outcomes of the business. Leaders who are alert, conscious of the gravity of the problems and the intricacy of the management functions are crucial in choosing the leadership styles that are effective enough to handle changes and new developments in the business.

## 2. Theoretical Background

### 2.1 Leadership

Leadership is the process of motivating, encouraging, and directing behaviour and activities of people in order to assist the group or organisation achieve its objectives (Jones & George, 2004). It is a procedure where someone, or, in certain situations, a small group of individuals, persuades and inspires others to achieve objectives in a specific setting (Cole, 2005). It is further described that leaders utilise their abilities and knowledge in guiding and bringing a group of subordinates towards intended actions that are relevant to their organisational strategic objectives (Jackson and Parry, 2008).

### 2.2 Leadership Style

The leadership style refers to how a leader imparts instructions, formulates strategies, and inspires others, as well as their attitude towards each of these tasks (Jooste, 2009:33). A leader uses a set of behaviours to persuade subordinates to accomplish organisational objectives (DuBrin, 2006:348). The focus on leadership styles is based on the belief that employees are more likely to perform better at workplace when managers who adopt a particular style of leadership (Mullins *et al.*, 2007: 371). It is generally classified into three styles: (i) authoritarian leadership: concentrate authority and derives power through position, regulation of rewards, and force, (ii) democratic leadership: leader entrusts power to subordinates, trust the knowledge of subordinates and encourages participative management, and (iii) laissez-faire leadership: pass whole power to members, give absolute freedom to do what the subordinates think best but remain available when help is needed (Mullins, 2007:371; Daft, 2008:40). In addition, two prominent leadership styles viz., (a) transactional leadership and (b) transformational leadership styles emerged in the 1980s, playing an important role in organizational change and growth.

#### (a) Transactional leadership style

In the transactional leadership style, the leader communicates a need and reward comes from meeting that need but the corresponding punishment comes in case of failure (Kunin & Walker, 2017). In this leadership style, effective performance is recognised and rewarded, but bad performance is subject to punishment (Kunin & Walker, 2017). It is an exchange of relationships between superiors and subordinates (Burns, 1978). The leader-follower relationship is built on speculative rewards in transactional leadership (Howell & Avolio, 1993).

#### (b) Transformational leadership style

This type of leadership is characterized by having optimistic perspective on the prospects of organization and are largely focused on aiding people in achieving excellence by communicating a feasible objective and ambition to employees, and trying to increase their confidence by working together along with employees to identify and address their requirements (Peterson *et al.*, 2009). It motivates the employees to strive above personal interests and established expectations in realizing predetermined goals of organizations (Abasilim *et al.*, 2019). It is considerably more effective leadership approach than other leadership styles (Obasan & Hassan, 2014). F

### 2.3 Employee Performance

It is described as the outcome of a task or activity that is observable and can be assessed (Niranjana *et al.*, 2005). It is the execution of tasks exhibited by employee in facilitating the organisation accomplish its objectives. It

could be a multi-dimensional concept and a basic criterion for deciding whether an organisation succeeds or fails flat (Prasetya & Kato, 2011). It is the efficient performance of tasks by employees, which is critical to achieving the strategic goals of an organization (Amos *et al.*, 2004).

#### **2.4 Leadership and Employee Performance**

Leadership generally determines the outcomes and performance of employees by exhibiting the appropriate behaviour (Pradeep, D. D., & Prabhu, N. R. V., 2011:199). Leaders should always realize that inspiring the employees is critical to meeting the targets for employee performance (Wall *et al.*, 1992). According to Northouse (2013), ineffective or unsuitable leadership styles can have a considerable influence on employee performance. Depending on different factors, particular leadership styles may or may not be associated with employee performance (Fu-Jin *et al.*, 2010). To improve the performance and productivity of employees, a suitable and competent leadership is thus desirable in the organization. It is crucial to realise high employee performance to ensure organisational survival (Noorshahi, 2006). Benefits are offered to employees on a rewards basis under transactional leadership, which motivates followers to meet performance expectations and fulfil their obligations in order to receive the rewards that are due (Bass, B.M., 1985). Al Khajeh (2018) recommends that organisations must give special emphasis on transformational and democratic leadership approaches. Previous study has explored and confirmed that leadership styles affect employee performance, with transformational leadership yielding much higher performance (Bass, B.M., 1990; Howell, J. M., & Avolio, B. J., 1993). According to Obasan Kehinde, A. *et al.*, (2014), transformational leadership will produce positive and successful outcomes in a business because it motivates workers to go above and beyond expectations. Wang *et al.* (2005) implied that transformation leaders may create high-quality interactions with their team members, which will in turn affect how productive they are.

### **3. Research Objectives**

The purpose of this study is to explore and determine the impact of transactional and transformational leadership styles on the employee performance of MSMEs in Manipur. Therefore, two research objectives mentioned below are developed that will fulfil the purpose of this research.

- (a) To ascertain whether employee performance is related to transactional and transformational leadership in MSMEs of Manipur.
- (b) To analyse the impact of transactional and transformational leadership on employee performance in MSMEs of Manipur.

### **4. Hypotheses of the Study**

According to Raja & Palanichamy (2015), transformational and transactional leadership styles are positively related to employee performance. Due to their imperative traits, these specific leadership styles are the major focus of the literature on leadership styles (Bass & Avolio, 1990; Meyer & Botha, 2000). The following two hypotheses are developed to support the objectives of this research:

- (a) H<sub>1</sub>: Transactional and transformational leadership styles are positively correlated with employee performance.
- (b) H<sub>2</sub>: Transactional and transformational leadership styles have significant effects on employee performance.

### **5. Research Methodology**

The research approach is empirical in nature. This study was undertaken utilizing data from primary and secondary sources. A systematic and structures questionnaire adapted from previous works has been utilized for

gathering the primary data from MSMEs in Manipur. A total of 800 questionnaires were distributed of which 686 usable respondents were retrieved for the study. The questionnaires were gathered by simple random sampling from the population. A review of the literature was conducted from secondary data sources, viz., Google Scholar and other relevant publications. The independent variables for the study include transactional and transformational leadership and employee performance is taken as the dependent variable. The questionnaire was set using 5-point Likert scale extending from 1 (strongly disagree) to 5 (strongly agree). The questionnaire was adapted from leader reward and punishment scales for transactional leadership (Podsakoff, P. M., *et al.*, 1984), transformational leadership inventory by Podsakoff, P. M., *et al.*, 1990), and employee performance measurement derived from Pradhan, R. K., & Jena, L. K., (2017). Reliability test, validity test, factor analysis, Pearson’s correlation, and SEM have been implemented for analysing and deriving information based on the primary data with the help of SPSS version 23 and AMOS version 24.

**6. Analysis of Data and Interpretation**

The demographic information of the respondents gathered using the structured questionnaires was compiled and examined as given below Table 1:

<b>Table 1: Demographic Characteristics</b>				
<b>Gender</b>	<b>Frequency</b>	<b>Percent</b>	<b>Valid Percent</b>	<b>Cumulative Percent</b>
Male	429	62.5	62.5	62.5
Female	257	37.5	37.5	100.0
Total	686	100.0	100.0	
<b>Age</b>				
10-25 years	62	9.0	9.0	9.0
26-35 years	275	40.1	40.1	49.1
36-45 years	326	47.5	47.5	96.6
46 and above years	23	3.4	3.4	100.0
Total	686	100.0	100.0	
<b>Qualification</b>				
10th-12th standard	264	38.5	38.5	38.5
Bachelor	358	52.2	52.2	90.7
Diploma	11	1.6	1.6	92.3
Master	35	5.1	5.1	97.4
Ph.D	1	.1	.1	97.5
No formal Education	17	2.5	2.5	100.0
Total	686	100.0	100.0	
<b>Place of the enterprises</b>				
Thoubal	69	10.1	10.1	10.1
Kakching	70	10.2	10.2	20.3
Churachandpur	92	13.4	13.4	33.7
Senapati	99	14.4	14.4	48.1
Ukhrul	68	9.9	9.9	58.0
Imphal East	95	13.8	13.8	71.9
Imphal West	96	14.0	14.0	85.9
Bishnupur	97	14.1	14.1	100.0
Total	686	100.0	100.0	
<b>Designation</b>				
Owner	486	70.8	70.8	70.8
Executive	19	2.8	2.8	73.6

Manager	16	2.3	2.3	75.9
Supervisor	16	2.3	2.3	78.3
Project Leader	3	.4	.4	78.7
IT operator	5	.7	.7	79.4
Employee	141	20.6	20.6	100.0
Total	686	100.0	100.0	
<b>Department</b>				
Administration	12	1.7	1.7	1.7
Human Resources	9	1.3	1.3	3.1
Finance	39	5.7	5.7	8.7
Sales and Marketing	418	60.9	60.9	69.7
Information Technology	3	.4	.4	70.1
Operations	35	5.1	5.1	75.2
Customer Services	170	24.8	24.8	100.0
Total	686	100.0	100.0	
<b>Year of Enterprise</b>				
Less than 1 year - 5 years	230	33.5	33.5	33.5
6 - 10 years	334	48.7	48.7	82.2
11-15 years	104	15.2	15.2	97.4
16 and above years	18	2.6	2.6	100.0
Total	686	100.0	100.0	

The KMO value obtained is 0.765, ensuring that the sample size is adequate for conducting the research (Table 2). To establish and derive the components, the exploratory factor analysis was performed by the principal component extraction method and the varimax rotation suppressing loading below 0.7. Three components reflecting transactional leadership, transformational leadership, and employee performance were extracted as shown in Table 3.

**Table 2: KMO and Bartlett's Test**

Kaiser-Meyer-Olkin Measure of Sampling Adequacy.	.765
Bartlett's Test of Sphericity	Approx. Chi-Square
	2191.622
	Df
	45
	Sig.
	.000

**Table 3: Rotated Component Matrix<sup>a</sup>**

	Component		
	1	2	3
EP_32: Employees accomplish their responsibilities on time.	.870		
EP_31: Employees consistently deliver excellent results in their works.	.831		
EP_33: Employees are capable of handling several responsibilities to achieve goals.	.759		
EP_39: Employees offer assistance to co-workers when required.	.745		
TL_20: I would immediately appreciate any increase in job quality.		.829	
TL_21: I recognize and reward my employees who do exceptional job.		.818	
TL_19: When my staff do well, I provide positive acknowledgment.		.742	
TFL_28: I am capable of devoting myself to my goals.			.848
TFL_29: I am constantly looking for new business opportunities.			.820
TFL_25: Rather than merely telling, I lead by example.			.769

Rotation Method: Varimax with Kaiser Normalization

Extraction Method: Principal Component Analysis

Rotation converged in 4 iterations.

**Table 4: Reliability Statistics**

Variable	N of Items	Cronbach's Alpha
Transactional Leadership (TLL)	3	.738
Transformational Leadership (TFL)	3	.751
Employee Performance (EMP)	4	.828
Overall	10	.746

The final items considered for the study consist of 10 items in total that have factor loading which are above 0.7 after conducting the factor analysis. The items of the constructs were adequately examined for reliability. The items considered for the measuring the constructs were above the acceptable value of 0.7, as shown in Table 4. Therefore, the items for the construct were reliable for analysis. Pearson’s Correlation Test was used to ascertain a significant association among the variables viz., transactional leadership, transformational leadership, and employee performance. Since the obtained p-values are less than 0.05, it confirms that there is a significant correlation among the variables as given in Table 5.

**Table 5: Correlations**

	TLL	TFL	EMP
TLL Pearson Correlation	1	.136**	.296**
TLL Sig. (2-tailed)		.000	.000
TLL N	686	686	686
TFL Pearson Correlation	.136**	1	.150**
TFL Sig. (2-tailed)	.000		.000
TFL N	686	686	686
EMP Pearson Correlation	.296**	.150**	1
EMP Sig. (2-tailed)	.000	.000	
EMP N	686	686	686

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

To assess the measurement model, CFA has been performed with the help of AMOS version 24. The values obtained for the measurement model are shown in Fig 1 and AMOS outputs (Table 6 and 7) indicate that all the values are within the acceptable limit ( $CMIN= 103.209$ ,  $CMIN/df=3.225$ ,  $SRMR= .0429$ ,  $GFI=0.970$ ,  $AGFI=.949$ ,  $CFI=.967$ ,  $NFI=.953$ ,  $TLI=.9954$ ,  $RMSEA=.057$ ), making the model a good fit (recommended by Hu, L., Bentler, P.M., 1999) and the measures of model validity are within the acceptable values as shown in Table 8. Therefore, the measurement model considered for the study is a good fit.

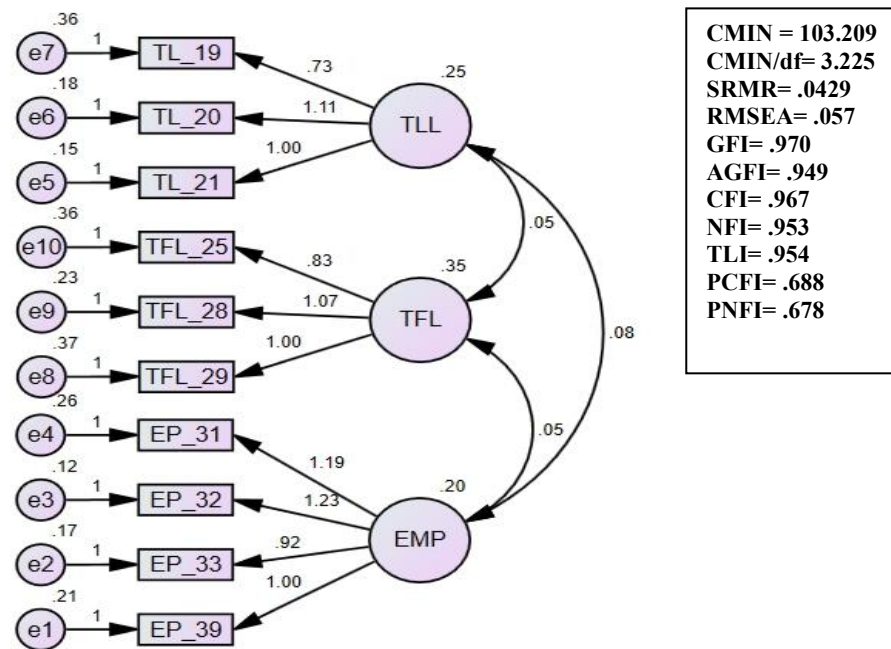


Figure 1: CFA of Measurement Model

(Source: Author)

Table 6: Regression Weights: (Group number 1 - Default model)

	Estimate	S.E.	C.R.	P	Label
EP_39 <--- EMP	1.000				
EP_33 <--- EMP	.916	.057	16.208	***	
EP_32 <--- EMP	1.233	.067	18.398	***	
EP_31 <--- EMP	1.188	.071	16.661	***	
TL_21 <--- TLL	1.000				
TL_20 <--- TLL	1.106	.078	14.117	***	
TL_19 <--- TLL	.733	.062	11.864	***	
TFL_29 <--- TFL	1.000				
TFL_28 <--- TFL	1.066	.080	13.292	***	
TFL_25 <--- TFL	.834	.063	13.187	***	

**Table 7: Covariances: (Group number 1 - Default model)**

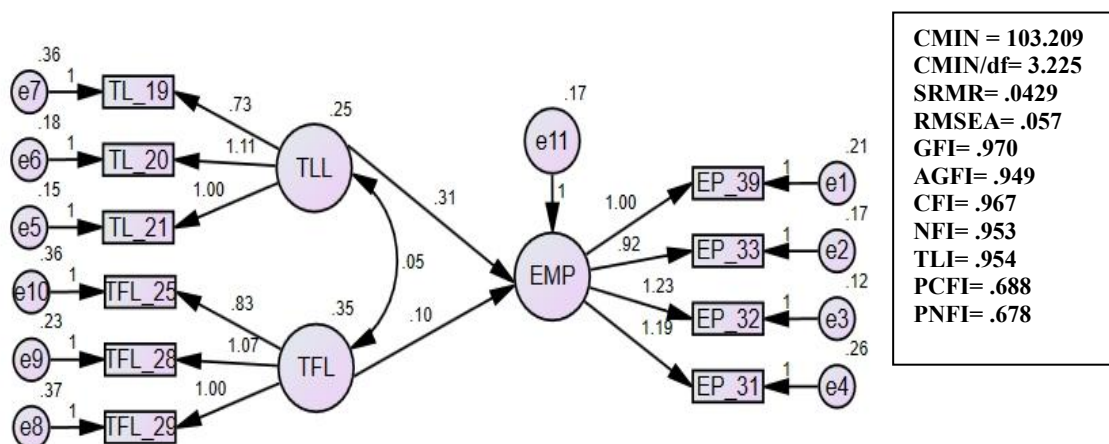
	Estimate	S.E.	C.R.	P	Label
EMP <--> TLL	.083	.012	7.023	***	
EMP <--> TFL	.050	.013	3.831	***	
TLL <--> TFL	.047	.015	3.146	.002	

	CR	AVE	MSV	MaxR(H)	EMP	TLL	TFL
<b>EMP</b>	0.833	0.556	0.138	0.848	<b>0.746</b>		
<b>TLL</b>	0.752	0.511	0.138	0.791	0.371***	<b>0.715</b>	
<b>TFL</b>	0.755	0.509	0.036	0.772	0.189***	0.158**	<b>0.714</b>

**Table 8: Model Validity Measures**

(Source: Using the Gaskin, J. & Lim, J. (2016), "Master Validity Tool", AMOS Plugin)

The SEM technique was implemented to test the hypotheses of the causal model. Since the p-values are less than 0.05 as shown in Table 9, transactional and transformational leadership have a significant impact on employee performance. However, transactional leadership has a greater impact on employee performance as compared to transformational leadership. The model fit indices for SEM model as shown in Figure 2 were calculated ( $CMIN= 103.209$ ,  $CMIN/df=3.225$ ,  $SRMR= .0429$ ,  $GFI=0.970$ ,  $AGFI=.949$ ,  $CFI=.967$ ,  $NFI=.953$ ,  $TLI=.9954$ ,  $RMSEA=.057$ ), the values obtained are within the acceptable limit confirming the causal model is a good fit.



**Figure 2: SEM of Causal Model**

(Source: Author)

**Table 9: Regression Weights: (Group number 1 - Default model)**

	Estimate	S.E.	C.R.	P	Label
EMP <--- TLL	.313	.044	7.096	***	
EMP <--- TFL	.100	.035	2.877	.004	
EP_39 <--- EMP	1.000				
EP_33 <--- EMP	.916	.057	16.208	***	
EP_32 <--- EMP	1.233	.067	18.398	***	
EP_31 <--- EMP	1.188	.071	16.661	***	
TL_21 <--- TLL	1.000				
TL_20 <--- TLL	1.106	.078	14.117	***	
TL_19 <--- TLL	.733	.062	11.864	***	
TFL_29 <--- TFL	1.000				
TFL_28 <--- TFL	1.066	.080	13.292	***	
TFL_25 <--- TFL	.834	.063	13.187	***	

**7. Findings and Conclusions**

The empirical results supported the significant role of leadership and the varying effects on employee performance. It ascertains the positive relationships of transactional and transformational leadership styles on employee performance and their significant effects. However, transactional leadership has a stronger positive impact on employee performance. It suggests that transactional leadership would result in more successful outcomes in the enterprises since benefits are provided to employees on a rewards system, which inspires followers to live up to their commitments and perform to the expectations of the enterprises. In conclusion, the transactional leadership is more effective in MSMEs of Manipur and should be accompanied by the transformational leadership for business leaders in realizing higher employee productivity in the organization.

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**9. Conflict of Interest:** The authors declare that there are no conflicts of interest.

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