

**LEADERSHIP STYLES, EMPLOYEE WORK
BEHAVIOURS AND INNOVATION IN THE
PAKISTANI SMALL AND MEDIUM
ENTERPRISES SECTOR**

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LEADERSHIP STYLES, EMPLOYEE WORK BEHAVIOURS AND
INNOVATION IN THE PAKISTANI SMALL AND MEDIUM
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ALI JAVED

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ABSTRACT

Recognizing the significance of rapid responsiveness and innovation in today's business climate, a study has been conducted to identify the predictors that drive innovation and responsiveness in the SME sector of Pakistan. The study focused on two leadership styles, "transformational leadership and empowering leadership", as independent variables to investigate the relationship with two dependent variables, "firm innovativeness and market responsiveness", through the two employee behaviors as the mediators, "innovative work behavior and proactive work behavior". The study aimed to fill the gap left by previous studies by examining these relationships from the perspective of employee behaviors as the mediation, which was an area of negligence. The study addresses the literature gap by examining market responsiveness, a less explored construct in innovative marketing. It investigates how leadership and employee behaviors influence this market responsiveness. The study is also unique in a way that it used dimensions of the variables as well as testing the relationships with other variables. The study followed the positivism paradigm as philosophy, deductive as the research approach, and survey method as the research strategy. Data was collected from 384 respondents in 13 cities in Punjab, Pakistan, through stratified random sampling technique. Respondents were both leaders and their followers (subordinates) working in the SME sector of Pakistan. The results showed that transformational leadership is a good predictor variable for innovative and proactive work behavior, firm innovativeness, and market responsiveness. Empowering leadership was also found to be a good predictor of innovative and proactive behavior, but not for innovativeness and responsiveness. Proactive work behavior was found to be a reliable indicator for both firm innovativeness and market responsiveness. Despite assumptions, it is found that innovative work behavior does not significantly influence firm innovativeness and market responsiveness. Moreover, proactive work behavior was found to mediate relationships between leadership styles and innovation, but innovative work behavior does not. Findings suggest that organizations should prioritize the cultivation of transformational leadership, promote proactive work behavior, and prioritize quick market responsiveness and innovation to stay ahead of the competition.

Keywords: Transformational leadership, empowering leadership, innovative work behavior, proactive work behavior, firm innovativeness, market responsiveness.

APPROVAL

This is to certify that this thesis conforms to acceptable standards of scholarly presentation and is fully adequate, in quality and scope, for the fulfilment of the requirements for the Degree of Doctor of Philosophy.

The student has been supervised by: **Professor Dr Juhary Ali & Dr Swa Lee Lee**

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(8 March 2025)

DECLARATION

I hereby declare that the thesis submitted in fulfilment of the requirements for the Degree of Doctor of Philosophy is my own work and that all contributions from any other persons or sources are properly and duly cited. I further declare that the material has not been submitted either in whole or in part, for a degree at this or any other university. In making this declaration, I understand and acknowledge any breaches in this declaration constitute academic misconduct, which may result in my expulsion from the programme and/or exclusion from the award of the degree.

Name: Ali Javed

A handwritten signature in black ink, appearing to read 'Ali', written in a cursive style.

Signature of Student:

Date: 8 March 2025

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I dedicate this thesis to my beloved parents, who have been the pillars of my success and the driving force behind my academic achievements

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TABLE OF CONTENTS

ABSTRACT	ii
APPROVAL	iii
DECLARATION	iv
ACKNOWLEDGMENTS	vi
TABLE OF CONTENTS	vii
LIST OF TABLE	x
LIST OF FIGURES	xi
LIST OF ABBREVIATIONS	xii
CHAPTER 1 INTRODUCTION	1
1.0 Chapter's Context	1
1.1 Background of the Study	1
1.1.1 Background of the SME Sector of Pakistan	4
1.2 Problem Statement	6
1.3 Purpose of the Study	14
1.4 Research Questions	15
1.5 Significance of the Study	16
1.5.1 Significance for the Organizational Leaders	16
1.5.1 Significance in the Literature	17
1.5.1 Significance in the Cultural Context	18
1.6 Limitations of this Study	18
1.7 Personal Motivation for Choosing the Topic	19
1.8 Operational Definitions of Variables	19
1.8.1 Transformational Leadership	19
1.8.2 Empowering Leadership	20
1.8.3 Innovative Work Behavior	21
1.8.4 Proactive Work Behavior	21
1.8.5 Market Responsiveness	21
1.8.6 Firm Innovativeness	22
1.9 Chapter Summary	22
CHAPTER 2 LITERATURE REVIEW	24
2.0 Chapter's Introduction	24
2.1 Transformational Leadership	24
2.1.1 Idealized Influence (II)	26
2.1.2 Inspirational Motivation (IM)	27
2.1.3 Intellectual Stimulation (IS)	27
2.1.4 Individualized Consideration (IC)	28
2.2 Empowering Leadership	29
2.3 Innovative Work Behaviors (IWB)	31
2.3.1 Idea Generation	32
2.3.2 Idea Promotion	33
2.3.3 Idea Realization:	33
2.4 Proactive Work Behaviors (PWB)	33
2.4.1 Personal Initiatives	34
2.4.2 Taking Charge	35
2.4.3 Voice	36
	vii

2.5	Firm Innovativeness	36
2.5.1	Product Innovation	38
2.5.2	Process Innovation	38
2.5.3	Administrative Innovation	38
2.6	Market Responsiveness	40
2.6.1	Market Sensitivity	41
2.6.2	Customer Focus	41
2.6.3	Competitor Orientation	41
2.6.4	Inter-functional Coordination	41
2.7	Literature Review Synthesis	42
2.8	Leadership (TL, EL) and Work Behaviors (IWB, PWB)	48
2.9	Work Behaviors and Innovation (Innovativeness, Responsiveness)	53
2.10	Leadership and Innovation (Innovativeness, Responsiveness)	57
2.11	Work Behaviors (IWB, PWB) as the Mediation Mechanism	62
2.12	Supporting Theories	67
2.13	Chapter's Summary	68
CHAPTER 3 METHODOLOGY		70
3.0	Chapter's Introduction	70
3.1	Research Design	70
3.1.1	Mode of Inquiry	70
3.1.2	Application	71
3.1.3	Objective Type	72
3.1.4	Type of Research Design	74
3.2	Paradigm	75
3.2.1	Types of Paradigm	76
3.2.2	Burrell and Morgan Model	77
3.3	Target Population & Sampling Frame	80
3.4	Respondents and Procedure	85
3.4.1	Respondents	85
3.4.2	Procedure	90
3.5	Ethical Consideration	91
3.6	Research Onion	92
3.7	Instrument	95
3.7.1	Pilot Study and Content Validity	97
3.8	Measures	99
3.9	Data Analysis to be Used	102
3.10	Chapter Summary	102
CHAPTER 4 RESULTS & ANALYSIS		104
4.0	Introduction of Chapter	104
4.1	Data Normality & Screening	104
4.2	Scale Reliability	107
4.3	Respondents Profile	111
4.4	Descriptive Statistics	117
4.5	Factor Analysis	118
4.5.1	Exploratory Factor Analysis	120
4.5.2	Confirmatory Factor Analysis	125

4.6	Composite Reliability	130
4.7	Content Validity	131
	4.7.1 Convergent Validity	131
	4.7.2 Discriminant Validity	132
4.8	Multicollinearity Analysis	134
4.9	Structural Equation Modeling (SEM) for Hypothesis Testing	136
	4.9.1 SEM 1st Order Model	137
	4.9.2 SEM 2nd Order Model	146
	4.9.3 Mediation Analysis	159
4.10	Chapter Summary	169
CHAPTER 5 DISCUSSION & CONCLUSION		171
5.0	Introduction of the Chapter	171
5.1	Motivation for the Study	171
5.2	Discussing Statistical Tests Applied	173
5.3	Discussion of Test Results	177
5.4	Discussion of Hypothesis Test	180
	5.4.1 Summary of Hypothesis Results	194
5.5	Answers to Research Questions	197
5.6	Theoretical and Practical Implications	198
	5.6.1 Theoretical implications	199
	5.6.2 Practical Implications	203
5.7	Limitations of the Study & Future Research Recommendation	206
5.8	Conclusion	208
REFERENCES		212
APPENDICES		241
	Appendix A	241

LIST OF TABLE

Table 1.1	Criteria of SME	4
Table 2.1	Literature Review Synthesis	43
Table 3.1	Sampling Frame of Selected Cities	83
Table 3.2	Krejcie and Morgan (1970) Sample Size Table	86
Table 3.3	Reliability Analysis of Questionnaire Pilot Study	97
Table 3.4	Scale and Items	99
Table 4.1	Skewness and Kurtosis Test	106
Table 4.2	Scale Reliability	109
Table 4.3	Respondent's Profile	112
Table 4.4	Response Rate	116
Table 4.5	Mean and Standard Deviation of Variable	118
Table 4.6	KMO and Bartlett's Test	120
Table 4.7	Summary of EFA	121
Table 4.8	Rotated Component Matrix	122
Table 4.9	Model Fit	127
Table 4.10	Composite Reliability	130
Table 4.11	Convergent Validity	131
Table 4.12	Discriminant Validity	133
Table 4.13	Multicollinearity Analysis	135
Table 4.14	Standardized β & P Value for the Main Hypothesis	139
Table 4.15	Standardized β & P Value-Sub-Hypothesis (A)	150
Table 4.16	Standardized β & P Values-Sub-Hypothesis (B)	155
Table 4.17	Standardized β & P Values-Sub-Hypothesis (C)	157
Table 4.18	Mediation Analysis	160

LIST OF FIGURES

Figure 2.1	Theoretical Framework	65
Figure 2.2	Schematic Diagram of Theoretical Framework	66
Figure 3.1	Types of Research	73
Figure 3.2	Type of Research Design	75
Figure 3.3	Burrell and Morgan Model	79
Figure 3.4	Map of Punjab Province, Pakistan	82
Figure 3.5	Province Wise Distribution of SME's in Pakistan	82
Figure 3.6	Stages in Research Process	89
Figure 3.7	Research Onion	93
Figure 4.1	CFA Model	126
Figure 4.2	SEM 1st Order Model	138
Figure 4.3	SEM 2nd Order Model (A)	147
Figure 4.4	SEM 2nd Order Model (B)	148
Figure 4.5	SEM 2nd Order Model (C)	149

LIST OF ABBREVIATIONS

AVE	Average variance extracted
<i>B</i>	Beta coefficient
CFA	Confirmatory factor analysis
CMIN	chi-square value
CR	Composite reliability
Df	Degree of freedom
EFA	Exploratory factor analysis
EL	Empowering leadership
FI	Firm Innovativeness
IWB	Innovative work behavior
MR	Market Responsiveness
N	Number of respondents
PWB	Proactive work behavior
SEM	Structural equation modeling
SME	Small & Medium Enterprises
SMEDA	Small & Medium Enterprises Development Authority
SRMR	Standardized root mean square residual
TL	Transformational leadership
VIF	Variance inflation factor
α	Cronbach's alpha coefficient

CHAPTER 1

INTRODUCTION

1.0 Chapter's Context

The first chapter of the thesis is the introduction. This chapter includes an overview of the thesis, in which the topic is introduced. Starting from the background of the study, this covers the definitions of the study's variables, current and conflicting findings, and unresolved issues related to the area of research. The next section is related to some basic details related to the SME sector in Pakistan. It is followed by the next section, which is a problem statement, here the unresolved issues related to innovation, leadership, and employee behaviors in Pakistan have been discussed, and the problem that needs to be addressed is specified. Moreover, the gaps in previous knowledge have been addressed, and how this study will cover them is stated.

The next section is the purpose of the study, which covers the need to conduct the study and what the researcher would like to achieve through this study. Next are the research questions that the study will answer. The chapter then covers the next section which is the significance of the study, here the importance of the study is described, and how this study will be helpful for the leaders of Pakistan, especially in the SME sector of Pakistan, who desire innovation and compete for it. Moreover, my personal motivation for choosing this topic, and my previous contributions related to the given topic are explained. Lastly, in this chapter, operational definitions of the variables are explained.

1.1 Background of the Study

In this current era, organizations are facing immense market competition. Innovativeness and responsiveness are considered essential elements for competition

and survival. Therefore, extreme focus nowadays is placed on creativity, proactivity, and innovation. Moreover, because of the unpredictable technology changes and transforming and turbulent environment, organizational leaders are coming to realize that they need employees who are innovative and proactive enough to deal with every certain or uncertain situation (Shalley & Gilson, 2004; Boonyarit, 2023; Chen & Li, 2015; Zeya-he et al., 2023, Strauss, Griffin & Rafferty, 2009).

Investigating the antecedents of both innovativeness and innovative behavior has been a significant field of research in recent periods. Leadership is a key antecedent of proactive and innovative behaviors (Afsar & Umrani, 2020; Song, Zhou & Boyi, 2023; Jong & Hartog, 2007; Strauss, Griffin & Rafferty, 2009) and innovativeness (Arici, & Uysal, 2022; Denti & Hemlin, 2012; Khalil, 2016).

Among the different leadership styles, the study examined the two leadership styles: transformational leadership and empowering leadership. Over the previous 3 decades, Transformational Leadership has turned out to be a popular area in leadership research (Baker et al., 2022; Yavuz, 2020; DeChurch, Hiller, Murase, & Doty, 2011; Dusk, Resick & Mawritz, 2013). Transformational leadership is the “style of leadership in which the leaders transform their followers from one level to another, where they can perform more than what they initially intend to perform” (Givens, 2008; Bass 1985; Krishan, 2005).

Empowering leadership, on the other hand, involves sharing power with the followers to give them autonomy, more responsibility and make them feel psychologically empowered (Spreitzer, 1995; Ahearne et al., 2005). As compared to transformational leadership, which is a supportive style of leadership, the empowering leadership is more of a delegative style of leadership.

Theoretical arguments support the influence of both leadership styles on innovativeness and responsiveness, as both of them support innovative activities and create a supportive culture required for innovativeness (Gumusluoglu & Ilsev, 2009; Kim & Park, 2000; Jaiswal & Dhar, 2015). However, empirically, the relationship has given both positive (Li, Mitchel & Boyle, 2016; Matzler et al., 2012; Gumusluoglu & Ilsev, 2009; Naqshbandi & Tabche, 2018; Afsar & Umrani, 2020; Lei, Leangkhamma & Le, 2020; Menguc et al., 2007) and negative results (Jaussi & Dionne, 2003; Osborn & Marion, 2009; Wilson-Evered et al., 2001).

The present study uses the behavioral mediation mechanism by taking the two active work behaviors of employees: “proactive work behavior behaviors” and “innovative work behaviors”. Proactive work behaviors refer to the “self-initiated and also the change-oriented behaviors in the workplace” (Schmitt, Hartog & Belschak, 2016; Wu & Parker, 2017). On the other hand, innovative work behaviors refer to a “behavior process that is multi stage involving the generation, promotion, and implementation of novel ideas” (Jannsen, 2000).

The study assumes that the individual behaviors of employees play a crucial role in taking firms towards innovativeness and responsiveness because it is the people who actually execute the actions required by the leaders to take firms towards the innovation. Moreover, the present study is conducted in the SME sector of Pakistan. It is because the SME sector of Pakistan relies heavily on the dominant roles of top leaders, and it also faces a race of competition, innovation, and responsiveness. The SME sector of Pakistan constitutes about 90% of the total enterprises in Pakistan. In annual GDP, their share is 40%, and 80% of the non-agricultural labor force has been employed in SME (SMEDA Pakistan, 2022)

1.1.1 Background of the SME Sector of Pakistan

The focus of this research lies within SME (small and medium enterprises sector) of Pakistan. This sector is characterized by a significant reliance on the leadership of top management and filled with intense competition, the hunger for innovation, and the need for responsiveness. As far as the definition of SME is concerned, organizations define it in terms of the number of employees, assets, and production levels. According to the State Bank of Pakistan, those organizations are considered being under the umbrella of SMEs (small and medium enterprises) whose number of employees are less than 250 and have the annual sales up to 800 million Pakistani Rupees (PKR). The State Bank of Pakistan also differentiated the organizations in terms of small vs. medium organizations. In the small organizations' category, the size of employees is less than 50, and annual sales are up to 150 million Pakistani Rupees (PKR). Whereas in the category of medium enterprises, employees number is less than 250, and annual sales reach up to 800 million Pakistani Rupees (PKR). Table 1.1 below shows the criteria of SMEs.

Table 1.1: Criteria of SME

	Number of Employees	Annual Sales
Small Enterprises	Less than 50	Up to PKR 150 million
Medium Enterprises	51 - 250	Above PKR 150 million and up to PKR 800 million

Adopted from Revised Prudential Regulations for SME Financing

Pakistan is a developing country; however, SMEs are contributing a lot to the development of the country through employment generation, GDP, and export earnings. The SME sector of Pakistan constitutes around 90% of the total enterprises in Pakistan. In annual GDP, their share is 40%, and 80% of the non-agricultural labor

force has been employed in SME, while the share of SMEs in Global GDP is 55% (SMEDA Pakistan, 2022). SMEs are not restricted to any one field. Instead, they are in different sectors, such as retailing, manufacturing, agribusinesses, livestock, education, transport, construction, and health etc. (National SME policy, 2021). In the SME sector of Pakistan, there are approximately 5.2 million industrial units that contribute 40% to GDP and 25% to exports, including wholesale, retail, IT, textile, and service sectors (National SME Policy, 2021). Most of the SMEs (small and medium enterprises) in Pakistan are run by sole proprietorships and family or friends' businesses (Saif, 2015)

For promoting the SME sector in Pakistan, a development authority named SMEDA (Small and Medium Enterprise Development Authority) was established in October 1998. However, the first policy regarding SMEs was announced in 2007 by SMEDA Pakistan. The purpose of SMEDA is to provide the ideal environment, facilitation, financial support, guidance, advice, and business development services to SMEs (small and medium enterprises). In recent times, SMEDA has started appreciable projects for promoting SMEs (small and medium enterprises) which include the "Kamyab Jawan - Youth Entrepreneurship Scheme, The Economic Revitalization of Khyber Pakhtunkhwa Project (ERKP), and The Public Sector Development Programme (PSDP) (SMEDA, 2023).

SMEs (small and medium enterprises) are also facing numerous restraints and challenges. A lot of conflicting strategies have also slowed down the progress of this sector. Lack of financial support from the government, lack of loan acquisition, lack of innovation support, power shortages, and technology acquisition are some of the major challenges faced by the SME (small and medium enterprises) sector of Pakistan

(The Nation, 2020). The recent pandemic “COVID-19” also hit the SME sector in Pakistan badly, along with the other sectors. During this pandemic period, 28% of the SMEs in Pakistan got closed, and many of the employees lost their employment, although some of them got reopened after the improvement in the situation (Global State of small Business Report, 2021).

1.2 Problem Statement

Even though the corporate leaders now see creativity and rapid responsiveness as vital for the firm’s success, but the approaches and behaviors they are following are not the ideal ones. The power distance and authoritarian approaches, where they train their followers to passively follow and respect the orders, cannot lead them to innovation (Molino et al., 2013; Pizzolitto, Verna, & Venditti, 2023; Grant et al, 2009).

Pakistan is a developing country, and is facing numerous problems in the smooth running of its growth and development (Sohil, Sohail, & Shabbir, 2021; Nazir, Khan, & Khan, 2023; Saif, 2015). The SME (small and medium enterprise) sector of Pakistan, which is considered the backbone of the economy, is facing enormous and frequent challenges despite its remarkable and valuable contributions. Many of them are related to innovation, technology, workforce, human resource management, lack of leadership support, risk aversion, corruption, and lack of external support (Iqbal & Ahmed, 2021; Anser et al, 2022; Amir, Ali & Ahmed, 2020; Soomro, Shah & Mangi, 2018; Arshad et al., 2020 Khaliq et al., 2015). Innovation is particularly crucial for the competitive business organizations, where organizations compete to innovate in order to survive in the markets, and achieve the first mover and sustained competitive advantages (Puranam, Singh, & Zollo, 2006). For developing countries, the concept of innovation becomes even more significant, necessary, and valuable because of rapidly changing business environments, institutional instabilities, high uncertainty, and

imbalances (Farashahi & Hafsi, 2009; Smallbone, Saridakis & Abubakar, 2022). So here the role of ideal leadership, which can promote innovativeness among their organizations, becomes even more crucial (Tipu, Ryan & Fantazy, 2012).

Pakistan is among those countries that lag behind in responsiveness, innovativeness, and competitiveness. According to the Global Innovation Index (2022), Pakistan ranks 87th out of 132 countries, whereas, as per the Global Competitive Index (2019), it ranks 110 out of 141 countries, which specifies that it is a clear backbencher. One of the primary reasons why Pakistan lags behind is the non-supportive cultural attitudes (Pakistan Today, 2017) and the ineffective leadership styles (Saif, 2015). According to Saif (2015), an important drawback of SMEs in Pakistan is that leaders are unaware of the appropriate leadership styles to make their followers behave out of the box. Here, organizational leaders discourage trying novel ideas and their followers try to adopt the path their predecessors followed. According to Khan et al. (2020), leadership styles practiced in Pakistani organizations are still very traditional, in which behaving innovatively is discouraged and considered a high risk and cost-consuming.

In Pakistan, especially in the SME sector, leaders try to manage employees very informally. They try to externally satisfy the employees through salaries, rewards, and bonuses (Khan, Ghauri & Awang, 2013) but put very little emphasis on the internal motivation. As Zahra, Sarwar, and Baig (2015) concluded in their study, the overall transactional leadership style is dominant in Pakistani middle-level managers as compared to the transformational leadership style. This transactional style of leadership makes the employees narrow-minded, short-term oriented, and risk avoiders, which is harmful to their creativity of employees. According to Nawaz, Hussain & Sohail (2020), mostly transactional style of leadership in Pakistan is

prevailing in the corporate sector of Pakistan, where leaders are power hungry to enforce the rules and regulations. Such a transactional style of leadership might boost satisfaction, commitment, loyalty, or well-being, but it cannot enhance creativity and innovativeness.

Furthermore, the cultural context of Pakistan consists of high-power distance, authoritarianism, and strong uncertainty avoidance (Islam et al., 2022; Tipu, Ryan & Fantazy, 2012). This high-power distance culture, which is dominant in the majority of Pakistani firms (Bashir, Abrar & Ghazanfar, 2012) is too harmful for employees in the long run, because it actually suppresses intellectual skills of the employees. They feel hesitant to behave innovatively in such a culture because they recognize the reality that they will be extremely blamed by the leaders if their actions lead to failures (Abbas & Ali, 2021). Through these passive behaviors among their employees, it is less likely that the organization can achieve innovation.

Moreover, it is considered that the behaviors of the followers deeply depend upon the influence of the leader who leads by an example where followers try to copy him or her (Hartog & Belschak, 2012). So, when the employees see their leaders focusing only on the short-term objectives, they also try to replicate it. They become less self-determined, do not use their own intellectualness, and do not try to use an innovative thinking approach. (Young et al., 2021).

In SME Pakistan, numerous factors influence innovative work behaviors, and addressing these challenges is critical for nurturing a culture of innovation. Some of the potential issues that are reducing innovative work behaviors include risk aversion, limited resources, lack of awareness, lack of training, communication barriers, and more importantly, leadership support (Anser et al., 2022; Pasha et al., 2022; Shah,

Shah & Gohari, 2022). Some other issues that are hindering the innovative performances of SMEs in Pakistan are insufficient external knowledge, lack of business strategy adoptions, lack of favorable environment, corruption, absence of networking political influence, and lack of internal skills (Arshad et al., 2020; Haleem, Jehangir & Ullah, 2019; Iqbal & Ahmed, 2021; Amir, Ali & Ahmed, 2020)

Furthermore, another concept prevailing in the SME sector of Pakistan is that they rely extensively only upon the marketing and promotional aspects of the business (Nazim, Batool & Arooj, 2019), assuming it will lead their firms to receive the quick market responsiveness and innovativeness. They are putting less emphasis on the employee behaviors aspect and supportive leadership aspect of the business.

So, for innovativeness to happen, organizational leaders need to promote and support it, because it is the behaviors of the employees that actually lead the firms toward the practical occurrence of the innovation (Shalley & Gilson, 2004; Grošelj et al., 2021). It's less likely to achieve innovation and quick market response when the behaviors of employees are passive and order following. According to Khan et al. (2020) in order to make employees innovative, and out of box thinkers, Pakistani leaders need to adopt certain change-oriented leadership practices such as helping and supporting employees, giving useful suggestions for development, and encouraging employees to use their own intellectualness to solve their problems. But unfortunately, these practices of Pakistani leaders are extremely rarely followed, which is causing real issues of low innovation in the country's development, especially in the SME (small and medium enterprises) sector (Khan & Ahmed, 2020).

Although the relationship between leadership and innovation has been extensively explored by different researchers (e.g. Borins, 2002; Novitasari et al.,

2020; Arici & Uysal, 2022; Stoker et al., 2001; Lakshman, 2016) however, particularly empowering leadership and transformational leadership's relationship with innovation has not received the scholar's attention it deserved. Although some studies have explored this particular relationship, it is noteworthy that the extent of scholarly attention dedicated to it, may not fully capture its significance. Moreover, market responsiveness and firm innovativeness have been previously explored with strategic perspectives, i.e. culture, HRM, customer satisfaction, and strategic learning (e.g. Garrett, Covin, & Slevin, 2009; Wakrija & Kant, 2022; Chang et al, 2013; Wei, Samiee, & Lee, 2014). However, their relationship with behavioral antecedents, i.e. innovative and proactive work behaviors, leadership behaviors, remains an area of negligence.

Previously, the studies conducted on the relationship between leadership (TL, EL) and innovation indicates that the focus of the researchers was on the supportive climate, culture, learning, empowerment, and task interdependencies. The individual employee behavioral aspect seems to be missing in previous relevant studies. For example, Gumusluoglu & Ilsev (2009) examined the relationship between transformational leadership and innovation through the moderation of support for innovation. They have not explored any mediation mechanism for the relationship and have left it for future researchers. Similarly, Khalil (2016) in his study linked transformational leadership to employee innovation through the moderating effect of perceived supportive climate. His study also does not provide the mediation mechanism of the examined relationship. Moreover, the research conducted by Saeed et al. (2019) used psychological empowerment as the moderator between transformational leadership and innovation, whereas the study by Alameri et al. (2021) used job complexity as the moderating variable to explore the relationship between