

# Incidence of Strategic Planning in Small Business: an Overview

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## Abstract

*During the last several years, extensive attention has been paid to the issues relating to strategic planning. Even practitioners and academicians have continued their debates on the merits of strategic planning. The literature on planning in small business has grown considerably over the past decades. With a few notable exceptions, many scholars have recommended that small firms need to use strategic planning as an essential tool for their improved performance. According to Gibb and Scott (1985) strategic planning can almost certainly influence the growth of the company and provide a framework for enhancing this or it can also help maintain the existing size and capability of the firm. However, the preconceived notions of strategic planning support the idea that formal strategic planning practices heighten the owner managers' ability to think strategically (Porter, 1980; Lyles et al., 1993). Hence, the present study is initiated on incidence of strategic planning in small business. Secondary data have been taken from research monographs, books, and journals etc. Therefore, this study will contribute to the existing stock of knowledge in the literature of strategic planning in small business. Finally, based on the empirical findings strategic planning contributed significantly to the relationship with the overall performance of small business under study.*

**Keywords:** *strategic planning, small business, performance*

**JEL Classification:** *M1, M14, M16*

## Introduction

Importance of strategic planning as a major activity of organizational management is being increasingly accepted by both academician and professional managers. The literature on planning in small business has grown considerably over the past decades. With a few notable exceptions, many scholars have recommended that small firms need to use strategic planning as an essential tool for their improved performance.

Support for the planning process in small firms comes from a variety of writers in a number of forms (Gibb and Scott, 1985). It is often asserted that strategic planning is essential for a small as well as a large business for no other reason than that it helps them to take better advantage of the opportunities which lie in the future and to forestall the threats that it contains (Steiner, 1967). Strategic planning is seen as a necessary attribute of entrepreneurship. Carland et.al., (1984) used the term “entrepreneur” to mean the innovative owners of small firms who use strategic management practices. Strategic planning is also assumed to be associated with

success. As Bamberger (1980) noted there is a positive relationship between the existence of a more or less formal strategic planning system and the firm's growth.

## **Concept of Strategic Planning**

Strategic planning was defined operationally by three elements of the strategic planning process: environment awareness, the existence of idea or formal documentation of a future strategic course of action, and awareness of both short and long term implications of strategies. Environmental awareness is a concept from business management by which businesses gather information from the environment, to better achieve a sustainable competitive advantage. To sustain competitive advantage the company must also respond to the information gathered from environmental scanning by altering its strategies and plans when the need arises.

Strategic planning consists of planning processes that are undertaken in firms to develop strategies that might contribute to performance (Tapinos, et.al, 2005). Key aspects of strategic planning are: a long-time horizon, formality, the use of planning instruments, and frequent control of plans. Strategic planning can contribute to performance by generating relevant information, by creating a better understanding of the important environment, and by reducing uncertainty (Hodgetts and Kuratko, 2001). Strategic awareness implies the ability to make an assessment of the total implications of any particular change (Gibb and Scott, 1985). This means not only awareness of the immediate implications of any new development but also reflection on the longer term repercussions. In order to gain insights into strategic awareness of owner managers, who had projections about their strategic action, they were asked to talk about: the implications of their future projects on their time and life style; the firm's capital assets; employees; raw materials; and marketing.

## **Small Business**

Small-scale industries can play an important role in the economic advancement of many countries. Historically, the small-scale enterprises have formed the base of industrial structures and facilitated the process of industrialization in most countries irrespective of their stages of development. In the light of scarce resource endowments and other socio-economic realities of developing countries, this sector typically comprises over ninety percent of all industries. Small business is a field that is often mentioned but since it covers a wide range of activities its concept and definition vary enormously from one place to another, from one country to another and from one author to another.

There is no universally accepted definition of small-scale industries. But the term 'small-scale industry' is used everywhere, both in developed and developing countries, to denote the character of a particular type of industry. In fact, the definition has undergone changes over time in most countries. Even in a single country the definition varies from time to time. Some scholars use qualitative criteria and attempt to define them in terms of functional characteristics like specialization in management, access to capital market etc.

One study on small business sector has identified more than 50 different definitions in 75 countries (ILO, 1977). However, publications in the field of small business do not usually make any distinction between different types of small business, be they manufacturing, service or retail, since the difference between them is almost non-existent as far as the characteristics of the enterprises and entrepreneurs as well as their pattern of functioning are concerned.

Carland et. al., (1984) defined small business in line with the "Canadian Federation of Independent Business" but denied small business's ability to engage in new marketing and innovation. According to them, "small business enterprise does not engage in any new

marketing and innovation practice". On the other hand, Barnett and Machness (1983) defined small firms as those which are characterized by: (1) A lack of specialist services to advise management; (2) The necessity for senior people to get involved in all aspects of running the business; (3) Only one or two people are usually involved in significant decision making; (4) A lack of time for the senior men to think about the development of the firm. Some argue that the least objectionable way to define "small business" would be "to sort out firms according to the number of employees or persons engaged".

A small business may be defined as a business with a small number of employees. The legal definition of "small" often varies by country and industry, but is generally under hundred employees in the United States (US) while under fifty employees in the European Union (In comparison, the American definition of mid-sized business by the number of employees is generally under five hundred while two hundred and fifty is for that of European Union). (Barnett and Mackness, 1983). These businesses are normally privately owned corporations, partnerships, or sole proprietorships. However, other methods are also used to classify small companies, such as annual sales (turnover), assets value or net profit (balance sheet), alone or in a mixed definition. These criteria are followed by the European Union, for instance (headcount, turnover and balance sheet totals) (Levitsky, 1988).

Histrich and Dronvsek (2002) emphasised that the field of small business is close to entrepreneurship as the latter, recognises the importance of the manager, who is very often the owner. However, entrepreneurship and small businesses were largely neglected within the field of management and economics until the late 1970s and early 1980s. With the 1970s, being a decade of structural crises that hit mostly large companies, small businesses came to be regarded as the answer to structural changes and employment problems (Huse and Landstrom, 1997). One of the key triggers to shift the emphasis from large to small organisations was Bolton Report (1971), which drew attention to the economic importance of small firms. As a result, interest in entrepreneurship and small business increased significantly in many European countries and education programmes were created in several European universities (Huse and Landstrom, 1997). Keeping this in mind, Levitsky (1988) defined small businesses as those enterprises which employ no more than 5-10 workers, including the owner and family. They engage in non-corporate income generation and use less than US\$10,000 equivalent of total capital; the starting capital is often less than US\$100 and rarely exceeds US\$ one thousand. Others defined small enterprises as establishments with ten to forty nine persons whereas the cottage and household industries as establishments with one to nine persons, thus excluding cottage or household units from small business enterprises.

### **The Environment of Small Business**

The environment of small business is often defined by the type of business or service rendered, and in most instances the opportunities for small business are defined by the characteristics of a community. Small business comprises many local enterprises, service companies, and professional organizations that constitute more than half of all non-farm employment in the United States. This profile of small business is remarkably similar among most free-market nations. Small businesses include merchandisers to which we turn for a significant amount of our daily purchases. It also includes "practices" and "personal service" enterprise of doctors, accountants, tailors, interior designers, and many others to whom we turn for personal needs. There are also a substantial number of small manufacturers, wholesalers, distributing companies, and vendors who focus on specialized niches to provide everything from local bakery goods to space telecommunication equipment. Many of these entrepreneurs are small by choice. They probably have opportunities to expand into new markets or to develop into larger organizations, but they prefer the autonomy of a small business and subsequently avoid rapid expansion.

The independent business person has quite a different role from that of a high-growth entrepreneur or corporate business manager. As a risk-taking owner of an entrepreneurial venture, innovation and growth require the organizational abilities to gather resources and establish new venture teams. Corporate business managers become professional specialists, focusing on specific tasks or responsibilities, such as tax accounting, design engineering, or advertising. Small business owners must wear many “professional hats” at once. They may hire a few people, but they behave more as an autonomous owner than as a professional manager. The owner will also assume the risks associated with financing and operating a new business, but those risks are seldom related to innovation development.

### **Incidence of Strategic Planning in Small Business**

Even though some studies (Watts and Ormsby, 1990) have provided frustrating results as to the relationship between strategic planning and performance of small business, and that there is a tension between normative statements and the findings of empirical research (Hanlon and Scott, 1993), increasing evidence has confirmed that strategic planning has a positive effect on the performance of small businesses (Schwenk and Shrader, 1993). Another view is that formal strategic planning provides a structure for decision making, helping small business to take a long term view. Others have claimed that formal strategic planning enables organisation to better prepare for and to deal with the rapidly changing environments that most of them face. Furthermore, strategic planning is supposed to yield objectives that provide criteria against which organisational attainments can be measured (Orpen, 1993). Lyles et.al., (1993) argued that as small business owners adopt a more formal planning process, the breadth of strategic planning can most certainly influence the growth of the company and provide a framework for enhancing this or it can also help maintain the existing size and capability of the firm (Gibb and Scott, 1985). However, their excessive focus on formalisation and ignorance of the value of strategic thinking and awareness has held a controversial explanation of the planning-performance relationships.

Research indicated that strategic planning in small business is informal, unstructured, and irregular, supported by insufficient and ineffective information, usually obtained through informal sources, and reactive rather than proactive (Gibb and Scott, 1985; Flavel, 1991). Although managers in small firms engage in strategic thinking, such deliberation is seldom formal (Gibb and Scott, 1985, Mintzberg, 1994). Many reasons have been identified for the absence of formal strategic planning in small business. These include lack of time, cost, expertise, information, training, education and skills of owner-managers (Robinson and Pearce, 1984; Shrader, et.al., 1989). A number of authors have suggested that a formal strategic plan may not be suitable for small business as they believe that high level of formality may often fade away important innovations and suppress creativity and spontaneity. They also argued that strategy may often emerge outside the formal process of planning and that the emergent strategies are often successful and may be more appropriate than planned strategies.

In the absence of an explicit strategic planning process in small business, the importance of the awareness of environment and that of strategy - the ability to make an assessment of the total implications of any particular change - have been found to be crucial to the development and survival and growth of small business (Gibb and Scott, 1985). This means that environment awareness, making timely changes and most importantly, the awareness of the implications of their strategic actions are more important in small business than merely formalisation of their thinking and awareness. This may appear more naturally with some owner-managers. However, other inputs also influence the process. As with the study of Gibb and Scott (1985), the data reported here that most owner-managers of small firms have ideas or portfolio of ideas of projected action to avail themselves of relevant opportunities and for dealing with the threats existed in the environment. The generation and evaluation of ideas is mainly characterised by

personal judgements of owner-managers, and by insufficient information often based on limited knowledge of the market place, customers' needs, technology, and policy, especially of support policy. Their ideas, in many cases, are not clearly articulated. They are also very often flexible, reactive and set for unspecific time horizons. Owner-managers usually do not think about alternative ideas in advance in case planned strategies would be difficult to implement as many of them are unaware of potential changes that may occur in the environment over longer periods. Owner-managers very often shift to other ideas or make changes to their original ideas once they experience intolerable changes in the environment as well as in their resources. In other words, Mintzberg and Waters (1985) called "entrepreneurial strategy", which involves the features of both deliberate and emergent strategies.

Similar to the results mentioned by Gibb and Scott (1985), differences were also found among the firms in this study in different degrees in terms of the awareness of the implications of present ideas. Even though owner-managers are capable of anticipating the possible implications of their strategic actions for a reasonably longer time period, however, in many cases, their breadth of anticipation is limited in terms of time and area covered. Finally, the findings of the present study support the studies of Gibb and Scott (1985) and Mintzberg and Waters (1985) and indicate that although owner-managers are aware of relevant events in the environment, although they have strategic course of action to exploit the opportunity or to deal with the threats in it, and although they are aware of the implications of their strategic courses of action, such deliberations are reactive and seldom formalised. Although the preconceived notions of strategic planning support the idea that formal strategic planning practice heightens the owner-managers' ability to think strategically (Porter, 1980; Lyles et al., 1993), the owner-managers in this study, like in Gibb and Scott's study (1985), seemed to never use written plans to shape their future strategic orientation. They also normally do not put their future strategies courses of action in written formalised documents. They do not even perceive written plans as useful for small business firms. Some firms use written strategic plans fundamentally to fulfil the requirement of the external agencies supporting them. The future strategic orientation of the small firm is not affected by this externally made written plan. Table 1 below shows those major findings of the previous studies.

**Table 1. Major findings of previous studies**

<b>Author(s)</b>	<b>Findings</b>
Schwenk and Shrader (1993)	Strategic planning has a positive effect on the performance of small businesses
Orpen (1993)	Formal strategic planning enables organisation to better prepare for and to deal with the rapidly changing environments that most of them face.
Lyles et.al., (1993)	Small business owners adopt a more formal planning process, the breadth of strategic planning can most certainly influence the growth of the company
Gibb and Scott (1985)	The study of the data reported here that most owner- managers of small firms have ideas or portfolio of ideas of projected action to avail themselves of relevant opportunities and for dealing with the threats existed in the environment.
Mintzberg and Waters (1985)	They indicated that although owner-managers are aware of relevant events in the environment, although they have strategic course of action to exploit the opportunity or to deal with the threats in it, and although they are aware of the implications of their strategic courses of action, such deliberations are reactive and seldom formalised.

The purpose of this research was to explore how small enterprises practice strategic planning and to confirm if such practices relate to the preconceived notions of planning described in the literature. It was not designed to determine the cause-and-effect functions of various enterprise, owner-manager, and environment specific factors influencing the elements of strategic planning.

## Conclusion

Bamberger (1980) noted that there is a positive relationship between the existence of a more or less formal strategic planning system and the firms' growth. Watts and Orimsby (1990) pointed out the relationship between strategic planning and performance of small businesses, and that there is a tension between normative statements and the findings of empirical research. Increasing evidence has confirmed that strategic planning has a positive effect on the performance of small businesses. Therefore this study will contribute to the existing stock of knowledge in the literature of strategic planning in small business. Finally, based on the empirical findings, strategic planning contributed significantly to the relationship with the overall performance of small business under study.

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## Efectul planificării strategice în întreprinderile mici: o privire de ansamblu

### Rezumat

În ultimii ani s-a acordat o atenție deosebită problemelor legate de planificarea strategică. Chiar și practicanții și academicienii și-au continuat dezbaterile asupra meritelor planificării strategice. Literatura de specialitate ce pune în discuție problema planificării în cadrul micilor întreprinderi a crescut considerabil în ultimele decenii. Cu câteva excepții remarcabile, mulți specialiști au recomandat ca firmele mici să utilizeze planificarea strategică drept instrument esențial în îmbunătățirea performanțelor. Conform studiului efectuat de Gibb and Scott (1985), planificarea strategică reușește să influențeze semnificativ creșterea companiei și să ofere un cadru care să accentueze acest efect, putând contribui la menținerea dimensiunii actuale și a capacității firmei. Totuși, noțiuni preconcepționate cu privire la planificarea strategică susțin ideea că practicile de planificare strategică formală sporesc capacitatea managerilor-proprietari de a gândi strategic (Porter, 1980; Lyles et al., 1993). Prin urmare, studiul de față s-a axat asupra incidenței planificării strategice în întreprinderile mici. Datele provin din monografii, cărți și jurnale etc. Astfel, studiul de față va contribui la stocul de cunoștințe existente deja în literatura de specialitate asupra micilor întreprinderi. În fine, bazată pe date empirice, planificarea strategică a contribuit semnificativ la relația cu performanța de ansamblu a întreprinderilor mici analizate.