A REVIEW OF SMEs STRATEGIC PLANNING FOR GROWTH AND SUSTAINABILITY IN KENYA: ISSUES AND CHALLENGES

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ABSTRACT

As the world economy continues to move towards increased integration, some of the greatest opportunities for Small-to-Medium Sized Enterprises (SMEs) will derive from their ability to participate in the global marketplace while sustainably increasing their competitiveness. It is generally accepted that SMEs are becoming increasingly important in terms of employment, wealth creation, and the development of innovation. However, there are considerable doubts about the quality of strategic planning and management in this very crucial economic development sector with policy-makers suggesting that there are particular weaknesses in innovation, a lack of financial acumen, marketing, entrepreneurial flair, practical planning and management knowledge, and human resource management. As a result, many firms do not reach their full potential and fail to grow. The present paper will therefore seek to employ exploratory desktop review to determine the SME Business development in Kenya with particular reference to Strategic Planning for SMEs Growth and Sustainability. The paper will in digging into the issue of Strategic Planning for SMEs, look into aspects such as SME Business Control Structure, Significance and Benefits of Strategic Planning for SMEs and show cause why SMEs fail to carry out Strategic Planning.

Key Words: *SMEs, Global Marketplace, Competitiveness, Strategic Planning, Business Control, and Entrepreneurship*

Introduction

As the world economy continues to move towards increased integration, some of the greatest opportunities for Small-to-Medium Sized Enterprises (SMEs) will derive from their ability to participate in the global marketplace while sustainably increasing their competitiveness. It is generally accepted that SMEs are becoming increasingly important in terms of employment, wealth creation, and the development of innovation. However, there are considerable doubts about the quality of strategic planning and management in this very crucial economic development sector with policy-makers suggesting that there are particular weaknesses in innovation, a lack of financial acumen, marketing, entrepreneurial flair, practical planning and management knowledge, and human resource management. As a result, many firms do not reach their full potential and fail to grow.

As in any country, SMEs do contribute to economic growth. However, there are challenges and opportunities that they face. This article reviews SMEs Strategic Planning issues and challenges affecting SMEs growth and sustainability in Kenya. Main areas to be included in the discussion are SMEs in the Agri-business sector, SMEs within the Manufacturing and Jua Kali sector, SMEs in the Information, Communication and Technology Sector and SMEs in the Transport Sector.

It is clear that as the world economy continues to move toward increased integration because of advances in communications technology, growth in developing countries, and reductions in trade barriers, some of the greatest opportunities for small businesses will derive from their ability to participate in the global marketplace (Alvarez, 1999). Within the developed and developing countries of the world, it is now generally accepted by policy-makers at local, regional and national level, that small to- medium sized enterprises (SMEs) are becoming increasingly important in terms of employment, wealth creation and the development of innovation (Nieman, Hough and Nieuwenhuizen, 2003; Vesper, Boden, and Roman in Carland, Carland and Ciptono, 1999).

On the other hand, there are considerable doubts about the quality of management in this sector, with policy-makers suggesting that there are particular weaknesses in innovation, lack of financial acumen, marketing, entrepreneurial flair, practical knowledge, values and psychological disposition of the entrepreneurs, and human resource management (Hodgetts and Kuratko, 1995). As a result, many firms do not reach their full potential and fail to grow, resulting in lost jobs and wealth for their region in which they are based.

A closer look at the organizational life cycle theory models reveals that there are between three to five stages that most organizations will go through. The Churchill and Lewis model (Timmons, 1990) suggests that four critical stages exist in the life of a SME where the stages are determined by the length of time the firm has been operative. Churchill and Lewis (Timmons, 1990) estimate the duration of each stage to be as follows: Stage 1 is the start-up phase and is 0-3 years in duration; Stage 2 is the growth phase and is 4-6 years in duration; Stage 3 is the maturity phase and is 6-9 years in duration; and Stage 4 being the stability phase is approximately 10+ years in duration. Coupled to each of these stages is a different set of business characteristics, challenges, managerial abilities and entrepreneurial needs that small businesses will have to face (Kuratko and Hodgetts, 1995).

Storey (2000) noted that politicians around the globe have, over the past decade, emphasized the importance of small enterprises as mechanisms for job creation, innovation, and the long-term growth and development of economies. However, the media coverage in the European economy on business, in general, contains over 95% of column space for large businesses even though, in the European economy 95% of all firms are in fact small and provide more than half of all jobs in Europe, yet little media coverage is afforded to these entities. To this end, the Kenya Government has not been left behind in the clamor for a more structure, vibrant, resource-rich and self-endearing SME sector. The Kenya Government is committed to seeing a more vibrant and fast growing SME sector, that is increasingly self-sustaining and able to create opportunities for social and economic growth. This commitment is contained in the Economic Pillar of the Kenya Vision 2030.

The Kenya Vision 2030 is the new country's development blueprint covering the period 2008 to 2030 (NESC, 2009). It aims at making Kenya a newly industrializing, middle income country providing high quality life for all its citizens by the year 2030 (GoK, 2009). The Vision has been developed through an all-inclusive stakeholder consultative process, involving Kenyans from all parts of the country. The vision is based on three pillars namely: the economic pillar, the social pillar and the political pillar (NESC, 2009). This vision's programme plan comes after the successful implementation of the **Economic Recovery Strategy for Wealth and Employment Creation**.

The economic pillar aims at providing prosperity to all Kenyans through an economic development programme aimed at achieving an average Gross Domestic Product (GDP) growth rate of 10 % per annum the next 25 years (GoK, 2009). The social pillar seeks to build a just and cohesive society with social equity. The political pillar aims at realizing a democratic political system founded on issue-based politics that respects the rule of law, and protects the rights and freedoms of every individual in the Kenyan society (NESC, 2009).

While reading the Budget Speech for the Fiscal Year 2010/2011, the then Minister for Finance, Hon. Uhuru Kenyatta proposed the establishment of a Sh3.8 billion Revolving Fund whose objective was to encourage the growth of micro and small enterprises (MSEs) to enable this important sub-sector to support industrialization, employment creation and economic growth. More importantly, the creation of the Fund was also aimed at enlisting the partnership of commercial banks to lower lending rates and cost of borrowing in general. Consequently, the Fund for Inclusion of the Informal Sector (FIIS), also known as the SME Fund, was launched on March 14, 2011. The funds were disbursed to the participating banks on June 24, 2011. The three banks, selected through a competitive tender process (Equity Bank, Cooperative Bank of Kenya and K-Rep Bank) signed agreements committing to lend the funds in line with the objectives.

The Government recognizes the critical role that small and micro enterprises play in the development agenda. The Government also acknowledges that a significant barrier to the growth of MSEs, most of which are owned by the youth, is access to affordable credit and lack of basic minimum requirements needed by commercial banks in order to lend to the SMEs. Financial exclusion arising from lack of credit access and cost challenges eclipses the potential in SMEs to grow their businesses. The SME Fund, therefore, aimed to meet the twin objective of addressing youth unemployment and encouraging growth of micro and small enterprises (MSEs) as key drivers of economic growth and development.

Despite this evident commitment by the Kenya Government to see a strong and enduring SME sector, still the survival rates of majority SMEs is in the brink. Statistics indicate that a high percentage of SMEs fail within the first two years of start-up (LeBrasseur, Zanibbi and Zinger, 2003; Littunen, Storhammar and Nenonen, 1998; Hall, 1995; Kuratko and Hodgetts, 1995). Storey (in Burns, 2001) suggests that younger firms are more likely to fail than older ones and states that 50 percent of firms cease trading within the first three years. Rwigema and Venter (2004: 68) state that "in most countries, the rate of business failure far exceeds that of success." Given the high failure rate of SMEs, internationally and locally, it is essential that the reasons for failure be investigated and a framework be developed to reduce the failure rate among start-ups.

It is therefore paramount to note that better-governed companies have less management problems (Wanjohi & Obuobi, 2010). They act on and recover from shocks more quickly, so they achieve faster and more reliable growth. Still, most SME owners across the world consider corporate governance relevant only to large companies and not to their very own business situations. It is more prevalent in Africa, where the concept is still unfamiliar even to relatively large SMEs. All businesses, regardless of size or nature, have systems of management and governance. How much of the business owners implement them as they influenced by culture, education, type of business, business environment, and other similar factors. In the end, SME owners agree on their need for systems because they need a method to the management of their businesses, if they are to achieve their goals.

Review of Strategic Planning for SMEs Growth and Sustainability

According to Wanjohi & Obuobi, (2010), and in practice, therefore, what constitutes a good SME Management was summarized in the following diagram outlining four pillars of strategic planning for SMEs:

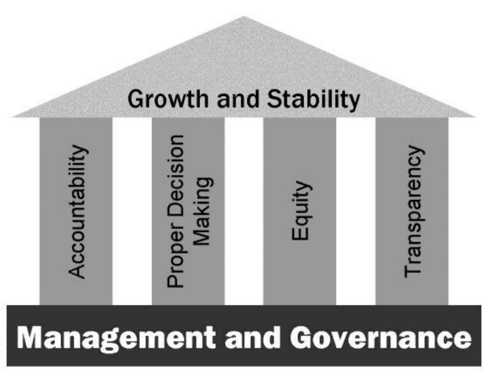

Figure 1: Foundations of Business Management and Governance

Source: (Wanjohi & Obuobi, 2010)

Wanjohi & Obuobi (2010) also observe that good management and governance systems need to abide by the above four basic standards: business control structure, budgeting and cash management, management accounts, and annual audit. They are widely viewed as necessary to establish a reliable organization. Businesses can customise these pillars according to their needs, without compromising on their essence as best practices. Their respective objectives are:

1. Business Control Structure: Ensure accountability to all stakeholders and manage relationships with shareholders, the board, management, staff, and other parties.
2. Budgeting and Cash Management: Instill the discipline of planning, for both profitability and working capital adequacy.
3. Management Accounts: Keep a close eye on actual income and expenditure against the budget.
4. Annual Audit: Assure anybody of the reliability of management and financial records and provide an outsider's expert assessment of a company's internal control system.

SME Business Control Structure

The main purpose of a control structure is to allocate responsibilities and functions to various company units and positions. A good structure brings order to an organization. It provides a guide on how one unit should relate to another, in order to establish efficiency in operations and effectiveness in decision making. It sets out a chain of command for all company employees. SMEs may not need complicated structures such as those adopted by big corporations, but they should establish one that fits their operations and which they can enhance as they grow. An effective organizational structure considers the needs and contributions of the following:

Shareholders

Business owners or shareholders are the main interested parties in the control structure because they usually start the business themselves and are the biggest investors. The entire structure is designed to be accountable to them because they have the right of control of the business and its returns and are ultimately responsible for everything within the company. Shareholders set up businesses to serve their interests, so every unit in the structure, including the board and management, have to work towards this objective.

The main function of shareholders in a large-business structure is to appoint a board. In SMEs, however, they are involved in more roles than that. In most cases, they also manage their businesses, which can be an asset because they have a special commitment to the success of the business, as owners. In addition, many of them are actually very skilled in management.

Even under SME conditions, though, the respective roles of shareholders and management have to be defined. Good shareholders should be able to review the management's performance objectively, even if they may be a part of it. They should be courageous enough to ask themselves if they are the best managers for their business. If they are not, they should give up that role. They should also be professional enough and hold annual general meetings and demand audited accounts to be given in a timely manner, which they should review as a measure of their business success.

Company Board

This SME Strategic Planning guide refers to a board as a formal group that is a permanent part of the organizational structure. It meets regularly and has clear responsibilities. Most SMEs associate boards with big corporations mainly because they view themselves as too small for such bureaucracies.

SMEs need to appreciate boards for their roles and contributions to the business. A board's composition should initially not be a major concern to SMEs as long as it functions effectively. Should the business require external expert advice, the board can expand to accommodate such individuals. Strength of a team of external experts that usually comprise the Board is that they are less involved in the managing of the business and are not directly affected by decisions, so they have the potential of being more objective. Otherwise, the owners and senior management can serve effectively on the board, with external auditors as advisers on financial and internal control matters.

The board should have regular and scheduled board meetings. These meetings have to be managed professionally, so they can be taken seriously and are productive. Every member should have an opportunity to contribute, with the minutes of the meeting recorded, filed, and ready for review in subsequent meetings. It is recommended that there should be at least two board meetings a year. The board should also contribute to and evaluate the company's long-term plans as presented by the management. It should also set targets for the management and hold it accountable against them. Other functions of the board are to:

1. Review and approve management accounts, budgets, and audited accounts.
2. Appoint senior managers on merit and give them real responsibilities.
3. Recommend competent auditors capable of giving appropriate advice and preparing expert, accurate accounts to shareholders.
4. Approve other major decisions (for example, loan applications, expansions, etc) accordingly, as they occur.
5. Operate in good faith for the company and its shareholders.

Some businesses can benefit much from the expertise of external advisers, but their owners do not use them because of concerns for their company's privacy. Of course, they forget that even company employees can be considered outsiders. They are also in a position to access and release company information to other outsiders'. SMEs should be encouraged to set up a board in order to deal with the company's direction, in a more organized and professional manner.

Management

The management is responsible for running a company's daily operations. Together with the board, it is also in charge of developing a long-term business plan. As part of its daily duties, the management should ensure that:

1. The company complies with all relevant rules and regulations, including appropriate licenses, tax authorities, etc.
2. The board is up-to-date with all the necessary information about the company.
3. The company manages its risks, both internal and external.
4. It uses its knowledge and experience to develop and communicate appropriate recommendations to the board.
5. Staff members are treated equitably.
6. It employs its expertise for the company's good.

According to Wanjohi & Obuobi (2010), the main goal of management is to maximize the shareholders' wealth. The success of this goal normally has a strong correlation with the individual goals of management team members. Because the management plays an important role in the business, shareholders and the board should ensure that they have the right team for the job. Appointments should be based on merit and positions must be matched with talent. Shareholders and the board should view management as an investment and should make an effort to pay them according to industry standards. Retaining good people should be one of their most important objectives. Employees should also be given real and clear responsibilities because it is important for their job satisfaction and accountability. In ethnically diverse countries like the ones in East Africa, businesses should make sure that they have a fair mix of staff members from different cultural backgrounds. This sends a message, both internally and externally, that the business is a professionally run organization.

Other Parties

There are other parties involved in the business control structure, which are not as strongly linked as the shareholders, board, and management but are very important just the same. Their roles in the business do not require the close involvement of the shareholders or the board. At different times, though, any of these entities may influence the business, just like the others do:

1. The company secretary is responsible for the efficient administration of a company, especially when it comes to the business's compliance with statutory and regulatory requirements. An example of these requirements is the filing of annual returns, resolutions, and other legal and required information. SMEs may outsource the function of a company secretary to a third party, while they are still unable to afford one on a full-time basis.

2. Customers keep the business alive. No matter what a business's market position is, it should always maintain its focus on satisfying the customer.
3. Creditors include lenders and suppliers. They are very important to the business's growth and cash supply. The management should ensure that the company pays its dues in a timely manner and that a good relationship is maintained with them at all times.
4. Regulators make sure that businesses operate within the law and meet other required standards. Customers like to deal with credible businesses.
5. Communities play host to businesses, so the latter have a responsibility to them. Communities should be made to feel that a business is part of them and has their interest in mind. Developmental benefits and environmental protection are very important to communities.

Financial Management

Efficient financial management is a core element of good management and governance. Without accurate accounts, strong internal controls, and financial planning, it is almost impossible for business owners and managers to carry out their responsibilities effectively and efficiently. Good financial management is made up of budgeting and cash management, management accounts, and audited accounts, which are discussed in the following sections:

Budget and Cash Management

A budget projects a business's income and expenditure over a defined period. It assists owners and managers to understand how cash moves in and out over time. On the other hand, cash management is an activity that has always been a challenge to businesses around the world. Growing businesses have many cash needs, which must all be prioritized and accounted for.

Profitability does not necessarily mean that the business has available cash. In most cases, at the growth stage, available cash is spent on additional working capital and assets to sustain the development. Business owners and managers then have to manage situations without putting the company through cash strains and, sometimes, failure. Expansion should be run in a way that still allows the business to pay all its immediate obligations, especially to suppliers and creditors.

Entrepreneurs are naturally very ambitious and like to take advantage of every available opportunity, but it is wise to have proper budgets that project money inflows and outflows, prior to making new investments.

It is advisable for SMEs to prepare annual budgets. Ideally, each budget should be ready before the intended year starts to ensure that businesses make appropriate preparations early. The budget lays out all the planned expenditure against the expected income. Business plans are then made from a more informed position.

SMEs can also make early preparations to borrow, if they foresee cash shortages. Budgeting is a good way of setting performance targets because it takes into consideration the resources required to achieve those targets.

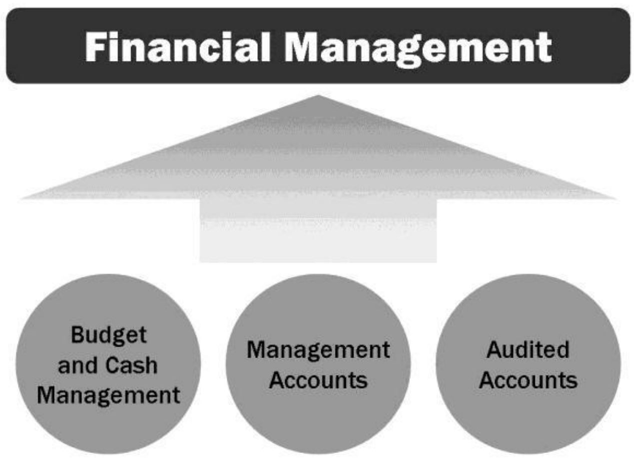

Figure 2: Elements of Financial Management

Source: (Wanjohi & Obuobi, 2010)

Management Accounts

Management accounts are necessary to provide updates of the company's performance. It is advisable for SMEs to produce them after every three months (quarterly). The accounts should include the three main financial statements: profit and loss, balance sheet, and cash flow. They give a clear picture of the business's financial performance and asset position. Management accounts also assist in internal decision-making processes. The success levels of targets and budgets are measured through management accounts. After each quarterly accounts report, management can decide on whether to maintain the same trend or to adjust in order to accomplish set targets. The business owners and managers also develop a better understanding of the company financials through management accounts because of their regularity and comprehensiveness. With them, businesses are viewed as more professional by outsiders, especially banks and similar institutions.

Audited Accounts

Auditors carry out a very important role in business management and governance. Their overall duty is to serve the shareholders by investigating company processes and systems. They provide an independent check of information supplied by the board and management to shareholders. They also act as advisers to both board and management on internal processes and tax policies. The auditors' concentration and expertise is in financial analysis. They are required to abide by acceptable accounting principles and standards.

Due to the sensitivity of the auditor's role, which involves inspection of management records and systems, their appointment should be carried out as professionally as possible. They should also be given a free hand to carry out their work. Professional standards require auditors to act independently and not to let future business prospects with their clients affect their work.

Significance and Benefits of Strategic Planning for SMEs

Continuity and Succession

Most businesses, especially SMEs in the East African region, are still owned and run by first-generation owners. There is a general lack of experience in business continuity from one generation to the next. For continuity to be successful, a business should have systems that are not overly dependent on one person. Good governance systems reduce the importance of individuality and emphasize team and system-based operations. Through the chain of command, the governance structure anticipates change of management in every position. Business owners should also learn the art of easing out of a business, especially as they grow older. They can reduce their role in the day-to-day running of the business and entrust that duty to one of the managers. Letting go of a business by its owners, especially if they started it, is rarely an easy process. However, it is inevitable and the owners have to gain courage to do it in a timely manner.

Appointment of a successor is also a normally challenging task for owners; they find it hard to identify an individual with the same qualities as theirs. They also tend to personalize the selection, which may not be a good approach. One way of making the search process objective and more professional is to involve other individuals or a recruitment agency. Where possible, procedures should be documented to make it easier to transfer them to different individuals.

Growth and Stability

A key requirement for organizational growth is an effective structure to support it. The need for qualified employees and specialized departments increases with business development. SME owners should start building appropriate structures and systems early enough to ensure sustainable advances.

Proper management and governance systems establish defined organizational structures, which are favorable for growth. Managers in this type of system are given greater decision making powers that make operations more efficient. Expansions also become realistic because the structures allow departments and branches to be held accountable effectively. One of the key challenges of growth is tracking the increased operations with accuracy.

As the business expands, the business owner's ability to supervise it personally and effectively is reduced. However, through management and governance systems, controls are simplified, which make it easier for owners to track business activities with little involvement.

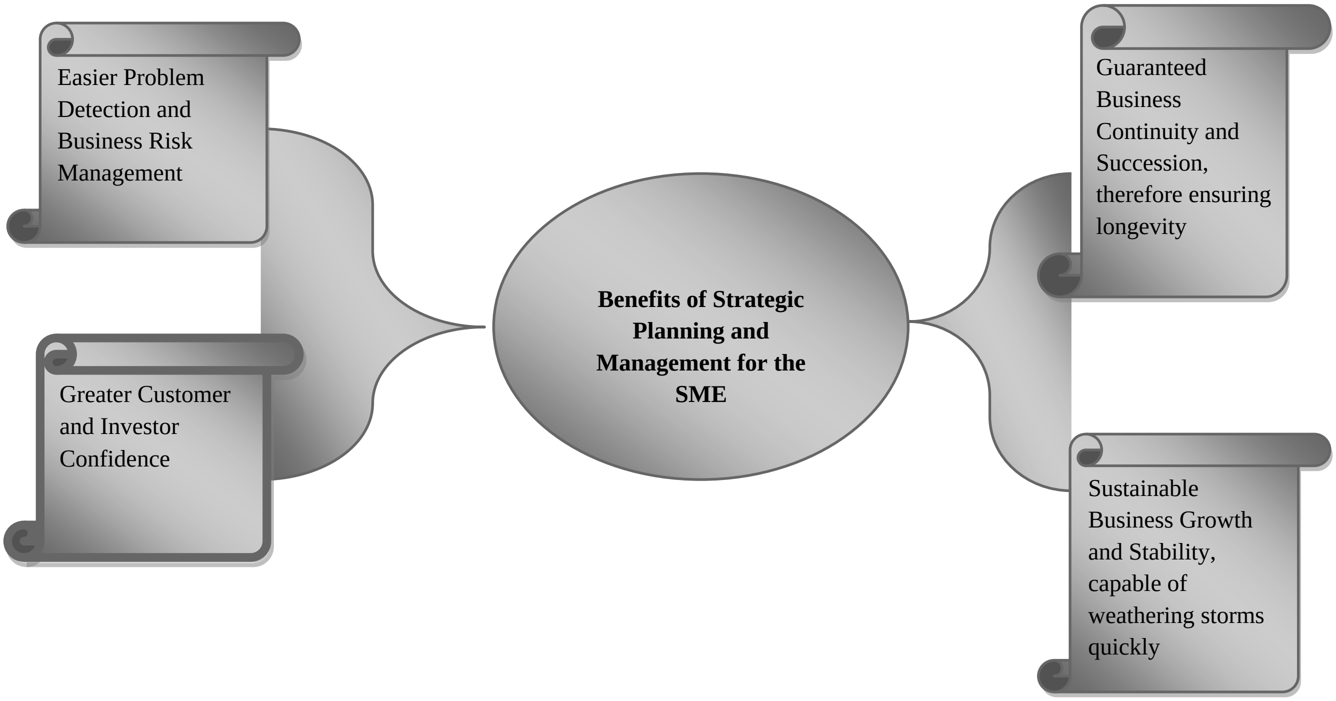

Figure 3: Benefits of Strategic Planning and Management for the SMEs

Source: Author

Easier Problem Detection and Risk Management

Risk management is a continual process in any organization. Reducing risk and improving response time to problems are some of the main qualities of a good management and governance system. Different accountability levels improve discipline in the entire command chain because they act as checks and balances for each other. Holding SME owners accountable can be challenging. It is very common for them to view and treat the business assets as their personal belongings.

All business assets are important for the company's continuity and growth, so any movement should be managed professionally and not at the owners' wishes. Cash movement can be especially very sensitive. Business owners should ensure that any funds borrowed or lent to the business should be recorded and treated appropriately.

In addition, funds that are drawn out of the company in the form of salaries or dividends should be done in a structured manner, so they do not hurt the business. The process is made easier by a proper financial reporting system and employment contracts. Records of every asset movement need to be captured, so it is clear how they are utilized and what they result to.

Greater Customer and Investor Confidence

Investors, customers, and creditors generally like dealing with businesses that have some openness and structure to them. Investors can be very particular with governance systems because they prefer to invest in the form of equity and become shareholders in the business. They normally insist on a defined governance system that provides them a chance to contribute and influence decision making. This also allows them access to necessary information. For fast-growing SMEs in East Africa, it is becoming popular to raise funds through equity. They are increasingly inviting new partners and investment funds to take up shares in their companies. It is then advisable to set up proper management and governance systems in anticipation of future fund-raising.

Why SMEs Fail to Carry Out Strategic Planning in Kenya

Researchers have given several reasons explaining some of the key determinants for failure by SMEs to carry out strategic planning and management of their enterprises. Some of these are outlined as follows:

Informality

Informality refers to the legal status of business owners' enterprise. In many cases, small and micro-enterprise operate without legal registration and mostly just referred to as "informal sector". According to Schiebold (2011), unregistered business has an implication on the business success in a number of ways. Due to its informal status or non-registered, they are unable to conduct business with official institutions or large formal businesses. Furthermore, they are excluded from exporting their products and therefore this could give them problem in raising the much needed working capital through official channels including banks and other Micro Finance Institution with whom and through which Government channels its funds for the SMEs.

Institutional Environment

Institutional environment refers to the official and unofficial rules and constraints that surround an entrepreneur and which shape the business operated (Schiebold, 2011). This institution consists of both written and formal constraints where the former may relate to legal matter while the informal constraints are being associated with norms, conventions and self-imposed codes of conduct (Shirley, 2008).

Entrepreneurial Characteristics

This item refers specifically to the characteristics of an entrepreneur and their implications to the business success. An entrepreneur is defined as an individual who develops and owns his own enterprise, risk taker, innovative, motivated, persistent and creative in converting a situation into opportunity. Successful entrepreneurs should have a unique set of personal characteristics, including: inspiration, creativity, direct action, courage and fortitude as these characteristics are fundamental to the process of innovation (Martin and Osberg, 2007). They should also have a certain set of capacities, mindset, (Schiebold, 2011), cognitive ability, motivation, competitive attitude (De Mel, Mckenzie and Woodruff, 2010). Entrepreneurial characteristics have a significant indicator in determining the success of micro-entrepreneurs. Cognitive ability can be influenced by the level of education. It is argued that entrepreneurs with an elementary school education tend to be less receptive to new technologies compared those who have a college education (Ghani, 1995). This situation is difficult to apply new technology and improve productivity.

Socio-cultural environment

This item refers to rules, shared values, beliefs, norms and code of conduct that is culturally rooted. The difficulty in changing these values and its significant impact on the socio-cultural environment can influence the level of success of entrepreneurs (Schiebold, 2011). In Malaysian context, it has been debated how Malay culture which is translated under the concept of Adat is very much intertwined with Islam, the official religion of Malaysia (Wazir Jahan, 1992). Study by Wan Nurhasniah (2011) on the concept of Budi and Muhammad (2009) have shown how Malay traditional culture, belief and practices of Islamic cultures were practiced by Malay women businessperson in Kelantan, Malaysia. This item is used to examine whether or not these values are adapted in the respondent’s business activities and its influence on the business growth.

Financing

Financing mechanism is important for investment and stimulating business productivity which is the main objectives for any businesses. This item is used to examine the challenges faced by SMEs in getting access to micro-credit financing schemes and the reason they avoid these schemes. Various studies have documented the difficulties faced by micro entrepreneurs to get financial assistance from local micro-credit schemes which include the lack of knowledge in loan application and high legal documentation required by the financial institutions (Nurbani et.al, 2010). This in return hampers the capability of the entrepreneur to access high caliber human resource and technical resources necessary for developing the SME into a more formal business organization.

Infrastructure

Infrastructure refers to both physical and non-physical. Physical infrastructure consists of roads, modern energy and non-physical item such as market structure. Location, according to Shaw (2002), which includes reliable power, communication, water and transport service will facilitate technological innovation and better access to inputs, markets and information. Furthermore, sound infrastructure will provide rural entrepreneurs to have access to urban markets.

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