

# Impact of Psychological Climate & Transformational Leadership on Employee Performance

Soumendu Biswas

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*The perceptions of an employee about his/her work environment play a predictive role in determining his/her level of job satisfaction. Similarly, managerial leadership that is based on leader-member trust and non-formal methods of communication also increases the meaningfulness of job interpretation. This in turn leads to improved individual performance which, when summated, leads to an overall improvement in organizational effectiveness. The present paper attempts to study the influence of psychological climate and transformational leadership on job satisfaction which in turn leads to better levels of employee performance. Data for the present study were collected from manufacturing as well as service sector organizations all over India.*

**Soumendu Biswas** is Assistant Professor, Management Development Institute, Gurgaon 122001. E-mail: sbiswas@mdi.ac.in

## Introduction

India is a country with a rich heritage of national culture. To a large extent, the socio-economic values and actions of Indians can be attributed to their long cultural history. Further, these cultural characteristics are deeply ingrained in the individual mindsets and markedly influence their cognitions and affect in their personal, social, and professional environment (Rao & Abraham, 2003). At the same time, the indigenous culture of India has readily accepted alien customs and traditions while preserving its unique cultural norms and legacies (Biswas et al, 2006). This has put the Indian social order as a classic example in the map of the South East Asian cultural geography. With reference to the crossvergent socio-cultural ethos therefore, India stands as a pioneer in establishing norms and reciprocities that govern managerial policies and procedures, especially in the light of the contemporary boundariless business environment (Ralston et al, 1997). In a cross-cultural framework, the preceding discussion indicates the elevated status

of India in the global socio-cultural atlas. In as much as Varma, Budhwar, Biswas, and Toh (2005) have remarked that India's traditional cultural systems are acting as a fulcrum for the South East Asian business environment.

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It has been observed that during periods of environmental confusion and chaos, societies in emerging economies such as India follow a path of least-resistance that leads to stability. They accomplish this by falling on their prosperous cultural tradition that acts as a timely buffer. This implies that in order to maintain internal cohesion and familiarize themselves with the external transformations such societies focus on retaining certain behavioural models that are local and at the same time welcome some customs and mores that are foreign and novel. Given that organizations function within the domains of social norms and values, it becomes an issue that needs further examination in the context of such behavioural singularities. On the basis of this supposition, the objective of the current study was formulated wherein the inter-relationship between three behavioral constructs were examined namely, transformational leadership, job satisfaction, and employee performance. More specifically, the present study investigates the causal impact of transformational leadership on employee perfor-

mance through job satisfaction which acts as the mediator variable.

### **Theoretical Background**

Prior to the introduction of New Economic Policy (NEP) in 1991, Indian business environment was apparent through the supremacy of firms in the manufacturing sector. These firms, whether public or private, were usually large organizations and were marked by mechanistic processes and bureaucratic practices (Biswas & Varma, 2007). In fact, firms belonging to the service sector such as, educational institutions, healthcare organizations, and media and communications were basically owned by the state. This was a direct consequence of the Nehruvian welfare philosophy that emphasized pluralistic utilitarianism. The fallout of such a socio-political arrangement was the lack of emphasis on individual aspirations and expectations (c.f. Varma, et al., 2005). Thus, till the privatization of the Indian economy in the early 1990s, Indian organizations were extremely bureaucratic and were characterized by one-way flow of decision making from the top to the bottom. Indeed, Hofstede (2001) observed that such managerial philosophies and practices are not uncommon in social cultures that are dominated by collectivism and high power distance norms.

However, with the liberalization of the Indian business environment managerial practices especially those related to cognitive and affective facets of individual employees at the workplace underwent major alterations. Furthermore,

human resource (HR) practices in Indian firms have experienced a sea change, as contemporary HR policies and practices are designed in a manner that promotes individual involvement on-the-job and encourages extra-role behaviour in addition to the in-role behaviour of employees (Biswas, 2006; Budhwar & Khatri, 2001; Pattnaik & Biswas, 2005). As Biswas and Varma (2007:666) observed “HR practices in India are increasingly geared towards improving the way individual employees perceive their day-to-day working environment, or the way they perceive the *psychological climate* [italics added] in the workplace”.

Thus, to understand the group of actions in relation to the administration of members of an organization, the appropriate literature recommends an investigation of those variables that are related to an individual’s acuity a propos their immediate workplace atmosphere based on their everyday experiences (Schneider, 1975; Strutton, Pelton & Lumpkin, 1993). The relevant literature recommends the examination of psychological climate as a primary antecedent of a variety of individual-level outcomes such as organizational commitment, job satisfaction, job involvement, and organizational citizenship behaviour (James, James & Ashe, 1990; Parker et al, 2003; Woodard, Cassill & Herr, 1994). This article seeks to empirically inspect these theoretical suggestions in the context of Indian management scenario.

Leadership refers to encouraging followers to track collective or at least joint objectives that symbolize the values

and drive of both leaders and followers (Krishnan, 2003). Thus the concern for the need and requirements of the followers is at the core of leadership principles and practices. Tichy and Devanna (1986) noted that the real need of followers was fulfilled by leaders who did not utilize their followership to attain their own ends, but who endeavored towards the realization of mutual development. Burns (1978) further notes that such leadership, which may be termed a moral leadership in itself could not be a driver of need fulfillment of the followers unless it took the form of transformational leadership. According to Burns (1978:20), transformational leadership “... occurs when one or more person engage with others in such a way that leaders and followers raise one another to higher levels of motivation and morality ...”

In continuation, literature reveals that transformational leadership is a significant correlate of the amount of effort exerted by followers, leader-member satisfaction, employee performance, and overall effectiveness of individuals and by extension, of the organization (Bass, 1998). According to Kirkpatrick and Locke (1996), the leader’s vision and its implementation through job indications positively affect subordinates’ performance and attitudes. Thus, organizational policy makers should recognize that effective courses of action can be devised if one keeps in mind the role of transformational leaders as a predictor of such guidelines and practices.

According to Bass and Avolio (1994), transformational leadership contributes to

organizations' attempts at improving operations by optimal utilization of its human resources. In order to do so, transformational leaders must chalk out appropriate designs related to HR practices and policies that are geared towards greater autonomy and augmented individual performance. In this connection, it was observed that transformational leadership led to follower-organization value congruence, which as a result, became a significant source of various positive outcomes in organizational and human resource management practices (Seltzer & Bass, 1990; Yammarino & Atwater, 1997).

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Job satisfaction has been defined as "a pleasurable or positive emotional state resulting from the appraisal of one's job or job experience" (Locke, 1976:1300). Wanous and Lawler (1972) identified several different operational definitions of job satisfaction examining different facets and their combined effect in providing a general understanding of the job satisfaction construct. Job satisfaction has been found to be a multidimensional construct manifesting the emotional evaluations of individuals regarding their expectations and how well they have been met. Schnake (1983) conceptualized three dimensions of job satisfaction representing its intrinsic, extrinsic, and social aspects. In effect, Schnake's (1983) dimensions of job satisfaction

cover cognitive and affective responses made by individuals in connection to their work environment.

Literature suggested that there are two forms of work performance – in-role and extra-role (Brief & Motowidlo, 1986; Williams & Anderson, 1991; Wolfe Morrison, 1994). In-role performance referred to an employee's action to fulfill the requirements of his/her job description (Williams & Anderson, 1991), whereas extra-role performances were those that were outside the formal role requirements and are at the employee's discretion (George & Brief, 1992).

Studies suggested that participatory management practices such as open communication and participatory leadership style would be positively associated with higher levels of employee performance on both the counts, viz. in-role and extra-role performance. Indeed, such practices would enhance an employee's level of job satisfaction leading to better performance.

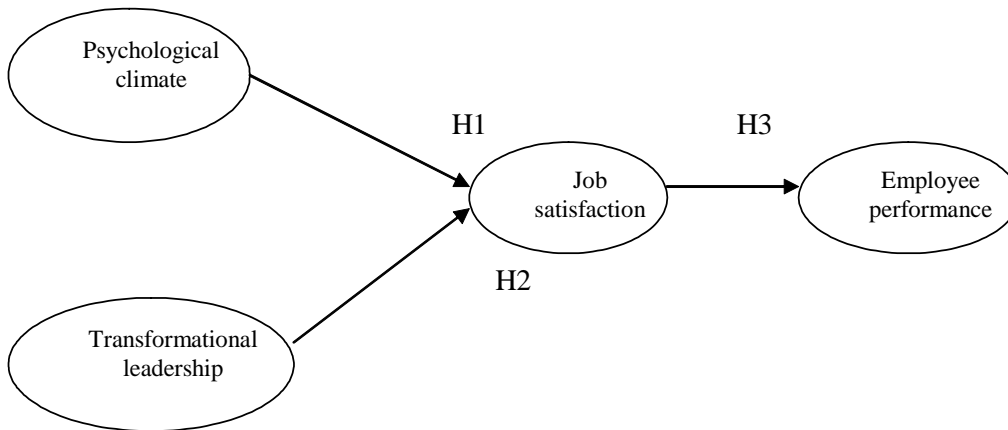
Based on the discussion above, the following hypotheses were formulated for the purpose of empirical testing:

- H1: Psychological climate will have a significantly positive impact on job satisfaction of individual employees at work;
- H2: Transformational leadership style will positively and significantly influence an individual employee's level of job satisfaction; and,

H3: An employee with high level of job satisfaction will exhibit higher levels of performance.

The three hypotheses above are presented schematically in the following path diagram:

**Fig. 1 Path Model Associating the Latent Constructs**



**Sample**

For the purpose of the present study, data was collected, first through randomly selecting Indian organizations, irrespective of their zonal locations, through the Yellow Pages directory. Further, a random selection of twenty organizations was made. Subsequently, the HR department of the selected firms was contacted in order to gain permission to collect data. Nine of the twenty organizations agreed to participate in the survey research. A list of participants who voluntarily agreed to fill the survey questionnaires was then collated. Based on the availability of the participants during the data collection period, four hundred questionnaires were distributed. Of these, three hundred and fifty seven participants returned completely filled-in and analyzable questionnaires which were subsequently subjected to statisti-

cal procedures. Thus, the response rate of the study was nearly 90%.

For the study, participants who were managerial level employees in their organizations were selected. Three levels of managerial executives were considered to fill the study questionnaire, viz. those belonging to the senior, middle, and junior management cadres. It was found that the average age of the participants was thirty-seven years. Moreover, they had a mean work experience of eleven years. Out of these three hundred and fifty seven participants, 83.9% were male, while 16.1% were females. With respect to the designation of the participants, 7.3% belonged to the senior level of management, 35.6 % to the middle managerial level, and 57.1 % belonged to the junior management cadre.

## Measures

To measure the major variables of the study, items were selected from the standardized questionnaires. The participants of the survey indicated their choice of response through a five-point scale. Furthermore, the respondents' demographic details were elicited through five items.

*Psychological climate* was calculated using the Psychological Climate Measure as reported by Brown and Leigh (1996). This scale comprised six factors of psychological climate namely, supportive management, role clarity, contribution, recognition, self-expression, and challenge and included 21 items. The reliability measure of this scale was found to be .83.

*Transformational leadership* was measured using the multifactor leadership questionnaire (MLQ) form 5X (Bass & Avolio, 1995). It comprised five factors which were idealized influence (attributed), idealized influence (behavioral), inspirational motivation, intellectual stimulation, and individual consideration and was manifested by 21 items. The Cronbach's alpha of this scale was .93.

*Job satisfaction* was measured using the 11 item Job Satisfaction instrument covering the three dimensions of satisfaction, namely, intrinsic, extrinsic, and social satisfaction as reported by Schnake (1983). Three items were used to measure extrinsic satisfaction, four items to measure intrinsic satisfaction, and four items were used to measure

social satisfaction. The Cronbach's alpha for this scale was .85.

*Employee performance* was measured using Lynch, Eisenberger and Armeli's (1999) Employee Performance Scale. This scale comprised a total of 16 items, of which 9 measured in-role, and 7 measured extra-role performance. Participants had to indicate the most appropriate response within a range of 1=strongly disagree to 5=strongly agree. The reliability index as represented by the Cronbach's alpha was .84.

## Data Analysis Technique

The Statistical Package for Social Science version 10.0 (SPSS 10.0) and the Analysis of Moments Structure (AMOS 4.0) were used to analyze the data. The statistical analyses that were conducted included a measurement and a structural equation model (SEM). The path model based on the hypotheses emerging out of the review of literature was subjected to structural equation analysis and fit tests. Apart from the regression analysis, a variety of statistics including the normed Chi-square ( $X^2/d.f.$ ), goodness-of-fit, centrality parameters, and normed-fit-indices as provided by AMOS 4.0 (Arbuckle & Wothke, 1999) were utilized to achieve the results.

## Results

In Table 1, the means, standard deviations, correlations, and the reliability indices of the key variables of the study are described. It was found that psychological climate correlated significantly

with job satisfaction ( $r=.63, p<.01$ ). Moreover, the correlations between transformational leadership and job satisfaction ( $r=.60, p<.01$ ), as did job satisfaction with employee performance ( $r=.67, p<.01$ ).

**Table 1: Descriptive Statistics, Correlations and Reliability Indices (N=357)**

	Mean	S.D.	1	2	3	4
1. Psychological climate	3.65	.53	(.83)			
2. Transformational leadership	3.39	.80	.67**	(.93)		
3. Job satisfaction	3.40	.65	.63**	.60**	(.85)	
4. Employee performance	3.56	.55	.55**	.53**	.67**	(.84)

\*\* $p=.01$

Values in parentheses represent Cronbach's alpha

Furthermore, the causal linkages between the variables were examined through regression analysis. Table 2 presents the standardized regression estimates between the key constructs. As shown in this table, psychological climate significantly influences the designing of job satisfaction (standardized  $\beta = .58$ ,

C.R. = 6.68). Similarly transformational leadership significantly predicts job satisfaction (standardized  $\beta = .24$ , C.R. = 3.34). It was also found that job satisfaction had a significant impact on employee performance (standardized  $\beta = .78$ , C.R. = 13.84).

**Table 2: Regression Estimates**

	Standardized $\beta$	C.R.
Psychological climate à Job satisfaction	.58	6.68
Transformational leadership à Job satisfaction	.24	3.34
Job satisfaction à Employee performance	.78	13.84

A review of literature related to Structural Equation Modeling (SEM) procedures suggested that the level of significance is based on the critical ratio (C.R.) of the regression estimate (Byrne, 2001). Thus, when C.R. values are greater than or equal to 2.58, it indicates a 99% level of significance. However, when C.R. values are greater than or equal to 1.96 but less than 2.58, it indicates a 95% level of significance.

Moreover, to calculate the fit indices which explain the relationships between

the hypothesized paths between the latent constructs, AMOS 4.0 SEM procedure was resorted to (Arbuckle & Wothke, 1999). For this purpose Maximum Likelihood Estimation (MLE) algorithm in order to determine the fit indices was used. Hence, the Goodness-of-Fit Index (GFI) and the Root Mean Square Error of Approximation (RMSEA) were reported as the absolute fit measures. According to Byrne (2001), absolute fit measures were used to compare the hypothesized model in the absence of any other model. Thus, the Tucker-Lewis

Index (TLI), the Normed Fit Index (NFI), and the Comparative Fit Index (CFI) are also mentioned. These indices indicate a comparison between the model that was hypothesized and the model with maximum constraints. Finally, the normed chi-square value was also considered as an acceptable measure of fit.

According to Hair, Andersen, Tatham and Black (1998), the recommended fit values for GFI, TLI, NFI, and CFI are  $> 0.90$ . Likewise, while an RMSEA of 0.0 indicates perfect fit, values that are less than 0.07 are considered as good fits. The range of the normed chi-square is generally accepted as  $1.00 < \text{normed chi-square} < 3.00$  (Hair et al., 1998). Finally,

the Adjusted Goodness-of-Fit (AGFI) as well as the Parsimony-adjusted Goodness-of-Fit (PGFI) measures were also reported.

Table 3 shows the fit measures of the proposed model. For the model as depicted in Fig. 1, the normed  $\chi^2$  value is 2.69. The GFI is 0.91, which is above the recommended value. The TLI is equal to .95, the NFI value is 0.93, and the CFI value is 0.96. These values are also much above the recommended values for the respective indices. With the threshold value of RMSEA being 0.07, the value of RMSEA for the proposed model is 0.07. Finally, the AGFI and the PGFI values are equal to .86 and .73 respectively.

**Table 3: Fit Indices**

Fit Indices	GFI	AGFI	PGFI	TLI	NFI	CFI	RMSEA	Normed $\chi^2$
Proposed Model	.91	.86	.73	.95	.93	.96	.07	2.69
Independence Model	.19	.12	.17	.00	.00	.00	.23	20.73

### Mediator Analysis

The history of mediator analysis is quite long and significant in the area of social science research (Alwin & Hauser, 1975; West & Wicklund, 1980). Here we followed the guidelines proposed by the relevant literature in this area (Baron & Kenny, 1986; MacKinnon, Warsi & Dwyer, 1995). With the aim of placing organizational commitment as the mediator variable, the following two conditions were taken into account:

1. Whether the direct path from the antecedent to the consequents were greater than the paths under the condition of mediation

2. Whether the direct path from the predictors to the criteria under the mediated condition was significant.

Since, condition (1) was negative and condition (2) was positive, the results showed that job satisfaction is a full mediator between the predictors, i.e. psychological climate and transformational leadership and the criterion variable, i.e. employee performance. These results are presented in Table 4.

### Discussion & Conclusions

According to Cowling and Newman (1995) socio-political upheavals lead to environmental transitions which in turn affect organizations and their members.

**Table 4 Analysis of Job Satisfaction & Job Involvement as Mediator Variables**

	Whether (direct path) > (direct path under mediated condition)?	Whether (direct path under mediated condition) is significant?	Results of the mediator analysis	% of explained mediation
Psychological climate → job satisfaction → Employee performance	No	Yes	Job satisfaction is a full mediator	73.92
Transformational leadership → job satisfaction → Employee performance	No	Yes		67.74

Such changes in the business environment lead to quite a few adjustments at the individual as well as the organizational levels. At the individual level, the primary factor that is affected would be individual perceptions about one's immediate environment (Martin, Jones & Callan, 2005). A perception about one's immediate work environment is what is known as psychological climate. Thus, changes in the business environment do have an impact on psychological climate which in turn affects many other individual behaviour and outcomes.

**A perception about one's immediate work environment is what is known as psychological climate.**

The present study takes a cue from these past conclusions and notes that perceptions of organizational members become critical data for understanding and interpreting individual behaviour and attitudes. Such understanding shows that

climate variables, individually interpreted, become pointers for an employee's level of job satisfaction (Drexler, 1977). Similarly, interaction between group members, supervisor subordinate relationship, and an individual's own perception about his/her job description also play a role in attitudinal outcome related to their jobs.

Work environment and its relationship to work related attributes and behavior suggest that work-place climate has a significant consequence on employees' perception about the work context. In so far as the construct of climate is concerned and extensive studies have confirmed (Katz & Kahn, 1978) that description of role clarity, supervisory support, and perhaps more importantly, an employee's perception about the various human resource policies and practices go to create a day-to-day environment of enjoyment and satisfaction. The above arguments are corroborated through the acceptance of the first hypothesis, that is, psychological climate will have a sig-

nificantly positive impact on job satisfaction of individual employees at work.

As the discussion above points out, individual and group level behavioural factors have significant impact on individual level outcomes. In this context, Bryman (1992) found that an important predictor of individual level outcomes, such as perceived extra effort at work, organizational citizenship behaviour, and job satisfaction was transformational leadership. Similar to psychological climate, transformational leadership was also found to influence employee-related outcomes during periods of intense economic competition that required higher levels of creativity and innovativeness (Howell & Avolio, 1993; Keller, 1992; Niehoff, Enz, & Grover, 1990). Thus, during these periods there are higher expectations about goal achievement. Due to the consequent role clarity provided by transformational leadership, it is expected that these enhanced goals shall be achieved and there is a general atmosphere of euphoric anticipation which leads to higher levels of job satisfaction.

Moreover, transformational leaders are those who enthuse and inspire their followers and base their relationship on mutual understanding and trust which involves fruitful non-verbal communication. Such leadership behaviour inculcates a sense of self belief and confidence in the followers. This in turn, would make employees less lackadaisical and open to more meaningful interpretation of their work related roles. This is the process by which transformational leadership affects individual job satisfaction levels.

**Transformational leadership would significantly and positively influence an employee's level of job satisfaction.**

The argument posited above supports the findings of the results wherein it was hypothesized that transformational leadership would significantly and positively influence an employee's level of job satisfaction, and where this hypothesis was found to be true, and thus accepted.

In this connection, positive levels of psychological climate and transformational leadership, leading to higher levels of individual employees' job satisfaction were hypothesized to lead to higher levels of employee performance. This implied that satisfied employees who are themselves enthused enough about their work roles will display higher levels of in-role and extra-role performance. As Voss, Keller, Ellinger, and Ozment (2004) observe that augmented job satisfaction would result in higher levels of employee productivity in conjunction with employee group behaviour. Indeed, in today's business environment, transformational leadership, by generating higher levels of job satisfaction ensures that employees are more motivated and that they perform even better.

In this context, what is posited to happen in a practical context is that an employee who is satisfied with his/her job, that is, in other words enjoys job satisfaction will definitely not wish to run down his/her *status quo* and would strategize to maintain the same (i.e. the

current level of high job satisfaction) by displaying continuous improvement with regard to in-role as well as extra-role performance, the summation of which would reflect his/her overall job performance as an employee. The above argument presumes that job satisfaction improves employee performance within ambit of day-to-day organizational life.

The above arguments provide justification for the acceptance of the third hypothesis that an employee with high level of job satisfaction will exhibit higher levels of performance.

**Employee with high level of job satisfaction will exhibit higher levels of performance.**

In the context of a liberalized and globalized business environment, there is a gradual shift of focus from the manufacturing sector to the service sector. Apart from this, there is also a notable decline in union-related activities. The fallout of this is a reduction in inter-departmental and/or inter-divisional rivalries and antagonism and promotion of a culture where co-workers are looked upon as internal customers. This has led to greater cordiality and harmony at the workplace which has in turn, improved individual employees' perceptions about his/her immediate work environment, making them more satisfied with his/her job. As a result, this has improved individual performance the overall effect of which has been an enhancement of organizational effectiveness.

Furthermore, with increasing competition and superior levels of performance expectations, employees are now required to achieve higher targets than before. Thus, the element of challenge has increased in the present work context and meeting these challenges are intrinsically rewarding and satisfying at the individual level and it encourages employees to perform better. While the element of job satisfaction leading to better performance is clear from this argument, what is also revealed is that in such a climate of overall enhanced performance, there shall be a significant improvement in organizational effectiveness.

With regard to the limitations of the present study, it is believed that the predictor variables could have included organizational culture and its strength in shaping up psychological climate. Future researchers in this area may examine relationships among the variables of the present study and look into the similarities and differences with respect to different industries, ownerships, and types of products and also include organizational climate, an organizational level construct along with psychological climate, an individual level construct as a predictor for the outcomes presented in the model of the present study.

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