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Impact of Strategic Planning in the Small Businesses in Kenya

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Abstract:

The Kenyan Small Enterprises sector is a very competitive sector, and they need strategic planning to stay put competitive. Kenyan Small businesses which include agriculture and rural businesses, have contributed greatly to the growth of the economy, mostly in the provision of employment. Hitherto there have been high failure rates and poor show levels. Many are confronted with the threat of failure within the first few years. Many SMEs perform well after start up, but only a few experience sustained growth through the full lifecycle and become large firms. It has been established that lack of strategic planning may thwart them from achieving their potential. There is very little evidence however indicating whether SMEs in Kenya engage in strategic planning, and if they do how it impacts on their general performance. This study attempts, through a literature review, to find out how strategic planning impacts their performance. The study established that the most successful businesses use strategic planning, and there is a high failure rate for those who do not. The recommendation is that the owner or entrepreneurs of the SME to be trained in the skills of strategic planning.

Keywords: SMEs, strategic planning, Performance

1. Introduction

Small and medium enterprises (SMEs) play a considerable economic role in Kenya, and economic planners in Kenya have recognized their importance in economic development and Vision 2030. Micro and small scale businesses are catalysts in socio-economic development, therefore the government has focused on the encouragement of SMEs as a way of encouraging broader participation in the private sector. SMEs are a medium for the accomplishment of national micro-economic objective in terms of employment generation at low investment cost, and augmentation of apprenticeship training.

According to Peacock (2004), at a macro level, SMEs have created the majority of new jobs in the Organization of Economic and Cultural Development (OECD) countries since the 1970s. Their collective contributions to respective gross domestic products (GDPs) are 30% in Australia and New Zealand, 51% in the UK and USA, 57% in Canada and Japan and 76% in Luxembourg. SMEs are a major source of entrepreneurial skills, innovation and employment. Prospering countries have SME driven economies because this sector is the cornerstone of strong economic growth. Employment opportunities, reduction in poverty levels and subsequent improved standards of living are some of the major contributions of the SME sector.

In Kenya SMEs employ 74% of the labour force and contribute over 18% of the country's gross domestic product (GDP). More than 90% of businesses come from this sector, and this makes up 30% of total employment. In addition, the recent Kenya Economic Survey notes that out of 503,000 jobs created in 2011, 440,400, or 80%, were in the SME sector. This belies their individual small size. It is acknowledged that micro and small scale entrepreneurs, including agriculture and rural businesses, have contributed greatly to economic growth (Kombo, Murumba & Makworo, 2011). The sector contributes to the national objective of creating employment opportunities, training entrepreneurs, generating income, and providing a source of livelihood for the majority of low income households in Kenya.

Notwithstanding their many contributions SMEs have witnessed high failure rates and poor performance levels (Jocumensen, 2004). Many are faced with the threat of failure within the first few months of their starting. It has also been recognised that while most SMEs grow strongly after start up, only a minority experience sustained and consistent growth through the full lifecycle and become large firms (Mazzarol, Reboud & Souter, 2009).

2. Performance Measurement

Business performance measurement and control systems are the formal, information-based routines and procedures that managers use to maintain or alter patterns in organizational activities. A typical performance measurement helps businesses in periodically setting SMEs goals, and then provides feedback to managers on progress towards those goals. The time horizon for these goals can typically be about a year or less for short-term goals, or span several years for long-term goals. Performance needs to be measured relative to some benchmark, be it a competitor's performance or a preset target. A specific measure can be compared to itself over time, or to a preset target, or evaluated along with other measures.

It is postulated that all factors held constant, a key determinant of business success lies in strategic planning (Robinson & Pearce, 1984). By neglecting strategic planning SMEs may not achieve their full potential and their survival could be at risk. Despite the commonly agreed benefits of strategic planning, there is little empirical research investigating the drivers that cause SMEs to engage in strategic planning for improved performance.

Strategic planning is concerned with the future consequences of current decisions, how desired outcomes are to be accomplished, and how success is to be evaluated. It also links short, intermediate and long term plans. Kinyua, (2010) asserted that SMEs have a fair strategy formulation practice, and have a game plan that seeks competitive advantage.

According to Mintzberg (1994), in the 1960s, corporate leaders embraced strategic planning as the best way to devise and implement strategies that would enhance the competitiveness of each business unit. Mintzberg asserts that the most successive strategies are visions not plans. In the last few years, extensive attention has been paid to the issues relating to strategic planning. With a few notable exceptions, many scholars have recommended that SMEs need to use strategic planning as an essential tool for improved performance, to maintain the existing size and capability of the firm, to take better advantage of the opportunities which lie in the future, and to pre-empt any threats to the business (Balasundaram, 2009).

(Gibson & Casser, 2005) assert that strategic planning is concerned with the setting of long term organizational goals, development and implementation of plans to achieve these goals and allocation or diversion of resources necessary for realizing these goals with respect to performance, strategic planning is generally more common in better performing SMEs. The study concluded that SMEs that engage in strategic planning are more likely to be those that achieve higher margins on profit and higher employee growth.

There is evidence that strategic planning is rare or non-existent in most SMEs in Kenya, they tend to orientate towards short-term operational rather than long-term strategic issues, and decision-making tends to be reactive rather than proactive (Wang et al, 2009).

SMEs in Kenya have been the means through which accelerated economic growth and rapid industrialization have been achieved (Harris et al, 2006). They have formed the base of industrial structures, and facilitated the process of industrialization in most countries irrespective of their stages of development (Balasundaram 2009).

SMEs are mostly managed by owners and relatives and financing is mostly provided by the owners. Often, the owners fail to realise the importance of external sources of capital in order to affect the expansion in the business. SMEs are usually distributed across four sectors, including agro-based industry, other industry, services, trade and in the finance and economic activities (Gathanya, Bwisa & Kihoro (2011).

A study by Kiprem, Peng & Pollard (2007) found out that SMEs in the USA represent an overwhelming majority of all businesses and account for almost one half of the Gross National Product (GDP). They create two-thirds of all new jobs and invent more than half of all technological innovations in the United States (US Small Business Administration, 2005). Similarly in Thailand; the largest number of businesses is comprised of SMEs. The catalytic roles of micro and cottage businesses have been displayed in many countries of the world such as Malaysia, Japan, South Korea, Zambia and India among others (Odeh, 2005). They contribute significantly to the GDP, export earnings and employment opportunities of these countries. Thus SMEs have been widely acknowledged as springboards for sustainable economic development (Osotimehin et al, 2012).

Emphasizing the importance of SMEs, Ayyagari, Beck & Demircug-kunt (2003), argue that it is primarily through the growth of SMEs that employees made redundant by large firms have been absorbed back into the workforce. Through a multiplier effect this employment provides incomes to regions which stimulate local economic activity, which in turn drives wealth and further creation of employment (Walker & Webster, 2004). Further to that, SMEs often in terms of entrepreneurial activity occupy fragmented or niche markets which large firms either cannot economically enter or are reluctant to do so, because of “unattractive” risk-return considerations (Peacock, 2004). Dolence (2004) established that there is a positive relationship between planning and performance in Asian SMEs. Performance in this regard related to profitability, market share, number of employees and reinvestment in the firm.

3. Overview of Strategic Planning

Planning is not a new phenomenon. It has its roots in military history (Sullivan & Richardson, 2011). The Greek word “stratego” applied to military plans for the destruction of enemies (Ruch, 2004). Strategic planning for business can be traced back to the 1920s when Harvard Business School developed the Harvard policy model, one of the first strategic planning methodologies for commercial businesses (Mahmood, Taleghani & Sharifi, 2011).

One of the common sets of activities in management is planning. In order to determine where the organization is going, regardless of whether it is in the private or public sector, it needs to be clear exactly where it stands, where it wants to go, and how it will get there (Kriemadis & Theakou, 2007).

Over the years companies have approached planning in many different ways. Strategy at all levels is the calculation of objectives, concepts and resources within acceptable bounds of risk to create more favourable outcomes than might otherwise exist by chance or at the hands of others (Yarger, 2006). It is further explained that strategy is the art and science of developing and employing instruments of national power in a synchronized and integrated fashion to achieve the laid down objectives. Grant (1998) postulates that strategy is a fundamental framework through which an organization can simultaneously assert its vital continuity and facilitate its adaptation to the changing environment. It is one of the top management tools for coping with both external and internal changes. It is the match between organizations resources, skills, environmental opportunities and risks, and the purposes it wishes to accomplish. A good strategy is one that has simple, consistent and long-term objectives. This involves the single mindedness of goals, unity of purpose and long term focus.

Pearce and Robinson (1988) point out that strategy helps in providing long-term direction for an organization. This provides a perspective for the various diverse activities overtime, which enables organizations perform current activities at the same time viewing them in terms of their long term implications for the probable success of the organization. Similarly strategy helps companies to cope with change (Pearce and Robinson, 1988). Due to the constant changes in an organizations operating environment, companies needs strategy in order to respond to these changes at all time. Strategy can help to guide the pattern of responses of companies to changes taking place in their environment.

Strategy enables companies to focus their resources and effort (Pearce and Robinson, 1988). The development of strategy helps managers identify critical tasks that need to be performed and hence helping in defining an organizational strategic thrust. Strategy also helps an organization develop a competitive advantage in the market. This in turn enables the organization to outperform and outwit the competition successfully

Organizations widely use strategic planning as an integral part of strategy, a means to an end. It is a way to position an organization through prioritising its use of resources according to identified goals in an effort to guide its direction and development over a period of time (Kriemadis & Theakou, 2007). The strategic planning process covers the entire spectrum of issues to the precise steps necessary for a smooth transition from current conditions to the challenges that lie ahead. Kriemadis & Theakou (2007) however caution that strategic planning rarely flows smoothly from one step to the next. Fresh ideas at one meeting may change decisions made earlier. This should not be a source of frustration; rather it reflects the necessary creative input of inventive team members. This echoes the views presented earlier by Stopford (2001) that strategic planning is not a static product which once set stays as it is; strategic planning is rather a constantly evolving process trying to follow the continual changes in the environment, implying that change and strategy are inseparable (Delmar & Wiklund 2008).

4. Strategic Planning and SME Performance

Planning can help maintain the firm at its existing size, or provide the framework for enhancing growth. Balasundaram (2009) asserts that strategic planning is essential to take advantage of future opportunities and to forestall any threats. Strategic planning here is described as a process of environmental awareness, the existence of the idea or formal documentation of a future strategic course of action, and awareness of both short and long term implications of these. Environmental awareness is a concept from business management by which businesses gather information from the environment to better achieve sustainable competitive advantage. The company also needs to respond to information gathered from environmental scanning by altering its strategies and plans as the need arises.

Tapinos et al (2005) also note that strategic planning consists of planning processes to develop strategies that might contribute to performance. One way it can do this is by generating relevant information to bring better understanding of the environmental factors, and reducing uncertainty. Strategic awareness therefore implies the ability to assess the total implications of any change. Tapinos et al emphasize that that means not only awareness of immediate implications, but also reflection on longer term repercussions.

Wang et al (2009) see strategic planning as being about competitive advantage. They emphasize that it enables a business to gain sustainable planning as efficiently as possible. Gibson & Cassar (2005) posit that it is those SMEs that engage in strategic planning that are more likely to achieve higher margins on profit and higher employee growth. Mazzarol (2004) contends that SME performance success is certainly driven by strategic planning. Kiptrem et al (2007) have shown that planning is as important for SMEs as for large organizations). Although formulating a consistent strategy is a difficult task for any management team, making that strategy work that is implementing it throughout the organization is even more difficult (Hrebiniak, 2006). Strategy implementation is a dynamic, intellectual and complex process which is comprised of a series of decisions and activities by managers and employees – affected by a number of interrelated internal and external factors – to turn strategic plans into reality in order to achieve strategic objectives (Schaap, 2006). Effective strategy execution rarely gets as much attention as formulation yet experienced managers appreciate that well crafted visions and strategic plans are useless if they cannot be effectively executed.

Despite all the evidence of the benefits of strategic planning, it is well recognized that it is rare or non-existent in the majority of SMEs (Peacock, 2004). Wang et al (2009) found that owner aspirations are integral to whether or not SMEs strategically plan. The concern is this may prevent achievement of their full performance and growth potential, and this is a big challenge to their survival. The authors concluded the findings were contradictory to the widespread opinion that due to lack of time, planning is less relevant for enterprise founders than other value increasing enterprise activities.

Rezaian (2008) concludes that organizations need strategy in order to adapt itself to the external environment and customer needs. Hanafizadeh et al (2006) add that nowadays organizations are so complex that without detailed planning they cannot survive.

Successful organizations will anticipate and address environmental turbulence through strategic planning (Rezaian, 2008). Strategic plans are those which are designed to achieve the competitive goals of the organization, so as to ensure the execution of the organizational mission (Rezaian, 2008). According to Hendrik (2010) strategic planning goes beyond planning like long term financial planning or capital planning, and involves a thorough assessment of the environment and the organization. This kind of planning, he points out is done with foresight and in an organized process. Tumusiime (2009), found a strong relationship between strategic planning and organization performance, strategic planning contributing 69.2% towards performance in SMEs. This implies that other factors combined, contributed only 30.6%.

A great deal of the research into the process of strategic planning in small firms has looked at the intensity of involvedness or “formality” used to identify the strategic planning process (Veliyath & Shortell, 1993). Formal business planning has been defined as the development, implementation, and continued update of a documented business plan tailored for a specific business (Stewart, 2002).

A study by Osotimehin et al (2012) reiterates that micro and medium scale enterprises have been accepted worldwide as instruments of economic growth and development. The study however concludes that despite governments' institutional and policies support to enhancing the capability of small and medium scale enterprises the majority did not grow into the large firms as projected at the onset. One of the reasons given was poor strategic planning by SMEs, which were found to be informal, unstructured and irregular, supported by insufficient and ineffective information which was usually obtained through informal sources (Balasundaram, 2009).

Several studies have emphasized that SMEs use and need formal sophisticated financial and strategic planning (Gibson et al, 2002). Well developed, soundly implemented and properly controlled planning processes contribute to a firm's success (Tapinos et al, 2005). Ciavarella et al (2004) found that one of the factors that motivated planning in enterprises was the personality of the owner. This also was important in survival of the firm, along with strategic choices. This is consistent with a study by Kiptrem et al (2007), which indicated that the level of strategic planning is positively associated with growth. Although SMEs typically employ a major share of an economy's total employees, SME management suffers from an insufficient business related knowledge base (Kraus, Reiche & Rescheke, 2008). Indeed formal plans or cost controls are often only provided on an irregular basis and planning instruments are usually only used by a small number of individuals and developed rather intuitively. These shortcomings lead to the conclusion that most SMEs fail due to the lack of proper strategic planning (Yarger, 2006; Kraus et al, 2008).

Zachary B. Awino (2013) demonstrated strategic planning as a learning tool and a strategic resource, which is consistent with the underlying assumptions of resource based theory, systems theory, chaos theory and balanced-score-card model assumptions. Strategic planning is an organization's process of defining its strategy, or direction, and making decisions on allocating its resources to pursue a strategy (Thompson and Strickland, 2004). In order to determine the direction of the organization, it is necessary to understand its current position and the possible avenues through which it can pursue a particular course of action. According to McNamara (2005), strategic planning determines where an organization is going over the next year or more, how it's going to get there and how it'll know if it got there or not. Strategic planning as a management tool has gained sustained prominence in the management of public services in the past two decades. It helps an organization focus its energy its objectives. It also ensures that members of the organization are working toward the same goals in order to assess and adjust the organization's direction in response to a changing environment (Thompson and Strickland, 2004). It is viewed as a disciplined effort to produce fundamental decisions and actions that shape and guide what an organization is, what it does, and why it does it, with a focus on the future strategic planning. It has been touted as one of the effective management tools in strengthening organization performance through effective decision making and systematic strategic planning formulation and implementation. According to Smith, (1994) Strategic planning is an effective management tool in transforming a bureaucratic public sector to a more responsive and innovative administration.

According to Robert and Duncan (2007), strategic planning gives overall direction to areas like financial strategy, marketing strategy, organizational development strategy and human resources strategy, to achieve success. Strategic planning better decisions making. Information communicated through vision and strategy allows people to make the best decisions in hiring and rewarding the right people, adopting and developing the right systems, and making the right investment decisions. In addition, strategic planning increases energy resulting from rallying behind a cause, and elimination of conflict and confusion of priorities. It also improves customer satisfaction; a true test of value and leads to higher retention and growth. As a result, good planning leads to competitive advantage in doing what you do better than others

According to Mahmood et al, (2011) in times of uncertainty, managers need a way to monitor and react to the environment. Strategic planning is ongoing and permanent, and is generally pursued as a rational undertaking to reduce uncertainty of performance through trade-off decisions from controversial choices. It determines end goals, and strategies for accessing, allocating and managing resources to achieve those goals (Karnani, 2006). In complex global environments, unpredictable change, time and uncertainty play an important role. Such changes have removed many organizations from the competition area (Hanafizadeh et al, 2006). In the strategic planning process, time and uncertainty have an important role too (Mahmood et al, 2011).

According to Hamidizadeh & Shahri (2007) organizations currently try to identify, strengthen and improve their capabilities for adapting and completing their knowledge skills to cope with the turbulent environment. In a complex and competitive environment with saturated and complex markets, lacking strategic planning places organizations in a poor competitive situation and eventually confronts them with failure.

The need for strategic planning is based on the issue that all organizations competing in a dynamic environment desire to spend their limited resources for their diverse and growing needs (Rezaian, 2008). Dynamism and turbulence caused by environmental changes adds the indisputable necessity of strategic planning. Presenting the necessary training and education to managers about strategic planning is vital to enable them to strengthen strategic insight and thinking in the organization (Mahmood et al, 2011). Armstrong (1982) examined the extent of formal planning by five main variables (i.e. setting objectives, generating strategies, evaluating strategies, monitoring the process, and commitment to the process) and concluded that it positively affects success. According to (Dumbu & Chadamoyo 2012) the basic management functions of planning, organizing, leading and controlling are not practised in most SMEs in the craft industry. The study recommends that management should be offered managerial training.

Penrose (1959) also pointed out that free time and becoming the owner of a successful business is not important for survival-oriented entrepreneurs. Instead they want to continue as they are. Growth can also be viewed to be necessary for survival. Growth theory also posits that successful growth leads to a critical stage, namely professionalization, which requires the owner/managers to change their entrepreneurial approach to a more professional one. Growth orientation therefore is explained as the degree to which entrepreneurs intend to engage in strategic planning using specific strategies to grow and expand their businesses.

5. Conclusion

An issue that has to be dealt with in a SME is planning, in order for the SME to determine where it is going, where it stands and how to reach where it aspires to go. An SME must have a strategic plan since this is an intelligent preparation for action. The strategic plan enables a SME to improve its vision, mission and values. It is able to know its environment, and hence realize its strengths, opportunities and threats through the SWOT analysis that only comes due to engaging in strategic planning. Analysis of strengths and weaknesses constitutes the internal analysis and threats and opportunities the external analysis. This motivates the SME to organize for future activities and to recognize and address challenges in its environment, as give it a competitive advantage over its competitors.

The resultant indicators for this include budget setting, training, improving capabilities and setting of guiding vision and mission statements. Mission statements are a way of defining the overriding purpose of an organization or its overriding aims. When mission statements are used sensibly, they can act as a mental model to refer to for thinking and action. Training is paramount in strategic planning; it is meant to equip the employees with knowledge and skills which positively impacts on the performance of the SMEs. Budget setting in SMEs is a vital tool that helps the firm to achieve rational distribution of resources, ensure better planning of operations as well as controlling the costs.

Strategic planning is characterised by improved performance, implementation of objectives and high profit turnover. Many argue that the sole purpose of a business is to make a profit; failure to make profit would clearly mean death of the enterprise. As such, better performing SMEs are highly profitable, competitive and are assured of survival in the business arena. It is postulated that strategic planning has a significant influence in growth in SMEs in Kenya. Strategic planning is a key driver of performance in SMEs in Kenya, and cannot be ignored. SMEs should be aware of the critical role strategic planning plays and the potential positive influence they have on performance.

The government acknowledges that the SME sector is the engine for growth and, driver of innovations and growth. Policy makers and academicians should, therefore, take an interest and pay attention to strategic planning aspects that enhance the performance, growth and sustainability of SMEs. The efforts of the Kenyan government by providing SMEs with monetary resources like grants and loans with zero interest rate may not be the universal remedy for sorting the problems of unemployed youth.

This study recommends that the government and institutions that support the growth of the SME sector consider investing in effective strategic planning processes and actions in businesses owned by SMEs, for example the launching of Chandaria Business Innovations and Incubation Centre (Chandaria-BIIC) at Kenyatta University. This supports new and innovative ideas from Kenyans. It in addition sponsors a culture of innovation among Kenyan youth through a range of programmes, through a platform for the provision of solutions to challenges facing various economic sectors. In line with Kenya's Vision 2030 and Kenyatta University's current Strategic and Vision Plan, Chandaria-BIIC centre of attention lies on supporting up to 100 innovations per year. It endeavours to intermingle academic research with innovation and establishment of SMEs, as well as to predispose Kenyatta University students' population and Kenyans in general towards being job creators rather than job seekers.

This means it is important for policy makers and relevant institutions to strengthen the strategic planning skills and capacity of SMEs. The Government of Kenya, through youth enterprises and other micro finance institutions to nurture entrepreneurs with strategic planning skills. It should also continue with its educational policies and increase the educational levels of Kenyans since businesses owned by SMEs are likely to be more productive when they engage more educated and skilled employees. The study also recommends that all SMEs should adopt strategic management practices to stay competitive and come up with proper corrective mechanism to ensure that deviations from original plans are reined-in, and that strategies or plans are responsive to changes in the business environment.

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