

# **THE ROLE OF DIFFERENTIATION STRATEGY ON HUMAN RESOURCE MANAGEMENT PRACTICES AND COMPETITIVE ADVANTAGE OF FIRMS LISTED ON THE NAIROBI SECURITIES EXCHANGE**

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## **Abstract**

*Sustainable competitive advantage has become a major area of study in Human Resource Management (HRM). There is vast support from theoretical and empirical literature that HRM practices has influence on competitive advantage. However, this study introduced differentiation strategy as the moderating variable. Further, the study determined the relationship between human resource management practices, differentiation strategy and competitive advantage of firms listed on the Nairobi Securities Exchange. The main objective of the study was to determine the moderating effect of differentiation strategy on the relationship between human resource management practices and competitive advantage of firms listed on the Nairobi Securities Exchange. The study was grounded on both configuration theory and universalistic theory. The review of the literature provided the conceptual model and hypothesis that guided the study. The study population consisted of 62 companies listed on the Nairobi Securities Exchange. The study used a cross-sectional survey design where data was collected at one point in time across the organizations. The primary data was collected through a questionnaire. The respondents were 62 heads of HR departments in different firms. The response rate was 63%. Data was analysed using stepwise regression analysis. The findings indicated that*

*differentiation strategy moderates the relationship between HRM practices and competitive advantage. This study enhance our understanding of the role of HRM practices and differentiation strategy on the competitive advantage of firms listed on Nairobi Securities Exchange.*

*Keywords: Human resource management Practices, differentiation strategy, competitive advantage, Configurational theory, Universalistic theory, Nairobi Securities Exchange*

## **INTRODUCTION**

Changing business environment has made adoption of HRM practices imperative for competitive advantage. Strong evidence exists in literature that different HRM practices have a positive association with a firm's competitive advantage (Delery& Doty, 1996,Wright & Snell, 1998, Pfeffer 1998, Wright & McMahan, 1999). If HRM practices are properly configured, they could be created by simply benchmarking competitors firms leading to replication by competitors therefore, not likely to provide a source of sustainable competitive advantage (Becker, Huselid, Pickus and Sptatt, 1997). Several studies have suggested that many firms view differentiation strategy as a more important and distinct means to achieve competitive advantage. Globalization has led to more intense competition among firms, with increased customer demands. HRM practices should therefore be linked with others HR strategies to create a HRM system that should be integrated with differentiation strategy for sustainable competitive advantage that is not easily imitated by the competitors. The result is an HRM system that produces employee behaviour that is focused on value. Even if an organization has effective and efficient HRM practices in place and treats its customer well and the customers do not perceive their product as unique, the organization cannot achieve competitive advantage. Therefore, for an organization to achieve competitive advantage it will depend on how it aligns HRM practices and differentiation strategy.

The firms listed on the Nairobi Securities Exchange operate in a dynamic business environment that affects their competitive advantage. For them to achieve competitive advantage they need sound HRM practices that embrace good governance that attract foreign investors and improve shareholders value hence competitive advantage. The firms need to integrate their HRM practices with differentiation strategy in a way that would lead to competitive advantage. The way in which these firms treat their employees affect their performance. The firms listed on the Nairobi Securities Exchange are preferred for this study because they cover different sectors of the Kenyan economy. In addition, their performance is also important for

Kenyan economic development and gross national product. Furthermore, the firms listed on the Nairobi Securities Exchange provide financial reports to the public for their scrutiny. For this reason, they are forced to engage in good corporate governance which further influences HRM practices. To achieve competitive advantage will depend on how the listed firms create a fit of the relationship between HRM practices, differentiation strategy and competitive advantage, which has not been studied.

## **THEORETICAL FOUNDATION**

The study is anchored to two theories which include configurational and universalistic.

### **Configurational Theory**

Configurational theories are holistic and are subject to typologies of ideal types. They explicitly adopt a system of assumption of equifinality (Wright & McMahan, 1992). In order to be effective, an organization must create HR systems that achieve both a vertical and a horizontal fit (Delery & Doty, 1996). The best fit approach highlights that HR strategies and business strategies must be aligned to achieve sustainable competitive advantage (Armstrong, 2008).

Horizontal fit refers to the internal consistency of the organization's HR practices and policies. Vertical fit refers to the congruence of the HR systems with other organizational characteristics such as the firm's strategy. Arthur (1994) argues that the ideal configuration will be one with the highest degree of horizontal fit.

It is therefore evident that in addition to systems being consistent with organizational and environmental conditions, they must also achieve internal coherence. Schuler and Rivero, (1989) observe that these configurations represent non-linear synergistic effects and higher order interactions that cannot be represented with traditional contingency theories (Schuler & Rivero, 1989). In addition, Khatri (2000) argues that configurational theories are concerned with how the pattern of multiple independent variables is related to the dependent variable. These configurations incorporate the assumption that multiple unique configurations of the relevant factors can result in maximal performance (Delery & Doty, 1996). The configurations are assumed to be ideal types that are theoretical constructs rather than empirically observed phenomenon (Wright & McMahan, 1992) the fit between HR strategies.

The model of this study is represented by the fit between HRM strategies and the differentiation strategy. The internal fit is represented by the fit between HRM practices as coherent and consistent bundles. The organization fit is the alignment between coherent sets of HR practices (HR systems/bundles) and other systems within the organization. This phenomenon represents the fit between the HRM practices bundles with differentiation strategy.

Considering that the internal fit is central to universalistic models, the main problem is how to determine an HR system, that is, as coherent of synergistic HR practices that blend better in producing higher business performance. Support of the universalistic approach to strategic HRM is mixed as there are notable differences across the studies as what constitutes a HR practices.

The study used configurational theory because it is considered by several authors to be a more theoretically valid and tenable approach to understanding SHRM for sustainable competitive advantage. This is because the configurational approach promotes a system of HR practices that are customized to suit a particular firm's competitive strategies and internal practices, policies and resources. It is only through the configurational use of HR practices in a unique context that human resources can be developed as a source of sustained competitive advantage. The dominant coalition is challenged to enable HRM to make a genuine contribution to sustainable competitive advantage, aside from the importance of distinguishing different fits. Although the alignment of HRM practices and business strategies lead to competitive advantage, Delery and Doty (1996) argue that there is no consensus on the agreed HRM practices that lead to optimal performance. Aiming for uniqueness can enable the organization to achieve competitive advantage. This can be achieved through differentiation strategy as well as good treatment of employees which will guarantee competitive advantage.

### **Universalistic Theory**

The universalistic scholars concluded that HRM practices positively influence the firm's competitive advantage (Martel & Carrol, 1995). Universalistic arguments are the simplest forms of theoretical statements in Strategic Human Resource Management (SHRM) literature since they imply that the relationship between a given independent variable and a dependent variable is universal across a population of organizations (Pfeffer & Cohen, 1984). Proponents of Best Practice consider that Human resource activities should be obtained following a set of HRM Practices that enable the organization to achieve sustainable competitive advantage. Scholars of Best fit model assert that if human resource policies of any organization align with business strategy would lead to competitive advantage (Armstrong, 2008).

Dyer and Reeves (1995) assumed that HRM practices promote operating efficiency, increase innovation and revolution ability, and increase organization performance benefits. Even though, not all HR practices are strategic, there is growing consensus about which practices can be considered strategic (Lado & Wilson, 1994). Drawing on theoretical works of (Miles & Snow, 1984; Osterman, 1987) there are a set of universal HRM practices aimed at high commitment or high performance that will benefit all organizations regardless of the context.

The most influential HR best practices set are associated with sixteen practices of Pfeffer (1994). He summarized these best practices into seven practices including employment security, selective hiring, self-management teams, provision of high pay contingent on the company performance, extensive training, reduction of status differences communication and employee involvement.

Cook and Frink (1998) investigated the HRM system practices of the firms in declining industries and found most high performance firms adopted HRM practices measures. Although HRM practices lead to competitive advantage, there is no consensus on the agreed HRM practices that lead to optimal performance (Delery & Doty, 1996). Huselid (1995) noted that a positive relationship between better HRM practices and the firm's competitive advantage. Kidombo (2007) established a significant and positive relationship between HRM practices and performance. Sagwa (2014) study on the relationship between HRM practices of firms listed on the Nairobi Securities Exchange. His study established a significant and positive relationship between HRM practices and performance. Proponents of the universalistic approach to SHRM consider the adoption of high performance practices of HRM. They constitute an excellent way to increase the human capital value and consequently increasing organizational efficiency which lead to competitive advantage (Wright & McMahan, 1999). This theory is appropriate in this study because it provides HRM practices that lead to competitive advantage.

## LITERATURE REVIEW

Empirical and theoretical evidence yields fairly conclusive findings that HRM practices have an influence on competitive advantage (Wright & McMahan, 1992; Coff, 1994; Berker & Huselid, 1997; Pfeifer, 1999). They indicated that HR can lead to competitive advantage because it meets the criteria for being a source of sustainable competitive advantage. Similarly, Coff (1994) notes that human resources are key assets that lead to sustainable competitive advantage because of causal ambiguity and systematic information making them inimitable.

According to Becker, Huselid, Pickus and Sptatt (1997), HRM practices should be linked with the firm business and strategic initiatives. The result is an HRM system that produces employee behaviours that are focused on key business strategy, which in turn drive profits, hence competitive advantage. Barney (1991) affirms that a firm's HRM system is a source of competitive advantage if it is rare and difficult to imitate (Wright & McMahan, 1992). If properly configured, HRM practices could be created by simply benchmarking firms, then they could be easy to replicate thus rendering them likely to provide a source of competitive advantage. Becker, Huselid, Pickus and Sptatt (1997) argued that the distinctive HR practices help to create unique competencies that differentiate products and in turn lead to competitive advantage of the

firm. They concluded that product differentiation is one of the essential functions of strategic management, and distinctive HR practices shape the core competencies that determine how the firms compete.

Banker, Mashruwala and Tripathy (2010) studied generic strategies and sustainability of financial performance. They found that unlike cost leadership strategy, differentiation strategy was associated with firms sustaining their financial performance to a greater extent. Gebauer, Gustafsson and Witell (2011) studied competitive advantage through service differentiation by European-based manufacturing firms. They found that companies that concentrated on either product or service differentiation achieved a stronger relationship between innovativeness and business performance than those that placed an average level of emphasis on both areas. Tanwar (2013) did a study on Porters' generic competitive strategies and found that differentiation is a viable strategy for earning above average returns in a specific business because the resulting brand loyalty lowers customers' sensitivity to price hence competitive advantage. Arasa and Githinji (2014) studied the relationship between competitive strategies and firm performance in telecommunication companies in Kenya. They found that product differentiation strategy should consistently focus its efforts on providing unique product or service to achieve sustainable competitive advantage.

Oloko, Anene, Kiara, Kathambi, and Mutulu (2014) studied marketing strategies for profitability at Safaricom Limited in the Kenyan telecommunication industry. The study revealed that marketing plays a crucial role in enhancing company profitability and growth. However, these studies did not consider contribution of HRM practices in a firm's competitiveness. Yet, differentiation strategy alone without good treatment of employees will not guarantee competitive advantage.

Sagwa (2014) studied the relationship between HRM practices and performance of firms listed on the Nairobi Securities Exchange. His study established a significant and positive relationship between HRM practices and performance, hence a competitive advantage. The current study used HRM practices adopted by Kidombo (2007), which are: internal career opportunities, retention strategies, training and development, reward strategies, performance appraisal, and employee relations and competitive advantage measures of (firm profitability and public image). Sagwa (2014) also assessed the moderating effect of competitive Strategies (cost leadership, focus and differentiation strategy) and firm performance. He found that competitive strategy has a positive and significant influence on the relationship between employee's outcomes and performance. Although his study highlighted the role of differentiation strategy on the relationship between employee's outcomes and firm performance, this study

designed its objectives to establish whether, differentiation strategy moderates on relationship between HRM practices and competitive advantage.

Huselid, Jackson and Schuler (1997) carried out research in 293 US firms on technical and strategic resource management effectiveness as determinants of firm performance. They established that effectiveness was associated with capabilities and attributes of HR staff. They also found that relationships existed between HRM effectiveness and productivity, cash flow and market value. Two important implications follow; First, professional skills and abilities of human resources staff members appear to support the implementation of strategic HRM activities and should be retained even by firms undergoing a paradigm shift in their approach to HRM. Second, business related capabilities appear important contributors to strategic HRM activities and their development among HRM professionals should be encouraged.

Chang, Pao-Long and Wei-Ling Chen (2002) study on effect of HRM practices on firm performance from High –Tech firms in Taiwan. They found that HRM practices such as training and development, benefits, teamwork, performance appraisal and human resource planning have a significant effect on employee productivity. This study supported the use of differentiation strategy as a moderating variable between HRM practices and competitive advantage. The study was done on high tech firms in Taiwan, which is a different context from that of the companies listed on the Nairobi securities exchange in Kenya. Ogbonna and Harris (2001) examined SHRM, market orientation and organizational performance. They found that there is a direct link between market orientation and performance and is mediated by the extent of market orientation exhibited by the organization. The current study used marketing and image management as moderating variable between HRM practices and competitive advantage and not as a mediating variable between HRM and competitive advantage.

The foregoing analysis shows that there is relationship between human resource management practices and competitive advantage. However, as demonstrated by various studies (Guthrie, Spell and Nyamori 2011; Chang, Pao-Long, Wei-Ling & Chen, 2002), differentiation strategy moderates HRM practices and competitive advantage. Although they provided an insight that differentiation strategy moderates HRM practices and competitive advantage, they did not use the differentiation strategy in terms of product innovation, marketing and image management and responsiveness to customers and also they did not use firm profitability and public image as the competitive measures. Based on these findings, the current study proposed that differentiation strategy moderates the relationship between HRM practices and competitive advantage. This is supported by the configuration theory that suggests that an organization must develop HR systems that achieve both a vertical and a horizontal fit hence competitive advantage (Delery& Doty, 1996). The knowledge gaps that this study addresses

include the moderating effect of differentiation strategy on the relationship between HRM practices and competitive advantage. This study, therefore, addressed these gaps by answering the question: What is the contribution of the differentiation strategy on the relationship between HRM practices and competitive advantage? The general objective of the study was to determine the relationship between human resource management practices, differentiation strategy and competitive advantage of firms listed on the Nairobi Securities Exchange.

## RESEARCH METHODOLOGY

The study applied positivistic philosophy. This is because the study involved objective testing of hypotheses that was formulated as predictions of objectively observed phenomena. A descriptive cross-sectional survey was carried out to determine the moderating effect of differentiation strategy on the relationship between Human Resource Management practices and competitive advantage. Using the descriptive survey design, the researcher was able to describe the variable of the study and derive predictive regressions models for predicting changes in the dependent variables. Data was at one point in time collected across 62 firms; thus cross-sectional survey was the most appropriate.

The target population of this study comprised all firms that were listed on the Nairobi Securities Exchange from 2013. The total number of the companies listed on the Nairobi Securities Exchange was 62 as at 2013 (Nairobi Securities Exchange Handbook, 2013). The respondents were HR managers. The census method was used.

Primary data was collected on HRM practices, differentiation strategy and competitive advantage. The questionnaires was designed on a five-point Likert scale. The responses ranged from 1= strongly disagree; 2 =disagree; 3 = neither disagree nor agree; 4= agree; 5= strongly agree. The respondents were asked to rate the extent to which organization used HRM practices which was adapted from Delery& Doty (1996); Pfeffer(1998) andKidombo, (2007). They were also questions related to differentiation strategy which was adapted from the literature. Finally the respondents were asked to rate the competitive advantage where firm profitability adapted from Busienei(2013) and public image was derived from the literature.

The study sought to establish the reliability of each study variable. The measurement scales were tested using Cronbach Alpha coefficient to ascertain the internal consistency of the five point Likert scales which were used in the survey. Studies by Nunnally (1967, 1978) are the most widely referenced either in support or criticism of obtained coefficient. The recommended value 0.7 was used as cut off point. Differentiation strategy had the highest reliability coefficient of 0.896 followed by HRM practices with a coefficient of 0.865, competitive advantage with reliability coefficient of 0.828. The Cronbach alpha coefficient of the constructs in the study were

considered appropriate to indicate a sufficient level of reliability. The study used inferential statistics (stepwise regression analysis) to establish the nature and magnitude of the relationship between variables and to test hypothesized relationship.

## ANALYSIS AND FINDINGS

### Response rate

The 62 questionnaires were distributed to all firms listed on the Nairobi Securities Exchange out of which 42 questionnaires were collected from heads of HR departments in the various firms. However, 3 questionnaires had incomplete data on some variables, leaving 39 with complete information. The response rate was therefore 63 percent which compares well with other studies of performance of firms listed on Nairobi Securities Exchange. For example, Kariuki (2014) had a 68 percent response rate, Sagwa (2014) 64 percent and Letting (2011) 87 percent.

### Multicollinearity testing

Multicollinearity was assessed using the Variance inflation factors (VIF) prior to the testing of hypothesis. VIF indicates whether a predictor variable has a strong linear relationship with the other predictor variables. VIF is the reciprocal of tolerance. Therefore, if tolerance of two or more of the variables is equal or less than 0.2 then there exists collinearity or if two or more variable have the VIF greater than 10 then there is Multicollinearity. The results of the two tests are presented in Table 1.

Table 1. Results of the Test of Multicollinearity

Model	Collinearity Statistics	
	Tolerance	VIF
Human Resource Information systems	0.327	3.054
Human Resource management practices	0.207	4.826
Differentiation Strategy	0.349	2.864

a. Dependent Variable: Competitive advantage

HRM practices had the highest VIF of 4.826, followed by HRIS 3.054 while differentiation strategy had the lowest at 2.864. Therefore, if tolerance of two or more of the variables is equal or less than 0.2 then there exists collinearity or if two or more variable have the VIF greater than 10 the presence of multicollinearity is confirmed (Hair et al,2006). Since all the tolerances of the variables were not less than two and no VIF that was greater than 10 the tests of multicollinearity was not confirmed.

## Hypothesis testing

The study sought to assess the moderating effect of differentiation strategy on the relationship between HRM practices and competitive advantage. To assess the moderating effect the following hypothesis was formulated from the conceptual framework:  $H_{a1}$  Differentiation strategy moderates the relationship between HRM practices and competitive advantage.

This hypothesis was tested using a stepwise regression method proposed by Kenny (2014). This involved testing the main effect of the independent variable (HRM practices) and the moderator (differentiation strategy) on the dependent variable (competitive advantage) and the effect of interaction between HRM practices and differentiation strategy on competitive advantage. Moderation is assumed to take place if the effect of interaction between the HRM practices and differentiation strategy on competitive advantage is significant. The three steps by Kenny (2014) were followed.

### ***Step One: HRM Practices and Competitive Advantage***

In step one; HRM practices were regressed on competitive advantage. The results are presented in Table 2.

The findings show the result of stepwise regression analysis for Model 1 when only HRM practices and competitive advantage are in the regression model ( $R^2=.278$ ,  $F=10.807$   $p<0.05$ ). From the table, HRM practices accounted for 27.8 percent competitive advantage. Further the table shows beta coefficient value of which is significant at ( $\beta= .740$   $t=3.287$ ,  $p<0.05$  indicating that for every unit change in HRM practices, competitive advantage increases by .740 (74 percent).

### ***Step Two: Differentiation Strategy, HRM Practices and Competitive Advantage***

In step two, differentiation strategy was added to the regression model equation (with competitive advantage as the dependent variable).

The introduction of the moderator differentiation strategy in Model 2 significantly improves the effect of differentiation strategy on the relationship between HRM practices and competitive advantage ( $R^2=.321$ ,  $F=6.370$   $p<0.05$ ). HRM practices and differentiation strategy explain 32.1% of the variation on competitive advantage. The F values are statistically significant ( $F=10.807$ ,  $P<0.05$  and  $F=6.370$ ,  $P<0.05$ ) that the influence of the independent variable and the moderator were significant in the model. Further, Table 2 shows the beta coefficient is ( $\beta=.805$ ,  $t=3.530$ ,  $P<0.05$ ), that is, for every unit change in differentiation strategy, competitive advantage increases by .805 (80.5 percent).

Table 2: Regression Results for the Effect of Differentiation Strategy  
on the Relationship between HRM Practices and Competitive Advantage

Model Summary									
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
					R Square Change	F Change	df1	df2	Sig. F Change
1	.528 <sup>a</sup>	.278	.253	.40461	.278	10.807	1	28	.003
2	.566 <sup>b</sup>	.321	.270	.39984	.042	1.673	1	27	.207
3	.661 <sup>c</sup>	.437	.372	.37084	.117	5.387	1	26	.028

ANOVA<sup>a</sup>

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	1.769	1	1.769	10.807*	.003 <sup>b</sup>
	Residual	4.584	28	.164		
	Total	6.353	29			
2	Regression	2.037	2	1.018	6.370*	.005 <sup>c</sup>
	Residual	4.316	27	.160		
	Total	6.353	29			
3	Regression	2.778	3	.926	6.732*	.002 <sup>d</sup>
	Residual	3.576	26	.138		
	Total	6.353	29			

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	.877	.604		1.452	.158
	HRM practices	.740	.225	.528	3.287*	.003
2	(Constant)	.116	.838		.139	.890
	HRM practices	.805	.228	.574	3.530*	.002
	Differentiation Strategy	.234	.181	.210	1.293	.207
3	(Constant)	.100	.777		.129	.898
	HRM practices	.819	.212	.584	3.869*	.001
	Differentiation Strategy	.223	.168	.201	1.330	.195
	HRM practices*Differentiation strategy	.171	.074	.342	2.321*	.028

a. Dependent Variable: Competitive Advantage

b. Predictors: (Constant), HRM Practices

c. Predictors: (Constant), HRM Practices, Differentiation Strategy

d. Predictors: (Constant), HRM Practices\* Differentiation Strategy, Differentiation strategy

c. \*P&lt;0.05

### ***Step Three: HRM Practices, Differentiation Strategy and HRM Practices\*Differentiation Strategy***

In step 3 the interaction term was added to the regression model. All the variables comprising HRM practices, differentiation strategy and the interaction term were entered in the regression model. The results reveal that the value of  $R^2$  increased by 11.7 percent from .321 to .437 ( $R^2$  change =.117) when the interaction term (HRM practices\*differentiation strategy) was added to the regression model.  $R^2$  for the interaction at ( $R^2=0.437$ ,  $F=6.732$ ,  $p<0.05$ ).The results further indicate that the effect of interaction between HRM practices and differentiation strategy was statistically significant ( $\beta=0.171$ ,  $t= 2.321$ ,  $p<0.05$ ) implying that a unit change in the interaction term between HRM practices and differentiation strategy causes 17.1 percent increase on competitive advantage. Based on these results, the hypothesis that differentiation strategy moderates the relationship between HRM practices and competitive advantage was confirmed.

The objective was to determine the moderating effect of differentiation strategy on the relationship between HRM practices and competitive advantage. The first finding was that differentiation strategy has a positive and statistically significant influence on the relationship between HRM practices and competitive advantage. This means that with the introduction of differentiation strategy into the regression model, the ability of the HRM practices to predict competitive advantage increased from ( $R$  square=.278.  $F=10.807$ ,  $p<0.05$ ) to ( $R$  square=0.321,  $F=6.370$ ,  $p<0.05$ ). These findings imply that differentiation strategy enhances the influence of HRM practices on competitive advantage.

## **DISCUSSION AND CONCLUSION**

Strong evidence exists in literature that shows that different HRM practices have a positive association with firms' competitive advantage (Huselid, 1995; Pfeffer&Veiga, 1999, Wright & McMahan, 1999; Truss, 2001). If HRM practices are properly configured for competitive advantage, they can be used for benchmarking with the competitors firm. In this case it could be easily replicated by competitors and therefore not likely to provide a source of sustainable competitive advantage. Several studies have suggested that many firms view differentiation strategy as a more important and distinct means to achieve competitive advantage. HRM practices should therefore be linked with others HRM practices to create a HRM system that should be integrated with differentiation strategy for sustainable competitive advantage that is not easily imitated by the competitors (Schuler & Jackson, 1987a).

This study is consistent with Schuler and Jackson (1989) who studied the determinants of HRM priorities and implications for industrial relation. He found that firms pursuing a differentiation strategy are hypothesized to place a higher priority on human resource innovation

than firms pursuing a cost efficiency strategy. Similarly, Sagwa (2014) studied the HRM practices and performance of firms listed on the Nairobi Securities Exchange. He established that competitive strategy has a positive and statistically significant influence relationship between employee's outcomes and performance. Employee's outcomes such as commitment, competence and empowerment which are as result of HRM practices implementation have a significant effect on firm performance especially when they are aligned with the firms competitive strategy on aspects like cost leadership, differentiation and focus strategy as evidenced by his study.

This study agrees with Neal, West and Patterson (2005) who examined the effectiveness of HRM practices on organizational climate and competitive strategy. The concepts of internal and external fit suggest that that there positive relationship between HRM and subsequent productivity will be stronger for firms with positive organization climate and for firms using differentiation strategies. Changing business environment has made adoption of HRM practices imperative for competitive advantage.

Configurational theory suggests the importance of coordinating HRM systems to enhance horizontal fit, and then linking HRM systems to the business strategy to maximize vertical fit (Delery& Doty 1999). HR practices should be linked to organizational strategy but these practices they need also to be strategically linked to each other to ensure that they are promoting the same goals (Wright & McMahan, 1992). This is in line with the findings of the current study that differentiation strategy moderates the relationship between HRM practices and competitive advantage. Differentiation strategy can enhance firm's competitive advantage when they are aligned with HRM practices. Both universalistic and configurational theories were supported by the findings of this study.

## **CONTRIBUTIONS TO THE THEORY, KNOWLEDGE AND PRACTICE**

The study confirmed that there is evidence to supports the moderating effect of differentiation strategy in the relationship between HRM practices and competitive advantage. The results of the study therefore have implication for theory, practice and policy.

The findings of this study are consistent with underpinning theories of this study. This study was anchored on two theories which included; configuration and universalistic. These theories were used to ground the arguments and concepts that enabled the study to be carried out. The grounded theoretical framework facilitated an informed investigation of the key variables and concepts.

Configurational theorists propose that firms must develop an HR system that achieves both vertical and horizontal fit in order to achieve competitive advantage (Delery & Doty, 1996). Drawing from configurational theory foundations, seven HRM practices referred as strategic were formulated based on bundling and aligned with differentiation strategy. The concept of bundling can be applied to competitive advantage regardless of industry or sector. When HRM practices are treated as a bundle and aligned to differentiation strategy, they contributed to competitive advantage of companies listed on the Nairobi Securities Exchange. This study confirmed that differentiation strategy moderates the relationship between HRM practices and competitive advantage.

HRM practices used in this study were drawn from the universalistic theory. The study confirmed that universalistic HRM practices lead to competitive advantage (Pfeffer, 1999). Pfeffer (1998) and Kidombo (2007) proposed seven HR practices that can influence the firm's competitive advantage. They include seven HRM practices as internal career opportunities, training and development, retention strategies, performance appraisal, reward strategies and employee relations. The seven HRM practices adopted by this study contribute to competitive advantage of companies listed on Nairobi Securities Exchange.

The purpose to this study was to determine the moderating role of differentiation strategy in the relationship between HRM practices and competitive advantage of firms listed on Nairobi Securities Exchange. To achieve these objectives, configurational, universalistic were used to examine and analyse the relationships. This study, hopefully, helps to fill this knowledge gap and enhance our understanding of the role of HRM practices and differentiation strategy on the competitive advantage of firms listed on Nairobi Securities Exchange.

The results of this study contribute to knowledge by confirming that differentiation strategy moderates the relationship between HRM practices and competitive advantage. These empirical findings are important and represent substantial contribution on literature and theory development for HRM practices, differentiation strategy and competitive advantage.

As far as policy is concerned the results of this study have implications for the government and the private sector. The study shows that HRM practices has effect on competitive advantage. The companies listed on the Nairobi Securities Exchange have been regarded as the major contributors of human capital in Kenya. Therefore, the findings of this study should assist the practitioners in policy making. Policies should be developed in areas of HRM practices, differentiation strategy and competitive advantage. In HRM practices, policy can be applied in the areas of career opportunities, retention, training and development, performance appraisal, reward strategy, employee relations and overall human resource management.

## LIMITATIONS OF THE STUDY

The entire population comprised only 62 companies listed on the Nairobi Securities Exchange which is relatively small. The external validity of the current study may be in question since the data belong only to Kenyan firms listed on the Nairobi Securities Exchange, which are few compared to those listed on other stock exchanges in many parts of the world. The study used cross-sectional design whereby the study was carried out at a specific moment in time. Although this may save time (given the time constraint of the study) it may also limit deeper investigations of many other possible causal relationships in the study. Therefore, a longitudinal study would probably provide more insightful findings of the study.

## RECOMMENDATIONS FOR FUTURE RESEARCH

The researcher suggests that future research studies should be conducted using a different population and contexts. Future researchers could also consider introducing different variables other than HRM practices, differentiation strategy and competitive advantage in testing for moderation effect of such variables on the relationship between HRIS and competitive advantage. The data was collected from the HR managers only. This is likely to bring common method bias. Future researchers should incorporate multiple sources such as line managers, workers, customers, suppliers and other stake holders of the company.

The study only used self-administered survey questionnaire. The researcher assumed that the responses would provide honestly and by a target group. Since it is not possible to ascertain this assumption, different instruments should be considered in future. The study confined itself to quantitative data collection methods and analysis. Future research could use both quantitative and qualitative data collection methods, which could probably obtain richer data and results.

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