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Strategic Planning and SMEs Performance: A Developing Country's Perspective

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Ever-increasing competition, changing environmental dynamics, fear of takeover, acquisition of cutting-edge technology, insufficient good management, and limited resources force firms to apply strategic planning to manage such situations and improve firm performance. Based on this, the paper examines how strategic planning influences the firm performance as well as the degree of importance attached to strategic planning by high performers as well as low performers. Data is collected through survey questionnaire from 245 respondents from small and medium enterprises (SMEs) manufacturing. Path analysis shows that strategic planning has a positive and significant impact on firm performance. More specifically, the non-financial aspect of performance showed more influence than financial performance. Digging the matter further, the multi-group analysis revealed no difference across high performers and low performers with respect to the impact of strategic planning on firm performance. This finding has an important implication for managers of both higher and low performers. Managers of low performers firms need to contemplate their strategic planning process and find out as well as rectify any mistakes to avail the associated benefits of strategic planning. Similarly, managers of high performers firms should find out any room of improvement in the process of strategic management to reap the benefits of strategic planning in essence.

Keywords: Strategic Planning, Firm Performance, Multi-Group Analysis SMEs, Pakistan

1. INTRODUCTION

The importance of small business cannot be denied in today's world for reasons such as its contribution to Gross National Product (GNP) and innovations (Norris, 1979) collective impact on economy (Robinson & Pearce, 1984), and employment of large share of employees in an economy (Kraus, Reiche, & Reschke, 2007). SMEs account for more than 85% of all manufacturing companies (Khalique, Hasan, Jamal & Sharri, 2011). As far as Pakistani perspective is concerned, almost 90% of all the businesses in Pakistan is comprised of SMEs and functions as the backbone of the economy (Khan & Khalique, 2014). SMEs contribute 8.80% to total GDP of Pakistan with growth rate of 8.18% per year ("Pakistan Economic Survey," 2017).

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Despite the significant role played by SMEs as economic driver, there are reasons why it is not contributing much to the country economy in terms of GDP. In this regard, there are number of challenges faced by SMEs that hinder its performance. These challenges include insufficient business related knowledge of management, provision of formal plans and cost control on irregular basis, and employment of planning instrument by only few small firms(Kraus et al., 2007). Likewise, Karagozoglu and Lindell (1998) note other bottlenecks faced by SMEs which include scarce resources to carry out strategic planning, inadequate access to capital in terms of financial, human, and customers, as well as the non-application of strategic planning by most firms that do not reach a 'critical size'. Considering these shortcomings which SMEs face, an examination of the significance of strategic planning in SMEs is mandatory.

Kraus, Harms and Schwarz (2006) believe that strategic planning contributes to the bottom line of SMEs by analyzing the environment (internally and externally) that helps reduce uncertainty by generating relevant and accurate information that leads to better understanding and decision making. Despite all the benefits associated with strategic planning, it has not been embraced much yet by small firms (Wang, Walker & Redmond, 2007). According to Emeka (2015), strategic planning was incorporated by almost every fortune 500 company and several other small firms in 1960s. Thus, SMEs that conduct strategic planning outcompete those that do not (Wang et al., 2007). Similarly, the secret of a small business success lies in the fact to plan regularly, do high level of planning, and to have some planning documents in written (Watts, 1990).

SMEs seems to have paid inadequate attention to strategic planning(Khan & Khalique, 2014). Similarly, Glen and Weerawardena (1996) note that large and small firms differ in developing and implementing their strategic planning for reasons such as firms' size, degree of available external consultancy, and the level of manager/owners entrepreneurial initiatives. For these reasons, replicating of strategic planning employed by large firms on SME might not work.

However, neglecting strategic planning will cost an SME by failing to achieve its targeted performance and growth. This may even place the survival of SMEs at risk (Beaver, 2003). Similarly, research on 9000 failed/ bankrupt firms of all types found that management inexperience, incompetence, and poor planning contributed to business failure (Wyant, 1977). Similarly, Cassar and Mankelow (1997) proved that planning plays a vital part in stopping SMEs from failure. Moreover, Bowen, Morara and Mureithi (2009) identifeid that lack of planning, poor financing and management factors are responsible for small business failure. In addition, Tourangeau (1981) appreciates the value of strategic planning, but at the same time warns that strategic planning is not a panacea for all ails of the firm but definitely part of a solution.

Irrespective of the firm size, organizations need to adhere to strategic planning to enable firms to respond to their constantly changing business environment and craft strategies. Accordingly, as SMEs comprise of 90 % of all businesses in Pakistan and still its contribution to the economy is unsubstantial. Thus, the research is of paramount importance to find out the impact of strategic planning on SMEs firm performance operating in KP, Pakistan to highlight its importance.

The next section reviews literature on SMES, SP, and empirical evidence on SME-SP relationship. Following review of literature, research methods are discussed that mainly describe strategic planning and its association with organizational outcome, and target sample as well as data collection technique. Next chapter reports the analysis and discussion of the hypothesis testing followed by conclusion of the research.

2. LITERATURE REVIEW

The process of Strategic Planning entails explaining strategy and making choices about allocation of resources (Adeleke, Ogundele, & Oyenuga, 2008). On other hand, Berry(1997)perceives strategic planning as a means that make a firm reach its destination by taking on the best path. Similarly, Hofer and Schendel, (1978) state that strategic planning helps managing and adopting to the dynamic environment. In addition, it lays emphasis on integrating strategy with the firms' external structure, processes, and production rather than focusing on internal efficiency.

Strategic planning helps accomplish the vision of upper management, diminishes unpredicted future risks (Vel, Creed & Narayan, 2012), and takes a firm from 'dream world' to 'real world' (Herter, 1995). Similarly, it serves two purposes; that is, adaptive thinking or efforts directed towards bringing firm-environment alignment (Ansoff, 1991), integration and control of different elements of a firm (Miller & Cardinal, 1994). Adaptive thinking helps executives of small firms to keep away from mistakes and overcome weakness of the firm (Aram & Cowen, 1990). However, Kotter (1996) contemplates that key objective of strategic planning is to facilitate firm craft, prioritize and choose strategies to achieve the desired results. In similar vein, Peattie (1993) argues that the main objective of employing formal strategic planning is to enhance a firm's performance by crafting and putting into practice better strategies.

2.1. Strategic Planning and SMEs

Ever-increasing competition and the changing environmental dynamism as well as complexity call for the embracing strategic planning (Emeka, 2015; Vel et al., 2012). Similarly, the fear of takeover, the need to procure the cutting edge technology, insufficient good management, and limited capital as well as limited resources make it necessary to integrate strategic planning (Ukeje & Akanwa, 2000). Matthews & Scott (1995) postulate that the activities of strategic planning help reduce the uncertainty in a company. For these reasons, it is compulsory for firms to get armed with strategic planning so as to survive and prosper (Ansoff, 1991; Miller & Friesen, 1983; Mintzberg,1994). In other words, gone are the days that strategic planning was considered a luxury or an option, it has now become mandatory (Emeka, 2015; Khan & Khalique, 2014; O'Regan, Sims& Gallear, 2007; Temtime, 2003).

Appreciating the role of strategic planning, many firms have embraced it for its benefits. For instance, provision of direction (Viljoen, 1994), improved coordination and control of a firm's activities (Arasa & K'Obonyo, 2012), as well as providing direction and main purpose to the organization and its employees (McCarthy, Minichiello, & Curran, 1975). By the same token, efficient allocation of resources, competitive advantage (Ohmae, 1983), and innovations are other benefits associated with embracing strategic planning (Porter, 1980; ohmae, 1983; Kotter, 1996). In order to reap these benefits, Gehani (1995) argues that strategic planning must be operative. Effective strategic planning is determined by a company's agility in terms of satisfying customer orders quickly, launching new products from time to time, and contracting in and out of strategic alliance without delays.

Despite these benefits, there are some reasons that make SMEs reluctant to adopt strategic planning. These include saying no to external help, sticking to tradition-based thinking, fearing to embrace radical change and incurring high costs (Scharpe, 1992) cited in (Kraus et al., 2007). More to the point, Robinson & Pearce (1984)reported the underlying motives for the non-use of strategic planning as the paucity of time, necessary knowledge and exposure, specific skills and expertise, and finally the lack of trust and openness. Likewise, Kraus et al.(2007) report various objections on the application of Strategic Planning in SMEs. These objections are: Flexibility and management of SMEs are suffered; the employment of limited resources in operational, sales and would do better in favor of SMEs than in strategy development; and a lot of bureaucracy involved in strategic management. Besides the criticisms made against strategic planning in SMEs, these authors also admit the importance of strategic planning, corporate goals achievement and view it as a future investment especially when the external environment is uncertain and turbulent.

By and large empirical research on planning-performance relationship revealed contribution to firm performance (Akinyele & Fasogbon, 2010; Arasa & K'Obonyo, 2012; Dauda, Akingbade, & Akinlabi, 2010; David, 1997; Greenley, 1986; Haleem, Jehangir & Haq, 2018; Henderson Bruce, 1979; Hofer & Schendel, 1978; Khan & Khalique, 2014; Miller & Cardinal, 1994; Owolabi & Makinde, 2012; Oyedijo, 2012; Robinson & Pearce, 1984; Rudd, Greenley, Beatson, & Lings, 2008; Suklev & Debarliev, 2012; Veskaisri, Chan, & Pollard, 2007).

In a study on 245 Pakistani manufacturing SMEs, Haleem et al. (2018) found out that strategic planning witnessed positive connection with both the financial as well as non-financial performance. Similarly, Glaister, Dincer, Tatoglu, Demirbag and Zaim (2008) carried out a study in Turkey using 135 questionnaires and noted that firm performance was positively influenced by strategic planning. They also noted the mediating roles of variables such as turbulent environment, firms' size and structure on the planning-performance relationship. According to Elbanna (2010) a research conducted in UAE concluded that majority of firms have embraced strategic planning. It is also noted that prerequisite resources for adopting strategic planning did not pose a great deal and the involvement of higher position in the organization in the strategic planning tended to attract wider involvement in the process of strategic planning. Interestingly, there were no significant differences in her four groups of firms, that is, public, private, small and large firms.

Song, Im, Bij and Song (2011) note from their empirical research that intensity of strategic planning and product development activities tend to enhance firms' bottom line. Study conducted by Alaka et al. (2011) in Nigeria witnessed a favorable influence of strategic planning on profitability. Likewise, Owolabi and Makinde (2012) conducted a study in Nigeria using employees of Babcock University as respondents and inferredpositive correlation between strategic planning and corporate performance. They further noted that strategic planning helps in realizing firms' aims and ends. Nonetheless, Arasa and K'Obonyo (2012) note that past studies on the planning-performance relationship largely investigated the direct relationship between strategic planning and firm performance and has failed to check the relationship between performance and individual part of strategic planning.

According to Arasa and K'Obonyo (2012) research, firm performance was strongly and positively influenced by strategic planning. Further, positive association between organizational performance and distinct elements of strategic planning (e.g. firm's purpose, environment scanning, spotting strategic issues, choosing and putting into practice appropriate strategy, and evaluation and control mechanisms) were revealed. More to the point, a study of 160 Finnish SME IT companies by Kohtamäki, Kraus, Mäkelä, & Rönkkö (2012) revealed that participative strategic planning was positively associated with personal commitment to strategy implementation that in turn led to superior performance. In the same way, research conducted by Jenster and Søilen (2013) on Chinese firms, finds that strategic planning significantly impact a company's performance.

On the flip side, researchers have witnessed negative connection between strategic planning and performance (Dincer, et. al., 2006; James W Fredrickson & Mitchell, 1984; Hand, Sineath III, & Howle, 1987; Kudla, 1980; Pearce et al., 1987). Kudla (1980)in his research on 129 manufacturing and other firms notes that the impact of planning on returns was negligible. Similarly, using data from 27 firms, James W Fredrickson and Mitchell (1984) noted negative association between comprehensive planning and performance of firms operating in unstable environment. Likewise, the study of Hand et al. (1987) witnessed that planning were negatively associated with performance. In addition, Dincer et al. (2006) undertook a research on Turkish firms and noted that formal planning is negatively associated with strategic planning.

As opposed to the proponents of strategic planning, there are other researchers who have proved tenuous or no connection between strategic planning and performance (Birley & Westhead, 1990; Capon, Farley, & Hulbert, 1994; Hopkins & Hopkins, 1997; Kallman & Shapiro, 1978; Leontiades & Tezel, 1980; Mintzberg, 1991; Pearce, Freeman, & Robinson Jr, 1987). Kallman and Shapiro (1978) carried out research on 298 motor carrier firms and notice that firms' performance remained similar and not linked with firm size and adherence to strategic planning. Similarly, no connection between planning and performance has been confirmed by the study of Leontiades and Tezel (1980) on 61 firms. By the same token, no relationship between strategic planning and SME success has been identified by the study of Gable and Topol (1987) on 179 small retailers in USA. More to the point, Capon et al. (1994) noted a small impact of planning on performance by using metal-analytic approach. More to the point, insignificant relationship between strategic planning and small firms' performance were noted by the study of Risseeuw and Masurel (1994) in small Dutch firms. Moreover, Powell (1994) in his study proved that positive and significant association between strategic planning and performance is spurious when firm size is controlled. He further argued that as compared to a stable environment strategic planning was more effective in a turbulent environment. In addition, planning was found to be gainful in cost leaders than differentiators.

Likewise, O'Gorman and Doran (1999) noted no direct influence of formal mission statement on success of small firms. Furthermore, Gibson, Cassar and Wingham (2001)in their research on 2956 small Australian firms revealed no connection between strategic planning and SME performance. Similarly, Capon et al. (1994) noted that non-planners performed almost similar to those who employed strategic planning in short-run but in the long-run strategic planners outperformed non-planners. Moreover, Perry (2001) found out that non-failed firms in USA did more planning than failed firms.

The above review of literature establishes ground for developing the following conceptual framework.

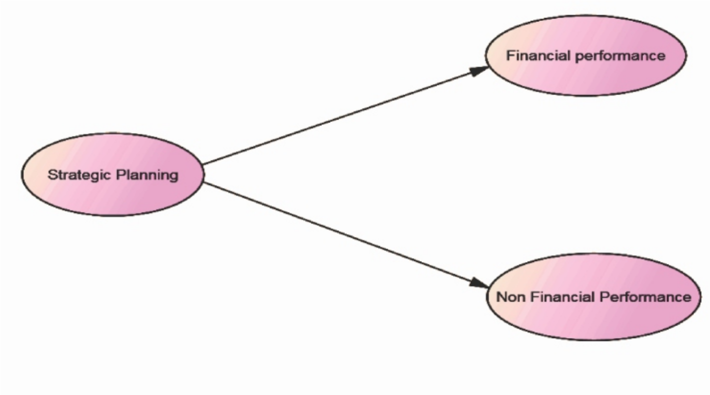

Figure: 1 Conceptual Framework

The conceptual framework leads us to frame the following two hypotheses.

H1. Strategic planning has positive influence on firm performance

H2. The positive effect of Strategic Planning (SP) on firms' Financial and Non-Financial Performance is stronger for High Performers (HP) than for Low Performers (LP).

3. RESEARCH METHODOLOGY

In this part sampling and data collection techniques are discussed followed by the measurement of the variables of interest namely firm performance and strategic planning.

3.1. Sample and Data Collection

In line with the recommendations of researchers(e.g. Hair, Babin, & Krey, 2017; Saunders, Lewis, & Thornhill, 2009) for conducting structural equation modeling/path analysis, we collected data from 245 respondents from SMEs manufacturing operating is Khyber Pakhtunkhawa, Pakistan. Following Saunders et al. (2009), the data were collected through delivery and collection method as it suited the business research situation. Moreover, Convenience sampling technique is employed as there is no available data base for SMEs. Similarly, the respondents consisted of owners and managers that added to the reliability and validity of the research as argued by Narkhede (2017). In addition, the definition of SME was followed as firms having more than 250M sales per year and having less than 250 employees given by Small and Medium Enterprises of Pakistan (SMEDA).

3.2. Measurement of Variables

The research aims to find out the influence of strategic planning on firm performance. Accordingly, the variables of interest are strategic planning and firm performance – financial and non-financial performance.

3.2.1. Strategic Planning

Strategic planning is measured as a first order factor targeting the understanding of managers regarding corporate strategy formation, managers being integral part of strategy formation process, managers' knowledge about important parameters for formulating jobs, managers' responsibility about the initiation and modification of long range operations strategy, and participation of managers in setting major future goals. Data on these five indicators were collected based on five-point scale ranging from 1 (lower performance than competitors) to 5 (higher performance than competitors).

3.2.2. Firm Performance

It is measured as a second order factor consisting of financial and non-financial performance. The financial aspect of the firm performance is measured in terms of profit growth, sales growth, profit margin, return on assets, and return on investment. Similarly, high customer satisfaction, employee satisfaction, retention, low turnover, as well as high market share are employed to measure the non-financial aspect of performance. Data on these indicators were collected based on five Likert point scale starting from 1 (performance lower than competitors) to 5 (performance higher than competitors).

4. DATA ANALYSIS

This part documents Confirmatory Factor Analysis (CFA) as well as reliability and validity checks followed by Path Analysis to test the impact of SP on FP.

4.1. Confirmatory Factor Analysis

Validity of the measurement scales are ascertained with the CFA (Kroes & Ghosh, 2010). Following Kroes and Ghosh (2010), CFA is conducted on all the measurement models namely strategic planning and firm performance simultaneously. More than one Goodness of Fit indices, suggests how well the proposed model fits the data, are calculated as no single fit index describe model fitness as recommended by researchers (Hair et al., 2017; Hu & Bentler, 1999; Janssens, De Pelsmacker, & Van Kenhove, 2008).

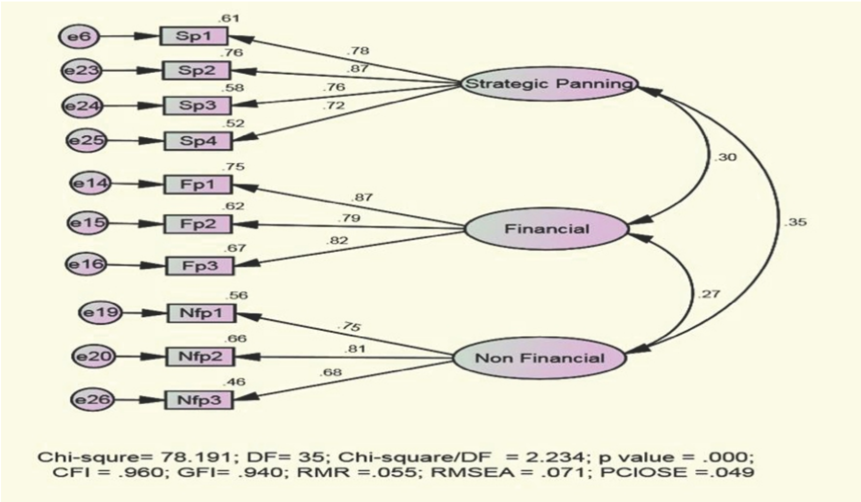

Figure: 2 Confirmatory Factor Analysis

4.2. Validity and Reliability

To ascertain the reliability and validity of the constructs, the Composite Reliability (CR), Average Variance Extracted (AVE), as well as Maximum Shared Variance (MSV) are calculated as recommended by Hair et al. (2017) and Fornell & Larcker (1981). The recommended thresholds for reliability and convergent validity are CR>0.7 and AVE > 0.5 respectively which are achieved. Similarly, Discriminant validity is ascertained by attaining MSV > AVE and squared correlation greater than AVE.

Table 1

Reliability and Validity

	CR	AVE	MSV	Financial	Strategic Panning	Non-Financial
Financial	0.865	0.681	0.092	0.825		
Strategic Panning	0.865	0.617	0.120	0.303	0.786	
Non-Financial	0.792	0.560	0.120	0.268	0.347	0.748

4.3. Path Analytic Model

We conducted Path Analysis to test the causal relationship among the variables of interest that is in consistent with the prior researchers (Badri, Davis, & Davis,2000; Hung& Lin , 2015). In line with the recommendations of researchers (Hair et al., 2017; Hu & Bentler, 1999; Janssens et al., 2008), all the goodness of fit indices namely Chi-square/Df (2.234), CFI (0.96), GFI (0.94), and RMSEA (0.07) meet the thresholds.

H1. Strategic planning has direct positive influence on firm performance

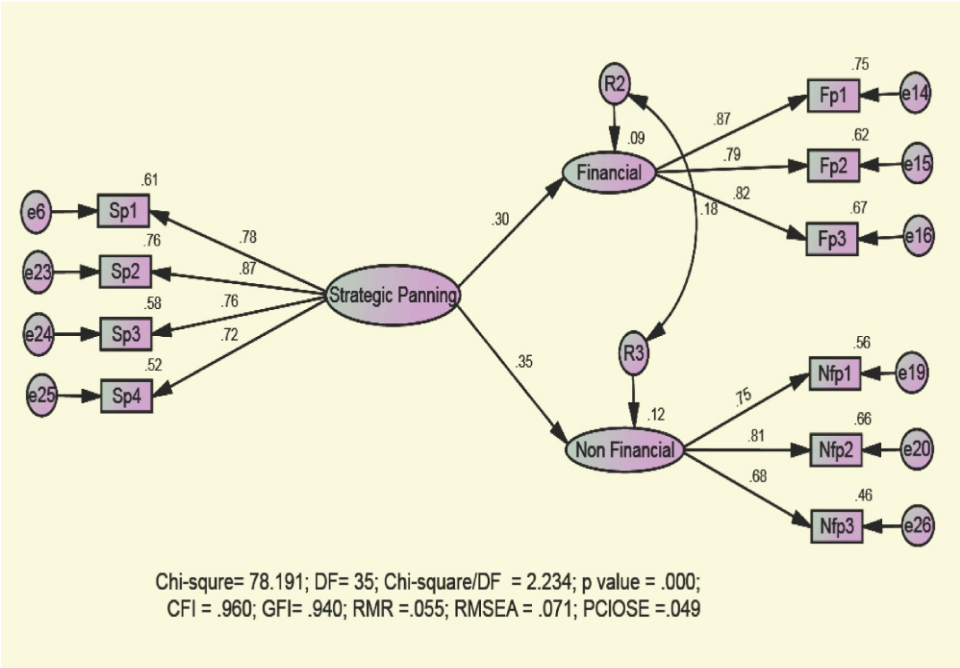

Figure: 3 Path Analysis of Strategic Planning and Firm Performance

The above path analytic model shows good fit indicated by several model fit indices meeting thresholds (e.g. Chi-square/Df<3, CFI and GFI > 0.9, RMR and RMSEA < 0.08, and P-close> 0.05). Strategic Planning shows positive and significant effect on Financial and Non-Financial performance as evidenced by CR>2 and p < 0.05. This result reinforces the study of prior researchers (Alaka et al., 2011; Andersen, 2000; El-Mobayeb, 2006; French, Kelly & Harrison, 2004; B. Gibson & Cassar, 2005; Glaister et al., 2008; Jenster & Søilen, 2013; Morgan & Strong, 2003; Owolabi & Makinde, 2012; Perry, 2001; Song et al., 2011; Stewart, 2003; Veskaisri et al., 2007) that report positive and significant effect of strategic planning on firm performance.

Noticeably, strategic planning exerts higher influence on non-financial performance (0.35) than on firm financial performance (0.30) as indicated by standardized regression loadings. The part of strategic planning that influences the most is that managers take part and contribute in strategy formulation indicated by the high standardized loading (0.87). This is followed by the part of strategic planning that deals with the understanding of mangers regarding the criteria for formulating jobs (0.78) as well as managers understanding of corporate strategy formation (0.76). The least emphasized part of strategic planning (0.72) deals with holding managers responsible for initiating and modifying changes in operations strategies.

This extends support to the acceptance of our hypothesis that strategic planning has positive and significant impact on firms' Financial performance (Alaka et al., 2011; Andersen, 2000; French et al., 2004; Owolabi & Makinde, 2012; Perry, 2001) as well as Non-Financial performance (El-Mobayeb, 2006; Song et al., 2011).

These results imply that firms should adhere to strategic planning for enhancing their firms' performance both financial and non-financial. Kraus et al. (2007) reported researchers that advocated that SMEs should not do strategic planning for reasons such as flexibility and management of SMEs are suffered; the employment of limited resources in operational, sales and R&D would do better in favor of SMEs than in strategy development; and a lot of bureaucracy involved in strategic management are disapproved by the research findings. Similarly, the stance of Aram and Cowen (1990) that strategic planning is only for large firms and not for SMEs are refuted as the research findings extend support for the positive and significant influence on firms' non-financial and financial performance.

H2. The positive effect of Strategic Planning (SP) on firms' Financial and Non-Financial Performance is stronger for High Performers (HP) than for Low Performers (LP).

In order to test whether the positive effects of SP on FP and NFP are stronger for HP than LP or not, we conducted MGA on the same model with little modification for achieving model fit (e.g. Chi-square/Df<3, CFI and GFI > 0.9, RMR and RMSEA < 0.08, and P-close > 0.05). The HP and LP groups were formed on the basis of average firm performance. First, the model was tested with entire data to check whether the model is different across the groups or not. MGA were carried out with all the parameters estimated freely in the model. The MGA test revealed that Chi-Square was not significant at the whole data indicating the two groups are not significantly different at model level.

Table 2

Estimates of Strategic Planning and Firm Performance

			Estimate	S.E.	C.R.	P
Non Financial	<---	Strategic Panning	0.249	0.056	4.461	***
Financial	<---	Strategic Panning	0.343	0.081	4.215	***
Sp1	<---	Strategic Panning	1			
Fp1	<---	Financial	1			
Fp2	<---	Financial	0.847	0.047	18	***
Fp3	<---	Financial	0.873	0.06	14.449	***
Nfp1	<---	Non Financial	1			
Nfp2	<---	Non Financial	1.167	0.12	9.725	***
Sp2	<---	Strategic Panning	1.188	0.08	14.9	***
Sp3	<---	Strategic Panning	0.909	0.071	12.802	***
Sp4	<---	Strategic Panning	0.847	0.047	18	***
Nfp3	<---	Non Financial	0.969	0.104	9.344	***

Consequent upon testing the whole model, the individual path analysis was carried out by constraining each path at one time while estimating the rest of parameters freely. The analysis showed that the individual path is not significantly different in the model across the groups. Thus, we cannot determine whether the effect of SP on firms' FP and NFP is stronger for HP or LP as the significant Chi-Square is the perquisite for establishing the strength of relationship. In conclusion, the hypothesis cannot be confirmed.

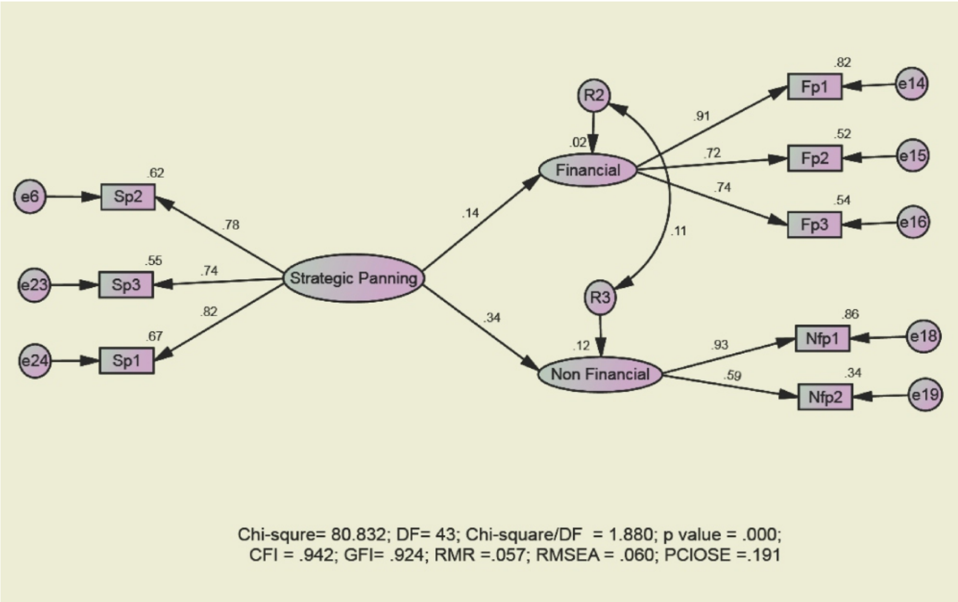

Figure: 4 Path Analysis of Strategic Planning and Firm Performance (HP)

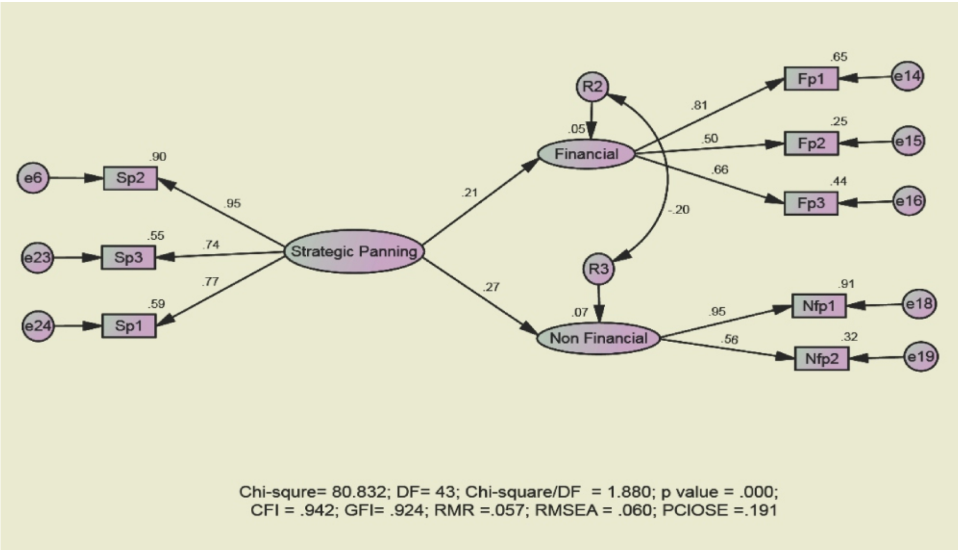

Figure: 5 Path Analysis of Strategic Planning and Firm Performance (LP)

Table 3

Over model estimates of Chi Square

Model (Structural Weights)	DF	CMIN	P
Environment – Performance	7	3.233	0.863

Model Comparison (structural weights)

Relationship	DF	CMIN	P
Strategic Planning – Financial	1	1.04	0.308
Strategic Planning - Non Financial	1	0.675	0.411

This research study is not an exception to have no limitations. Thus, the main constraints of the study included limited finances and access to respondents, as well as collection of perceptual and cross-sectional data only.

Future studies should conduct similar research on large scale and scope to validate or repudiate the findings of the study for enhancing our understanding of the SP-Performance relationship. Moreover, the same research should be extended to service sector SMEs as well. In addition, future studies should investigate the impact of some moderating and mediating variables on the SP-Performance relationship.

5. CONCLUSION AND IMPLICATION

This paper concludes that SMEs can enhance its performance not only financial but non-financial as well by conducting proper strategic planning. However, no difference across high and low performers were found with respect to effect of strategic planning on firm performance. This could be attributed to the lack of formal strategic planning as SMEs, by and large, do not exhibit in carrying out such activities for reasons such as lack of education and unawareness.

These findings have important implications for managers of both highand low performers. Managers of low performers' firms should pay due attention to their strategic planning process and find out as well as rectify any mistakes to avail the associated benefits of strategic planning. Similarly, managers of high performers' firms should find out any room of improvement in the strategic management process to reap the benefits of strategic planning. Moreover, SMEs should employ formal strategic planning to reap its benefits.

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