

The role of accounting information on business strategy formulation



Abstract

Although strategy development in large corporations has been well documented, the process of strategy deployment in Small and Medium Enterprises (SMEs) has not been extensively investigated by academic researchers. This study tries to provide new empirical evidence and the practical realities on the nature and practice of strategic planning in Greek companies. Its primary target is to examine the formulation of strategic planning in Greek SMEs and also the role of accounting information on the business strategy of SMEs in Greece.

The results of the research indicate a positive relationship between strategic planning implementation and accounting information received by accountants and used by SMEs and no relationship with other sources of advice such as government agencies or bank advisors. The importance that is given to sales, costs and profits signifies a business planning rather than a strategic planning orientation of Greek SMEs

Keywords: strategic planning, strategic activities, external advisors, accounting information

Introduction

Academic literature in strategic management of small and medium enterprises (SMEs) has been very limited. Although the nature of strategic planning processes has been shown to have an important effect on the performance of firms [1], the field of strategic planning in SMEs is still in the early stages of its development. Its adolescence, relative to other more established areas of business and management theory, is evidenced by <https://assignbuster.com/the-role-of-accounting-information-on-business-strategy-formulation/>

inconsistent and conflicting viewpoints [2] and only a few researchers have addressed the strategy-making processes of SMEs [3].

Limited research can also be observed on the usage of information from SMEs when strategically planning. Drury and Tayles [4] suggested that there is a need for more research that explores in much greater depth how managers use financial and non financial information. Recent research has shown that most SMEs are unable to utilize accounting and financial information. Owner-managers of SMEs may be expected to be fully aware of the product/service markets that their business are based in, but they may not be trained or proficient in accounting or financial management [5]. The aim of this study is to add to the developing literature on strategic planning implementation in SMEs in Greece. Specifically the objectives of the study are to explore the extent of strategic planning of SMEs, to investigate the activities that owner/managers plan in advance and to identify internal and external advisors that help SMEs to strategically plan.

Strategic Management and Strategic Planning

Strategy is a term that is widely used by senior and middle managers. But the term seems to have multiple of meanings. There is no commonly accepted and universal meaning of strategy [6]. Due to this fact the definition of strategy has been the subject of extensive research since the 1960s. It has been described as the process of determining the long-term goals and objectives of an organization, by adopting a specific course of action and by allocating sufficient resources [7].

This traditional and rational definition was later challenged by Mintzberg contention that strategy was more a pattern of action resulting from intended or unintended strategies. Mintzberg claimed that strategy could be something more than an explicit plan of action. His five strategy dimensions that he recognized were: “ strategy as plan”, “ strategy as pattern”, “ strategy as ploy”, “ strategy as perspective” and “ strategy as position”. These have been the basis for opening up the definition of strategy to a wider context of use [8].

Strategic planning concentrates on the setting of long-term organizational objectives, and the implementation of plans designed to achieve them. A suitable definition of strategic planning can be “ the devising and formulation of organizational level plans which set the broad and flexible objectives, strategies and policies of a business, driving the organization towards its vision of the future” [2]. Porter [9] noted that further work was needed to enable business to understand strategic planning by arguing that “ while there has been considerable progress in developing frameworks that explain differing competitive success, at any given point in time, our understanding of the dynamic process by which firms perceive and ultimately attain superior market positions is far less developed.”

The SMEs literature

Small and medium size enterprises (SMEs) play a crucial part for the economic growth of a country. SMEs contribute to outputs and employment and also affect the competitive ability of the large organizations [10]. SMEs can influence the competitiveness of large organizations by providing high quality inputs [11]. The importance of small and medium size businesses for <https://assignbuster.com/the-role-of-accounting-information-on-business-strategy-formulation/>

future economic development has been reflected in a number of policy papers which have focused attention on the role of entrepreneurship, owner-managers and the small firm sector [12].

3. 1 The SMEs sector in Greece

The contribution of the SMEs in the development, the employment and social coherence in Greece is substantial. In Greece, enterprises that have fewer than 50 employees form about 99. 5 per cent of the total number of enterprises and employ the 74 per cent of the work force of the private sector. It should also be noted that Greek SMEs provide 70% of the new employment, reinforce the regional development and financial balance of the regions and make part of a cohesive financial and social link in Greek society. The role of SMEs in the national economy and employment is vital, since the main business model in Greece is and it will remain the micro enterprise which employs less than 10 persons.

According to the criteria set by the European Commission, Greece has more than 733. 000 qualified SMEs, from which more than half, 394. 000 or the 53. 7 per cent does not employ any salaried workers and they employ 11 people on average. [13]

3. 2 Strategy in SMEs

Academic research has been conducted on several broad fronts in order to define strategy in SMEs, from planning processes, to the individual personality of the owner-manager and the growth of a wide range of available advisory services providing information on strategic choice. Perry et al [14] argued that strategy should be examined in the everyday

operating environment of the small firm. The formulation of strategy in SMEs has been the theme of many academic researchers. Some studies [15] examined the link between planning and performance in SMEs, while others [16] explored the difficulty of defining planning and strategic planning, and its dimensions, such as planning formality and performance in the small firm context.

The definition of strategy in SMEs is often perceived as person centred rather than process driven. The performance of small firms is linked with the leadership style of the owner. Nahavandi and Malekzedah [17] in 1993 argued that the style and personality of the manager is central to the strategy definition process.

Noble [18] after a series of exploratory interviews with the managing directors of SMEs, suggests that strategic deployment often fails as a result of SMEs' inability to forecast and overcome implementation barriers. O'Regan and Ghobadian [3] indicated a number of general barriers relating to the constraint of strategic planning implementation such as communication was inadequate, implementation took longer than expected, a shortfall in employee skills, objectives of strategy were not clearly understood by the staff, ineffective co-ordination of implementation, crises distracted attention from implementation, unexpected external problems arose and external factors impacted on implementation.

Research Design

This research applies the quantitative method to examine the implementation of strategic planning in SMEs in Greece. The central aim of

the research is to provide empirical evidence on how SMEs use strategic planning and what kind of advice they use to aid them.

Data were gathered by means of a survey questionnaire, all questions used a five-point Likert type scale; with a response of 1 indicating that an item received 'not agree' and 5 indicating an item received 'agree'.

The sample consists of small and medium enterprises that are located in the Greek capital Athens and belong to the service and manufacturing sector. Questionnaires were distributed to a whole sample of 546 owner managers of small and medium sized enterprises. A postal questionnaire was used instead of sending e-mails, in order and to protect the participants' anonymity and because some owner-managers were not familiar with the use of e-mails. From a total of 546 questionnaires mailed, 178 were returned, representing a 32 per cent response rate. Out of these 19 were found to have missing data and were deemed void. Therefore, data was collected from a total of 159 sets, representing a satisfactory response rate of approximately 29 per cent.

The questionnaire consisted of 4 sections, covering the following aspects:

Strategic planning implementation in SMEs

Strategic planning activities

Advisors that affect strategic planning

Accounting information used for strategic planning

Prior to distributing the questionnaire to the sample, a pilot study was conducted to discover any errors, ambiguities, inadequate answers, or highlight any confusing questions. Enterprises that participated in the pilot study were excluded from the main study.

Research Questions of the study

Question 1: Is there a significant relationship between Strategic Planning Implementation and the Total Strategic Planning Activities?

Question 2: Is there a significant relationship between Strategic Planning Implementation and the use of internal advisors?

Question 3: Is there a significant relationship between Strategic Planning Implementation and the use of external advisors?

Question 4: Is there a significant relationship between Strategic Planning Implementation and the use of accounting information?

Findings and Discussion

The findings of the present research are contradictory in certain respects. Despite a sizeable majority of respondents indicating that their companies undertake strategic planning, there is limited evidence of practical strategic planning in the sense of setting long-term business objectives. Research by Stonehouse and Pemberton [2] that was conducted for British SMEs had the similar results. In their research the 92 per cent of the companies indicated that they undertake strategic planning, either highly structured or of a general nature. They have found that most of these organizations were

concentrated on short-term sales, cost and profit targets rather than longer-term goals.

6. 1 Strategic planning implementation and strategic planning activities

Question 1 examined the relationship between strategic planning implementation and strategic planning activities. In order to answer the above question relating with the strategic planning implementation and the strategic planning objectives, correlation tests and T-tests were employed.

First the researchers with the use of factor analysis divided the strategic planning activities (objectives) into three categories. In the first category were sales, costs, profits, production/service procedure and customer service. In the second category were staff training, staff appraisal, staff recruitment and advertising and in the third category were the market share, the expansion of the size of the enterprise and the mission of the company. With the use of Pearson's and Spearman's correlation it was found that strong relationship between strategic planning implementation and strategic activities exists only for sale targets, cost targets, profit targets, production outcome targets and for the improvement of quality service. Greek owner managers of SMEs in their great majority when strategically planning, neglect activities such as staff appraisal, training and recruitment, advertising, mission fulfillment and market share targets.

The above results are in line with the findings reported by Stonehouse and Pemberton [2]. They found that contradictions between strategic planning implementation and strategic planning activities could be explained in terms

of a difference in perception between managers and academics on the nature of strategic planning. Furthermore, most Greek companies refer to strategic planning, but in practice they are more concerned with short-term objectives and what would be regarded by academic researchers as business planning.

6. 2 Strategic planning and internal advice and assistance

Question 2 examined the relationship between strategic planning implementation and human resources capital and internal advisors employed for strategic planning in Greek SMEs. Pearson Correlation and Spearman Correlation tests were used in order the research question to be answered.

The study on Greek SMEs has not found a significant relationship between strategic planning and human resources capital employed. Most owner managers surveyed did not share the belief that the personnel have the skills or the experience to assist in the deployment of strategic plans. This result can be confirmed by the findings of research question 1, that owner managers do not have long-term plans for their staff recruitment, training and appraisal

The above results are in contradiction with a research on Spanish SMEs by Aragon-Sanchez and Sanchez-Marin [19] who revealed that owner managers focus their attention on human resources as a key element that allows them to achieve a sustainable advantage. They noted that the competitiveness of SMEs is based on internal elements supported by resources such as personnel and their skills.

But other studies had similar results with what was found about the Greek SMEs. O'Regan and Ghobadian [3] identified a number of general barriers relating to the constraint of strategic planning implementation. Their pilot study confirmed eight main barriers with the shortfall in employee skills being one of them. The research by Hall and Young [20] on 182 failed small enterprises indicated that the most important cause for the failure of these companies were shortages in working capital (51.4 per cent).

6.3 The necessity of external advice

Question 3 examines the relationship between strategic planning implementation and the use of external advice by the owner managers. Pearson Correlation and Spearman Correlation tests were used for the analysis of this question.

The results of this research suggest that SMEs in Greece receive valuable external advice in order to plan strategically mainly from accountants. Government agencies and bank advisors are not contributing as beneficial advisors for the owner managers and only a minority of the respondents state that they receive useful advices for strategic planning. Pearson's correlation test has shown that there is a significant relationship between strategic planning implementation and the use of accountants, while there is not a significant relationship between other external advisors (government agencies and bank advisors) and strategic planning implementation.

These results are in line with previous studies which have investigated the association of strategy formulation and external advice. Berry, Sweeting and Goto [21] conducted a research on SMEs located in Manchester and found

that most of the business advisers had limited use by the owner managers. Only accountants had a key role in the processes of the SMEs but mostly on statutory work. They have also identified that accountants made a significant effort to shift into the value-adding areas of the SMEs; as it was perceived by the owner managers in the sample.

Alattar [22] found that the use of an accountant to be responsible for the accounting function in the enterprise resulted in a provision of more information which was useful for maintaining better planning and control. Deakins et al [12] study indicates that an important task for accountants is to act as a consultant to the owner managers and that this involves supplying advice on internal planning, decision-making and control. Gooderham et al [23] stated that in many countries, smaller business accountants play an important role as business advisers in addition to providing accounting services.

6. 4 Accounting Information used as tools for strategic planning implementation

Question 4 examined the relationship between strategic planning implementation and accounting information used as a tool by owner managers for strategic planning in SMEs using Pearson Correlation and Spearman Correlation.

This research has shown that owner managers of Greek SMEs take under serious consideration the accounting information they receive from external advice and they apply them as tools when they implement their strategic plans. This finding was consistent with what should have been expected as

accounting information have been identified as crucial elements of strategic planning

Stonehouse and Pemberton [2] noted that there is little evidence of usage of the “ tools” of strategic analysis with the most common tool relating to internal financial analysis. Collis and Jarvis [5] identified the three main resources of information used in the management of small companies; management accounts; cash flow information and bank statements. They have found that most SMEs use accounting information such as profit and loss account, balance sheet, cash flow statement and forecast and ratio analysis in order to monitor the profitability and for planning and controlling. Hall and Young’s research [20] showed that poor use of accounting information was one of the main reasons that led into failure the 38 per cent of the 21 small enterprises surveyed. Randal and Horsman [24] found that the lack and misuse of accounting information contributed to small enterprise failure. Holmes and Nicholls [25] suggested that the quality of accounting information utilised within small enterprises had a positive relationship with their performance.

Conclusion

This study has tried to examine from the respondents’ perspective the extent to which Greek SMEs use strategic planning and the influence of accounting information in the design and deployment of these plans. This paper has tried to identify relationships and differences, among the SMEs surveyed, between strategic planning implementation and (1) strategic planning activities of the firm; (2) the human resource capital; (3) external advice from, government agencies, banks and accountants; (4) accounting

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information such as profit and loss accounts, cost accounts, sales accounts, accounting ratios from the balance sheet and sales forecasts.

The results of the analysis have shown that owner managers when strategically plan emphasise on activities such as profits, sales, costs, production outcomes and customer service. The importance that is given to short-term financial objectives (sales, costs, profits) confirms a predisposition towards business planning rather than strategic planning. Other business objectives, that are closer related to strategic planning such as the company's mission, human resource training, market share targets and enterprise size targets are completely left out from strategic planning by the majority of the owner managers.

The use of accounting information and advice received from accountants were, according to the owner managers, the most significant factors that facilitated them during the design and implementation of their strategic plans. In the contrary, it was found that the human resources of the SMEs and external advice from government agencies and banks did not have an important role in strategic planning implementation.