AN EMPIRICAL INVESTIGATION INTO FORMALISED STRATEGIC PLANNING IN SMALL AND MEDIUM ENTERPRISES (SMEs) IN SRI LANKA

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ABSTRACT

An energetic Small and Medium Enterprise (SME) sector plays a pivotal role in the growth of any economy as it provides a number of benefits for economies, irrespective of their level of development. Recognising this reality, governments around the world increasingly encourage and support SMEs as part of their overall national development strategies (Abdullah & bin Bakar, 2000), and Sri Lanka is no exception. The commitment of the government of Sri Lanka to the strengthening of the country’s SME sector is clearly stipulated in its national economic policies. Despite this external push from the government, SMEs in Sri Lanka have yet to improve their sustainability (Wijesinghe et al., 2011, 2012). Prior research suggests a positive relationship between strategic planning and business performance. As such, it is highly likely that internal factors such as having formalised plans among SMEs could help to facilitate their survival and growth. The purpose of this paper is three-fold: 1) to explore, by means of an empirical investigation, the strategic behaviour of Sri Lankan SMEs; 2) to examine the reasons for adopting such behaviour; and 3) to ascertain whether their strategic behaviour is related to their performance in business. Due to the exploratory nature of this study, a mixed methods research approach is used. Ansoff’s (1988) model, which indicates that strategic behaviour can be reactive, proactive-ad hoc or proactive-systematic, is adapted to analyse the data collected from a survey of 150 selected SMEs and eight case studies. The respondents are the owners or senior managers responsible for long-term planning and decision-making. Findings reveal that less than 25% (32) of the respondents are using formal strategic plans. Further analysis confirms that these same respondents, classified as employing a proactive systematic approach, experienced growth in their operations.

Field of Research: Mixed Methods, SMEs, Strategic Planning, Strategic Behaviour Modes
1. INTRODUCTION AND BACKGROUND

A vibrant Small and Medium Enterprise (SME) sector plays a significant role in the growth of any economy. This is because SMEs provide employment opportunities to help generate dynamism by enabling entrepreneurial capability to be realised (Hussain, Si, & Ahmed, 2010) while using locally produced raw materials. As such, SMEs can provide some relief from the vicious circle of poverty (Hussain, Si & Wang, 2010; Amaratunge, 2003; Mintoo, 2004). Further, Davidson and Griffin (2003) point out that small businesses contribute many innovative ideas and technological breakthroughs to society. Governments increasingly encourage and support SMEs as part of their overall national development strategies, irrespective of their level of development (Abdullah & bin Bakar, 2000). For example, the development strategies underpinning the ‘Mahinda Chinthanaya (Mahinda Vision)’, first enunciated by the President of Sri Lanka, have been introduced since 2005. This strategic document clearly stipulates the commitment of the government of Sri Lanka to taking important steps to strengthen the country’s SME sector. Despite this intervention, SMEs in Sri Lanka have yet to improve their sustainability (Wijesinghe, Wijesinghe, Foreman & Elijido-Ten, 2011; Wijesinghe, Elijido-Ten, & Foreman, 2012).

Among the main objectives in strategic management research has been to find the answers to the questions of “why do some organisations succeed while others fail?,” and “what are the processes that allow organisations to succeed in business?” Some researchers (for example, Bracker & Pearson, 1986; Bracker, Keats & Pearson, 1988; Jones, 1982; Robinson & Pearce, 1983; Shrader, Mulford & Blackburn, 1989) have identified a positive relationship between strategic planning and business performance. Sun Tzu showed the importance of strategies to Asian businesses with his seminal contribution to strategic management, ‘The Art of War’. Since then, Asian businesses have started to apply strategies in their businesses. However, only a small number of studies have been conducted in this context to investigate their strategic behaviour and strategic planning (Ko, 2009). Therefore, this study aims to address the questions of the extent to which Sri Lankan SMEs undertake strategic planning in their management processes, the reasons behind the absence of such planning systems and the relationship between their strategic behaviour and performance, by means of an empirical investigation.

Due to the exploratory nature of this study, a mixed methods research approach is used, as it permits the combination of both quantitative and qualitative research techniques with their associated methods, approaches, languages or concepts, in a single study (Creswell Vicki, & Clark, 2007). Ansoff’s (1988) model, which indicates that strategic behaviour can be reactive, proactive-ad hoc or proactive-systematic, is adapted to analyse the data collected from a survey of 150 selected SMEs and eight case studies. The respondents are the owners or senior managers responsible for long-term planning and decision-making. Findings reveal that less than 25% (32) of the respondents are using formal strategic plans. Further analysis confirms that this same group of respondents, classified as employing a proactive systematic approach, experienced growth in their operations.

2. LITERATURE REVIEW

The literature review of this paper can be presented in two sub-sections.
2.1 Strategic Management

Business organisations evolved from the replacement of the barter system with a monetary system for the exchange of goods and services. It is claimed in the literature that those early businesses were traditional and mostly inefficient. They were not concerned about how to perform or how to organise that task (Drucker, 1999). After the industrial revolution in the Western world, an investigation was begun into how organisations can organise their activities in an efficient way. As a result, a continuum of management theories came into being. However, in the 1970s management practitioners and researchers identified some changes in the business environment and their concern about management moved the development of theories into another important phase. This resulted in a focus on studies designed to explore more theories that are grounded in a strategic or proactive base. The literature highlights this phase as contemporary strategic management. There has been some confusion regarding the terms strategic planning, strategy formulation and strategic management. Sometimes they have been used synonymously (De Kluyver, 2000). Therefore, it is useful to clarify this concept based on the literature in order to establish the position of the present study.

As noted by Verreyne (2006), strategy-making processes have been described in various ways, ranging from Mintzberg's (1973) adaptive and entrepreneurial model, to Hart's (1991) generative and symbolic model. However, Verreyne (2006) indicates that most of those authors have commonly recognised the rational or planned mode as the predominant strategy-making process found in firms (e.g. Mintzberg, 1973; Robinson & Pearce, 1983; Hart, 1991).

O'Regan and Ghobadian (2002) claim that strategic planning can be considered from a content or a process viewpoint. The term content relates to the distinct elements of the strategic plan that differ from firm to firm, while the term process relates to the mechanisms for the development of the strategic plan and its subsequent deployment. This entails that plans can be modified until they are implemented and often results in changed or unrealised content (Mintzberg & Waterman, 1985; Mintzberg, 1987). This is because, in a dynamic business environment, the plans of many organisations are constantly modified, revised and refined, often in the minds of the top management (Henderson, 1989; O'Regan & Ghobadian, 2002).

Combining both the process and content viewpoints, formal strategic planning is defined as a process of determining the mission, major objectives, strategies and policies (long-range plans) that govern the acquisition and allocation of resources to achieve organisational aims (Thomson & Strickland, 2001; David, 2007; Wheelen & Hunger, 2008). This method of planning helps with the effective management of environmental opportunities and threats, in the light of corporate strengths and weaknesses (Pearce et al., 1987, p. 658; Stonehouse & Pemberton, 2002; O'Regan & Ghobadian, 2004; Wheelen & Hunger 2008, p. 12). Therefore, strategic planning complements the management function that involves the entire strategic process within an organisation through a set of closely interrelated components: environmental scanning, strategy formulation, strategy implementation, and evaluation and control (David, 2007; Wheelen & Hunger, 2008).

Strategic management and planning has been recognised as an important tool for all kinds of organisations, but whether or not this should be formalised is still the subject of controversy (Angkasuvana, 2005). Nevertheless, in this study, a written strategic plan is adopted as a surrogate for formalisation. This is because a written strategic plan can be considered to be the result of a process of strategy formulation and it demonstrates the intention of the principal decision-makers to undertake
strategic management in their organisations. Although firms have written plans, the principal decision-makers do not suppress new strategies but them to emerge (Mintzberg & Warters, 1985).

2.1 Strategic Management in Asian Businesses

Asia covers a wide range of geographical, economic and cultural spheres. Therefore, it also comprises a variety of business cultures, with a variety of religious values, ranging from Buddhist to Islamic, and ethnic identities (Rowly & Warner, 2007). The literature shows that industrialisation in the West that required two hundred years was accomplished in less than 50 years in Asia (Achyuthan, 2004).

Even though practitioners consider that management is a universal requirement, the literature shows that there is a noticeable difference between Western and Asian business management practices. For example, Haley and Tan (1996) reported that the style of decision-making and strategic management practiced in Asia differs from that practiced in the West. This is because many Western managers learn strategic planning and how to use ‘minds’ and ‘hands’ during their ‘MBA days’.

Asian managers can survive and flourish anywhere, ‘not because they are Asian or Western managers, but because they are smart and gutsy managers’ (Hamlin, 2000, p. 91, cited in Achyuthan, 2004). This emphasises the fact that Asian managers are successful with ‘hearts’ and ‘guts’ as they use intuition with their considerable intelligence, even though they have little formal education and less managerial training (Ko, 2009; Wijesinghe, Foreman & Elijido-Ten, 2011). The Sri Lankan education system prepares students for government employment rather than encouraging engagement in self-employment (Nanayakkara, 1984). Therefore, the literature that has investigated the Sri Lankan entrepreneurial characteristics suggests that most of the founders of successful businesses started their entrepreneurial culture with virtually nothing (Perera & Buddhadasa, 1992; Ranasinghe, 1996a, cited in Fernando, 2007).

On the other hand, many researchers point out that top management in Asia play the dominant role in strategic decision-making, with little participation from and consultation with lower level managers or operational staff (e.g. Thomas & McDaniel, 1990; Ghosh & Chan, 1992; Chan & Chiang, 1994; Sull & Wang, 2005). This is identified as the ‘information black hole’ or ‘information avoids condition’ in Asian companies (see Haley & Tan, 1999, 1998). However, the industrial sectors in most of the Asian countries (Japan, Singapore, Malaysia and China) were developed in the late 1990’s and business owners and managers understand the importance of environmental scanning, personal knowledge of markets, and success in planning and selecting strategies (Haley & Tan, 1998), or in other words professionalism. This has led to the development of a number of unique strategic management styles for Asian economies, all of which were definitely based on local cultural values (Hofstede, 1994).

2.1.1 Ansoff’s (1988) Strategic Behaviour Modes

Ansoff introduced three modes to evaluate strategic behaviours of organisations: the reactive, proactive-ad hoc and proactive systematic modes. These modes differentiate strategic behaviour on the basis of how managers in an organisation prepare or respond to the strategic issues confronting their organisations, as shown in Table I.
Under normal circumstances, in the reactive approach to strategic behaviour the management would diminish strategic change. Strategy is generated and shaped by reacting to issues or circumstances such as ‘complaints’ or ‘suggestions’, or in response to a sales trend, reflecting a change in the tastes or preferences of customers. Reactive firms usually avoid drastic strategic changes until they are confronted by an imminent crisis. When an organisation does change, it does not make plans or seek alternatives, but depends on a process of trial and error. If a series of solutions (trials) fails, the firm goes into bankruptcy.

The proactive-ad hoc mode of strategic behaviour is a more forceful and energetic management behavioural pattern. There is no articulated or centrally guided planned strategy development. The organisation depends on perusing incremental strategic changes. The main difference between the reactive and ad hoc modes is that in the latter the requirement for strategic change is recognised, but the search for new strategies depends on trial and error, not on a written and well-articulated, comprehensive plan. Ansoff (1988) states that this mode is similar to logical incrementalism (see Quinn, 1978) and it connects with Mintzberg’s implicit strategy of a firm (see Mintzberg, 1979). Further, in this situation, firms need incremental evolution of their strengths in strategic behaviour, through commitment from the bottom-up, research and development, and marketing.

Finally, the proactive systematic mode pertains to a planned and systematic form of management. Strategies are based on the explicit forecasts of trends and analysis. Formal plans make the rationale and the generation of new moves explicit and co-ordinates their proper implementation on a firm-wide basis. Ansoff explains that in a turbulent environment, strategic planning is pitted against logical incrementalism, but by re-examining and reformulating the strategic logic (plans), a firm can ascertain its future development. He also mentions that written strategic planning does not conflict with entrepreneurship and creativity, because strategic planning and management also need novel capabilities, innovativeness and creative thinking.

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3 Logical instrumentalism – consciously trying to deal with precipitating events in an incremental fashion (Quinn 1978).
4 Implicit Strategy refers to strategy as a pattern (see Mintzberg 1979)
Table I: Strategic Behaviour - Ansoff’s Model

<table>
<thead>
<tr>
<th>Management Mode</th>
<th>Types of Change</th>
<th>Discontinuities, diversification, divestment, globalisation or technology substitution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reactive</td>
<td>Trial &amp; error reaction to unsatisfactory performance</td>
<td>Panic search for solutions in reaction to a crisis</td>
</tr>
<tr>
<td>Proactive Ad Hoc</td>
<td>Bottom-up, episodic, logical incremental initiatives by R &amp; D and marketing</td>
<td>Trial &amp; error search in reaction to perceived discontinuity. Episodic, systematic anticipation of discontinuities (Issues Management: Crisis Management)</td>
</tr>
<tr>
<td>Proactive Systematic</td>
<td>Firm-wide periodic exploration of historical trends and performance (Long Range Planning: Strategic Planning)</td>
<td>Firm-wide periodic, systematic revisions of the logic of the firm’s future development (Strategic Planning: Strategic Management)</td>
</tr>
</tbody>
</table>

(Source: Ansoff 1988, p. 229)

These modes clearly identify the strategic behaviour of firms that has been based on the definition of strategic management process (David, 2007; Wheelen & Hunger, 2008). Further, it helps to identify the most appropriate or successful strategy making process as that proactive systematic method (strategic management) which includes strategic planning and strategic thinking.

Ghosh and Chan (1992) conducted empirical studies of strategic planning behaviours in two Asian countries (Singapore and Malaysia) and explained that their strategic behaviours are generally reactive and ad hoc. This means the majority of business organisations in these two countries were not using systematic strategic planning processes at the time their study was undertaken. Similarly, Lee (1986) found out that compared to American companies, SMEs in Japan were not preparing written plans and were weaker in planning. Hitt et al. (1997) also revealed a similar difference between American and Korean managers. These differences prompted Nakamura (1992) to make clear the importance of strategic planning in East Asian countries, especially in Japan (Nakamura, 1997).

3. METHODOLOGY

Mixed methods research combines both quantitative and qualitative research techniques with their associated methods, approaches and concepts in a single study (Creswell et al., 2007). Bryman and Bell (2007) suggest that the mixed methods approach/triangulation has increasingly become the preferred method in social research, as it improves the accuracy of findings by collecting different kinds of data related to the same research. Due to the exploratory nature of the current study, the mixed methods research approach (triangulation) is used.
3.1 Data Collection

The primary data was collected from a sample of 150 small and medium-scale enterprises in the manufacturing sector and eight case studies in Sri Lanka. The snowball sampling technique was used for the survey (Bryman & Bell, 2007) as there is no complete, up-to-date or reliable database of the SME sector in Sri Lanka available to a private researcher. The case studies were selected using the purposive sampling method (Kuzel, 1992; Morse, 1989, cited in Miles & Huberman, 1994), based on the survey findings. The respondents were the owners or senior managers responsible for long-term planning and decision-making for a manufacturing organisation with five to 149 regular employees. The sample covered start-ups, stagnating, growing and failed SMEs to improve the validity and reliability of the findings.

More than one-third of the sample are drawn from the Colombo district because it is the most populated and industrialised (Kapurubandara & Lawson, 2007) of the 26 districts in Sri Lanka. Moreover, the owners and managers of SMEs in this district are usually considered to be more educated, and to have some knowledge of sophisticated management practices, than those in other districts. They also have the opportunity to make greater use of the available infrastructure facilities, such as information technology and financial services, and other forms of institutional support (Kapurubandara & Lawson, 2007), than their counterparts operating SMEs in the other districts in Sri Lanka.

As noted by Kapuge and Smith (2007), scaled responses (structured questionnaires) do not allow respondents to provide detailed answers. Consequently, researchers need to address this issue in subsequent follow-up interviews. Therefore, in addition to scaled data collection methods, further qualitative analysis is useful in contemporary social research. Previous studies on SMEs have successfully adapted the case study method to conduct in-depth investigations (for example, Ghauri et al., 2003; Caldeira & Ward, 2003; Huang, 2009). Ghauri et al., (2003) have used five case studies to conduct research related to SMEs. Similarly, in conducting case studies for this research, six existing (two successful, two stagnating and two newcomers) and two failed SMEs were selected in order to strengthen the external validity of the study.

3.2 Data Analysis

The quantitative analyses in this study comprise both descriptive and inferential statistical methods using SPSS. The descriptive analyses include calculating averages, frequency distribution and percentage distribution. While the descriptive statistics in this study provide information regarding the sample, inferential statistics (Chi-square and Fisher’s exact tests) were used to make estimates of likely values for population characteristics and relationships.

An in-depth interviewing method is used to gather qualitative data. As noted by Miles and Huberman (1994), qualitative data are usually presented in the form of words rather than numbers. Qualitative data is also a good source of well-grounded, rich descriptions and explanations of processes in identifiable local contexts. Therefore, the data analytical techniques suggested by Miles and Huberman (1994) and Yin (2003) for within-case and cross-case analysis are applied. These include theme identification, pattern matching and explanation building.
4. FINDINGS AND DISCUSSION

Of 150 participants in the survey, 17 firms were start-ups with less than two years’ experience in business. The other 133 included 64 stagnating, 66 growing and three failed firms. A total of 104 enterprises were small firms and 46 were medium-sized. With regard to ownership, 73 of the total of 150 were sole proprietorships. There were also 17 family-owned enterprises, 18 partnerships, 41 private limited companies and one government-affiliated SME.

4.1 Survey Findings

As suggested by the literature, all participant SMEs were divided into two categories, those that used formalised strategic planning (FSP) system and those that did not (non-formalised strategic planning - NFSP). Research established that only 32 SMEs use written or, in other words, formal strategic planning systems. Therefore, the remaining 118 SMEs can be categorised as non-formalised strategic planning (NFSP) enterprises. The companies in the FSP group comprise 25% small and 75% medium-sized manufacturers. Although the majority of NFSP enterprises (96 out of 118) were small firms, 52% of medium-sized enterprises were within the FSP category. Unsurprisingly, failed businesses had not undertaken formal strategic planning processes during their period of operation.

The results show that the first reason for 89 (75%) of 118 SMEs falling into the category of NFSP is a lack of time to prepare or maintain a formal strategic planning system. A total of 116 participants give their second reason for operating as a NFSP SME (see Table 2). Of those 116 firms, 40 (34%) stated that they did not use formal strategic plans due to an inadequate knowledge of planning within their organisations. A further 24 (21%) cited a lack of institutional expertise for not utilising such mechanisms. Only 67 firms stated a third reason in this regard (see Table 2). The majority of this group variously identify as their third reason an inadequate knowledge of planning, the type of industry to which they are attached, and environmental uncertainties.

4.2 Case-study Findings

The survey findings help to categorise SMEs as either FSP or NFSP, based on their having written plans. Therefore, a total of eight in-depth interviews were conducted to compare survey findings and examine the insights into strategic planning systems and barriers confronting the participants. FSP SMEs are experiencing growth in their business operations. Furthermore, according to case-study findings, NFSP firms can be further categorised: failed firms have been using reactive type strategic behaviour and other SMEs, mostly start-ups and stagnating firms are using either reactive or proactive but ad hoc systems (Ansoff, 1988).

Confirming the survey results, all participants who granted in-depth interviews explained that their shortage of time and lack of knowledge are the main problems in this regard. The owner-managers of SMEs, especially in the case of smaller firms, lack time because they are trying to actively participate in almost all the activities of their businesses. The reason behind this situation is that they are reluctant to delegate decision-making authority and empower their workers. They do not trust workers or their abilities. However, some owner-managers do not plan for their businesses but depend on luck in
business. One of the participants from a stagnating firm mentioned that, due to a lack of management expertise, he has no idea of the importance of having formal strategic plans and, therefore, it takes much of his valuable time to learn about such devices and try to put them into practice.

4.3 Synthesis of Findings

According to the survey, Chi-square test results indicate that for both small firms ($\chi^2 = 37.602 \text{ (df } = 1) \text{ Cramer’s V} = .501, p = .000 < .05$) and medium-sized manufacturers ($\chi^2 = 6.148 \text{ (df } = 1) \text{ Cramer’s V} = .366, p = .013 < .05$), there was a significant relationship between formal strategic planning and the current situation of the firms. The majority of growing SMEs are more likely to have formal strategic plans, but the majority of start-ups and stagnating firms are operating without such devices. Therefore, the reason behind growth and stagnation of SMEs can be considered a result of their strategic behaviour.

Two FSP firms, consisting of one small start-up firm and a growing medium-sized company, were included in this in-depth investigation group. On the basis of the experiences recounted by this group, SMEs will tend to use written strategic plans only if the principal actors within a firm have formal management education and/or prior business management experience. The participants also mentioned that their prevailing proactive systematic approach is very useful for dealing with the strategic issues they face in the current business environment.

Even though the matter of whether or not strategic planning should be in written form is a subject of controversy within the literature (Angkasuvana, 2005), these findings show that to increase rates of success in business, decision-makers should use their minds and hands (plans) simultaneously with hearts and guts (intuition).

5. CONCLUSIONS AND RECOMMENDATION

Although strategic management is a useful practice and strategic planning is a valuable tool in the management of a business, the majority of Sri Lankan SMEs do not undertake it in a systematic manner using a written plan. The reason behind this shortcoming in the sector is a lack of formal training in and knowledge of management, and the strength of some Asian cultural traits such as a dependence on luck and guts. Given this state of affairs, they tend to use reactive or proactive ad hoc modes of strategic behaviour. Even though in the 1990s these behaviours were justifiable because contemporary strategic management was only in the early stages of its development, after two decades it is no longer acceptable or excusable in highly turbulent business contexts. Sri Lankan entrepreneurs are in a confusion of Western management concepts and Eastern practices which is based on culture and intuition. As a result, there is a high likelihood of these organisations stagnating or failing. Some Asian countries, such as China and Japan, are trying to converge their practices with Western management concepts in order to obtain economic benefits. Following the approaches adopted by these nations, entrepreneurs in Sri Lanka, particularly those operating SMEs, should directly undertake strategic management in a proactive and systematic way in order to improve the performance and sustainability of their enterprises. This is because in order to increase rates of success in business, decision-makers should use their minds and hands (written plans) simultaneously with hearts and guts (intuition). Policy makers have a significant role to play in this scenario, as this pattern of behaviour should be instilled by
the education system of Sri Lanka. Then, regardless of size, all business organisations will be able to undertake their management processes more professionally in order to secure their own well-being.

REFERENCES


