

STRATEGY FORMATION AND FIRM PERFORMANCE OF EXPORTING SMALL AND MEDIUM ENTERPRISES (SMEs) IN THE PHILIPPINES

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Abstract: The growing awareness of the pivotal role of SMEs in global economic growth has challenged scholars and researchers on how to improve the performance of the SMEs. The SME sector is increasingly being recognized as a major source of employment, revenue generation, innovation, and technological advancement, in both developed and developing economies. (UNCTAD, 2000). While most researchers and writers recognize the role of the government's policy-support programs to the continued growth of the SMEs, they are one in asserting the crucial role of the managerial capabilities of the SMEs in driving their survival and growth. These managerial capabilities include, among other things, their ability to scan the environment, analyze the environmental opportunities and threats, and formulate strategies to shape their organizational performance, which are components of strategic management (Habito, 2017).

To address these gaps in the study of SME strategy formation, this paper presents a comprehensive discussion of the origins and dimensions of strategy, the process of strategy formation in SMEs, and its impact on firm performance. This paper attempts to contribute to the knowledge of the process of strategy formation of SMEs and its impact on firm performance, particularly within the context of an emerging economy like the Philippines.

Keywords: Strategy Formation, Firm Performance, SME

RESEARCH RATIONALE

In the Philippines, SMEs currently constitute 99% of all business establishments, employ 55% of the country's labor force and contribute to some 25% of value added. According to SME Development Council, the SMEs are a key component in the chain of institutions contributing to national economic growth. Most SMEs, however, face various challenges in the areas of human resource development, technology and R& D, access to financing, to name a few (SMEs in the Philippines, 2016).

The national government of the Philippines, including its local government units, recognizes the role of its coherent and strong policy-support for the growth of the local SMEs. The government's enactment of the Magna Carta for SMEs is a positive step toward this direction (Lawphil, 2013). However, it sees the individual performance of each small business enterprise as a pivotal determinant for the growth of the SME sector and for economic development in general. It is for this reason that studies and actual programs had been undertaken by the government to increase the capacity of local SMEs to foster their survival and growth. These capacity-building measures include training and development, global value chain network development, infrastructure projects, credit and policy support (PIDS, 2013).

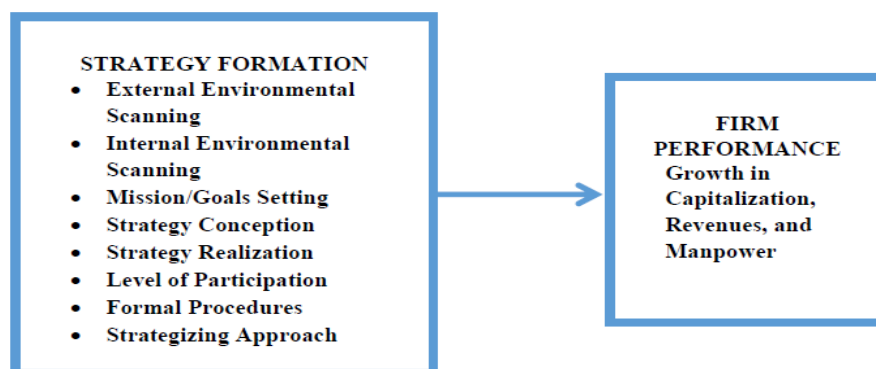
There is however a lack of government understanding and appreciation of the equal importance of developing the management capabilities of SMEs. As previous research has shown, policy instruments failed to acknowledge adequately that management capability, as opposed to technical considerations, are equally important determinants of SMEs innovation and success. To be able to succeed in the global competition, especially in the ongoing ASEAN integration, the country's SMEs must exhibit managerial competence and resilience (Habito, 2017). Indeed, as Karami (2015) pinpointed in his research, management training and development as well as senior managers' strategic awareness are crucial factors in firm's success. This lack of management capability building among SMEs, if properly addressed, may spell out a missing ingredient in the over-all recipe of fostering the growth of SMEs in the Philippines (Aldaba, 2012).

This study is an empirical investigation of strategy formation practices and firm performance of the country's small and medium-sized enterprises (SMEs) in the export sector. In addressing the gaps in the research track, the study seeks to determine the impact of strategy formation activities and enabling factors on firm performance. Specifically, the study aims to find answers to the following questions:

1. What is the extent of SMEs' strategy formation practices, in terms of external and internal environmental scanning, mission and objectives setting, strategy conception and strategy realization?
2. Is there a relationship between strategy formation activities with firm performance, in terms of growth in sales revenues, in capitalization and in manpower?
3. Which particular strategy formation activities have more impact on firm performance?
4. How do the following factors (such as level of participation in planning, formal planning procedure and strategizing approach) enable or hinder the effective strategy formation activities of the SMEs?
5. Do the enabling factors (such as the level of participation, formal planning procedure and strategizing approach) impact on firm performance of SMEs?
6. What are the insights of the SME participants of Case Study on the relationship between strategy formation and firm performance?
7. Based on the empirical findings and analyses, what recommendations can be made in terms of government policy enhancements, academic interventions and future research for the improvement of strategy formation practices and firm performance of Philippine SMEs?

Based on the analysis of the study and the overall business environment, a conceptual framework (as illustrated in Figure 5) was proposed. This framework has 11 factors namely: external environmental scanning, internal environmental scanning, mission and objectives setting, strategy conception, and strategy realization, level of employees' participation in planning, formal planning procedures, deliberate and emergent type of strategy-making approaches, and finally, the ultimate desired outcome would be firm performance which includes growth in sales revenues, growth in capitalization and growth in manpower.

Under this conceptual framework, the independent variables consist of external environmental scanning, internal environmental scanning, mission and objectives' setting, strategy conception, strategy realization, level of participation, formal procedures in planning and strategizing approach. And the dependent or criterion variable consists of firm performance. (y) is the dependent or criterion variable.



RESEARCH METHODOLOGY

The study used quantitative and qualitative research methods to analyze the relationship among strategy formation, enabling factors and firm performance. A survey was conducted among exporting SME managers/executives in Metro Manila. The survey measured the frequency of strategy formation activities, the presence of enabling factors and firm performance. The qualitative portion of the research inquired into possible explanations for the results of the quantitative portion.

The participants of the study were drawn from around 500 of exporting SME managers based in Metro Manila. Conclusive findings were derived from the empirical study of 87 operational exporting SMEs (about 18% of exporting SMEs in Metro Manila), representing a random sample with estimated .149 margin of error at significance level of 0.05.

A survey questionnaire was prepared based on related literature (see Review of Literature in this study) and the author’s framework of research study. The survey measured the frequency of strategy formation activities of SME managers according to a Likert scale of five (5) as follows: Never (1), Rarely (2), Occasionally/ Sometimes (3), Frequently (4), and Always (5). The strategy formation activities (60 items) were drawn from the findings of the quantitative study and related literature. These were categorized according to the following: external environmental scanning (10 items), internal environment scanning (4 items), mission and objectives setting (8 items), strategy conception (7 items), strategy realization (14 items), level of participation in planning (3 items), formal planning procedures (7 items) and type of planning (6 items). See Appendix C for list of items per category.

After studying the results of the quantitative study, two case studies were conducted to inquire into possible explanations of the results. This qualitative research is a holistic “two-case” case study that sought to uncover the assessment of two SME owner-managers on their strategy formation activities and their influence on their firm performance. These two wholly Filipino owned SME companies include an exporter of perishable seafood fresh produce and the other is an exporter of processed fruit products.

SIGNIFICANT RESULTS

Around 52% of the respondents are ages from 25 to 44 years; only 21% were ages less than 25 years old, 28% were more 45 years old or more.

Age	Percent
Less than 25 years	21
25 to 34 years	29
35 to 44 years	23
45 to 59 years	20
60 or more	8
Total	100

In terms of years of service to the company, 47% of the respondents have been working for the company for 11 years or more, 24% for less than three (3) years and 21% for three (3) to five (5) years.

Years of Service	Percent
Less than 3 years	24
3-5 years	21
6-10 years	7
11-15 years	9
16 - more than 16	38
Missing	1
Total	100

In terms of educational attainment, 90% were at least college graduates

Educational Attainment	Percent
HS graduate	1
Technical/ vocational graduate	1
Some college	8
College graduate	75
Masters/ Doctorate units or degree	15
Total	100

In terms of years of experience as a senior manager and/or executive, inclusive of previous work experience, 37% of the respondents had occupied senior management/ executive positions for six (6) to 10 years and 25% were in senior/ executive positions from three (3) to five (5) years. Around 20% occupied such positions for 11 years or more and 18% for less than three (3) years

Years as Senior Manager/ Executive	Percent
Less than 3 years	18
3-5 years	25
6-10 years	37
11-15 years	6
16 - more than 16	14
Total	100

Validating the Strategies

Participants in this research came from 87 small and medium scale enterprises. Around 67% of the companies are considered small-scale enterprises which have a capitalization of three million pesos to 15 million pesos. About 33% are considered medium-sized enterprises which have a capitalization of 16 million pesos to 100 million pesos. The average amount of capitalization for the participating companies is 26 million pesos.

The gross sales revenues as of Dec. 31, 2016 of the participants' companies range from 450,000 pesos to 207 million pesos. The average gross sales revenue is 24 million pesos.

The number of employees as of Dec. 31, 2016 of the participants' companies range from 5 to 700 employees. The average number of employees is 69.

Around 41% of the companies have been in operation for more than 12 years; 23% for more than three (3) years to six (6) years; 14% for more than nine (9) years to 12 years; 11% for three (3) years or less; and 10% for more than six (6) years to none (9) years. Around 55% export products while 45% export services.

When asked about their understanding of strategy realization as a critical component of strategy formation, both SME managers defined it as the set of activities of taking concrete actions, monitoring performance results, re-evaluating planned and unplanned actions, and making corrective actions. As both SME managers shared their view on the critical role of strategy realization in improving firm performance, they also shared the following insight, which has been propounded by literature: "Managers must not only think, talk and decide, but also do, to have concrete result and tangible impact; innovation is 5% inspiration and 95 percent perspiration."

Key issues and points converged during the individual interviews that have elicited new viewpoints and have provided, upon reflection and synthesis, stronger support for the empirical results of this paper. These major points are as follows:

The Critical Role of Strategy Realization

From the assessments of the two case respondents, this case study concluded that strategy realization activities have significant role in determining the strategic outcomes of SME's firm performance. The SME managers saw the need to focus on operationalizing their short-term plans to achieve their production and sales targets on monthly, quarterly and yearly bases. While their planning horizon is relatively shorter than that of the large corporations, the SME managers are inclined to be give priority on action-taking while being guided by their own version of strategic intent rather than by specific, strategic objectives.

The Practice of Strategy Formation in SMEs

This case study underscored the inclination of both respondents to rely on new information they gathered and/or practical lessons they derived from taking actions to realize their strategy and intent. Indeed, as shown in the literature, the practice of strategy formulation which sets the plan before action (which is normally followed by strategy implementation) is mostly applicable in large companies. These companies have the resources to put up a separate planning staff which draws out a concrete plan and implements the plan in a separate time horizon. In contrast, the SME firms which lack the resources, unlike the large companies, directly engage in almost simultaneous fashion, both intended and unplanned actions, to realize their strategy.

These actions-reflection-adjustment cycles is captured in the "strategy realization" component of strategy formation in SMEs. This cycle then develops a pattern of actions which eventually realize the firm's strategy over time. As illustrated by the literature, this pattern of actions and realization of strategic outcome constitute SME's strategic behavior which impacts firm performance.

The Relative Importance of Strategic Intent

Both the case respondents noted that the practice of setting formal and specific strategic objectives does not fit in their situations. For practical purposes, they prefer to set up goals or key results areas that have ranges or degrees of accomplishment depending on the prevailing circumstances during the strategy realization phase of strategy formation.

The Participation of Rank-and-file Employees in Planning Process

This case study uncovered the insight of SME owner-managers suggesting that the level of employees' participation in the whole planning process has a vital role in improving firm performance. They both shared the

idea that when a small company involves its rank and file in the planning process, the firm is able to develop awareness and commitment among its employees as to the goals and strategies of the firm. They become united in focusing their efforts toward the attainment of specific goals and always on-guard on spotting opportunities and threats and adapt to such emerging changes in the environment.

The Support of Private and Government Sectors

Both respondents agreed that the support from government and private sectors is crucial in ensuring the growth and success of SMEs in the Philippines. They specifically cited the Export Management Bureau of the Department of Trade and Industry that played a critical role in catalyzing the development of export market networks through its foreign market data base, frequent trade missions abroad and application of the country’s membership into free trade areas (FTAs). Specialist-consultants helped the SMEs learn modern packaging techniques that can pass the acid test of international standards. Financial consultants are a big help to SMEs not only in terms of accessing local funds but also in arriving at financial decisions for company’s growth.

Special trade associations such as PILEXPORT, PHILFOODEX helped the SMEs share their expertise in terms of trade facilitation, logistics and financial remittance system. The academe, as exemplified by the UP Institute of Small and Medium Size Industries (UPSMSI), plays a significant role in offering new courses and research programs on entrepreneurship development.

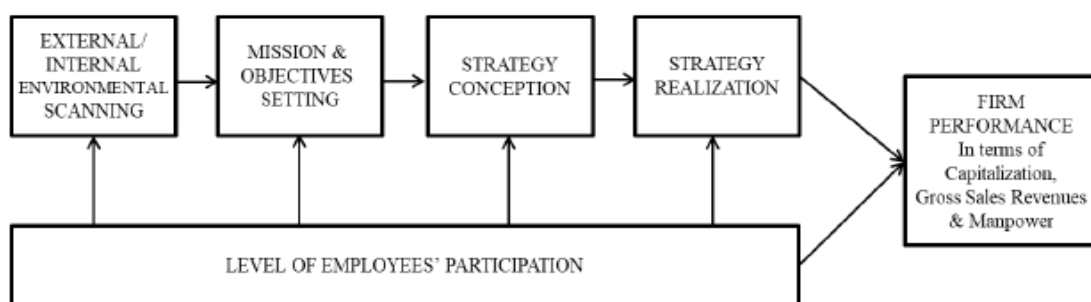
RECOMMENDATIONS

The following are the recommended strategies.

Policy Enhancements in Philippines SME Development

During the conduct of this study, the researcher had a meaningful interaction with the officers and staff of the Export Marketing Bureau (EMB) and Bureau of Small and Medium Enterprises (BMED) of the Department of trade and Industry (DTI). Both agencies have direct responsibilities for the development of the SME sector and export industry. The researcher was privileged to attend the 2017 National Export Congress --which laid down the strategies and policies of the DTI With the theme, “Innovation and Collaboration”, the Congress saw the growth prospects of the export industry with SMEs as its lynchpin.

The researcher, however, observed the absence of representatives of the BSMED in the said Congress, who could have addressed the concerns of the participating representatives of the SME exporting companies. Likewise, the issues affecting the exporting SMEs were not embedded in the whole program of the Congress, except in the speech by a DTI Director who talked on the need to promote innovation, inclusive growth and industry growth or the I-CUBES strategy. The observations of the researcher on the proceedings of the recent export congress point to some weaknesses in the government’s policy framework on SME development, such as: a) fragmentary and uncoordinated efforts by all government bodies to focus on SME development; and 2) the lack of emphasis in one very important dimension of SME development strategy, that is, upgrading the management capability of SME managers in the Philippines. This can be described in a illustration as such:



Hence, the following public policy enhancement is recommended: There must be an integrated SME development strategy, with emphasis in developing the management capability of SME managers, to be drawn and implemented by all stakeholders (private and government) with BSMED as the lead agency; and this lead agency must be given enough authority and budget to carry out its objectives.

Course Development and Research Interventions in the Academe

As uncovered in the case study, the case participants shared the view that the academe plays a significant role in the nurturing of strategic management as a field of academic and entrepreneurial discipline among SME owner-managers. While the University of the Philippines Institute of Small and Medium Sized Industries or UP-ISMI, was created to involve the academe in the development of SMEs in the country, the institution had focused its activities in giving skills training and upgrading, in the same fashion as the technical-vocational schools; and hence failed to address the strategic issue of management development of SME managers. Hence, the following academic intervention is recommended: There must be a new course curriculum on SMEs development that is anchored on a strategic management

SUMMARY AND CONCLUSION

Further analyses of the empirical results pave the way for better understanding of the situation of strategy formation and firm performance of SMEs in the Philippines. The following major conclusions have been derived.

The Predictor Variables in the Strategy Context of SMEs

While the quantitative results proved the predictive value of strategy realization and level of participation in the planning process, the qualitative research provided insights in support of this quantitative finding. Cognizant of the specific characteristics of SMEs – having simple structure, scarce financial resources and operational mode of planning, SME managers are inclined to prioritize strategy realization activities (over other strategy formation activities). In the same vein, the SME companies, given their specific characteristics, tend to involve their rank and file employees in planning process to systematize and facilitate organizational learning and teamwork – which are key to achieving flexibility and adapting to fast changing environment, especially in the international arena of competition.

The Support Roles of Non-Predictor Variables

While the other independent variables, such as environmental scanning, mission/objectives' setting and strategy conception do not have predictive values, as shown in the quantitative results, they nonetheless provide support to predictor variables in achieving strategic outcomes of SMEs' firm performance. As explained by the case study results, the emergence of these non-predictor variables may be traceable to the specific characteristics of Philippine exporting SMEs which do not fit in the traditional strategy formation model (usually applicable to large companies).

A New Framework of Strategy Formation For Philippine SMEs

The quantitative results of the research showed that only two out of eight independent variables have predictive values to firm performance. As supported by the literature, there has been a dearth of empirical studies on the appropriate model of strategy formation on SMEs. Most of the frameworks on strategic management were crafted from the experiences and needs of large companies, and thus suit their peculiar needs and circumstances.

The limited empirical studies on SME strategy formation, as shown by the literature, has 2 weaknesses, namely: one, its preference to the traditional deliberate and formal planning process (which is most applicable to large companies) over the emergent and informal planning process (which is most applicable to SMEs); and two, the study was based on the circumstances in a developed economy.

Based on the empirical findings of this dissertation research, the author has come up with a revised conceptual framework on strategy formation and firm performance of Philippine exporting SMEs that addresses the

weaknesses of previous frameworks on strategy formation and take the enabling and hindering factors for their improved firm performance in the context of a developing country like the Philippines.

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