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Implementing strategically aligned performance measurement in small firms

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Abstract

This paper investigates the potential for improving the implementation of strategically aligned performance measurement (PM) in smaller firms. It identifies structural and cultural characteristics that typify smaller firms and examines the PM literature to investigate implementation difficulties and whether they can be overcome through an alternative development process. An empirical study examines the implementation of strategically aligned PM in two small firms, using a process designed to overcome the difficulties that arise in this environment. The paper concludes that the current focus on achieving balanced PM systems is less critical in small firms and the key aim should be instead to stimulate strategically aligned improvement.

Keywords: Performance measurement; SME; Strategic alignment; Implementation

1. Introduction

The concept of strategically aligned performance measurement (PM) was developed from the many criticisms levelled at traditional, financially focused PM systems in the 1980s and 90s (e.g. Kaplan, 1983; Eccles, 1991; Ghalayini and Noble, 1996). This led to the development of a number of processes and frameworks which aim to link financial and operational measures to stakeholder requirements and align these with the overall strategy of the business (Kaplan and Norton, 1992; Lynch and Cross, 1991; Neely et al., 1996; Ghalayini et al., 1997). The purpose of this was to enable businesses to reduce their reliance on purely financial measures and drive performance towards the achievement of their strategic objectives. However, the majority of these approaches were designed and tested in, and for, large companies. Research has demonstrated that there can be considerable difficulties in implementing these methods effectively and that difficulties are particularly prevalent in smaller firms (McAdam, 2000).

Using examples from the literature, this paper explores the structural and cultural characteristics of small and medium sized enterprises (SMEs). It then tests a development approach which was designed specifically for use in SMEs, through an empirical study. The aim of the study is to establish whether it is possible to use this approach to

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develop strategically aligned PMs in SMEs, through the ability to work within the cultural and structural constraints of this sector.

2. SME characteristics

It is well documented that SMEs exhibit different characteristics from larger organisations. These differences are commonly perceived as being a consequence of the structural and cultural environment that these firms operate in. To explore the cultural and structural characteristics of SMEs adequately, an analysis of the literature was undertaken, examining SMEs from three perspectives: *Organisational Environment, Competitive Environment* and *Management Practices*.

3. Organisational environment

The most widely acknowledged factors that distinguish SMEs from larger companies relate to the organisational environment in which they operate, which is largely defined through the underlying organisational culture. Schein (1985) defines culture as "*a pattern of basic assumptions—invented, discovered, or developed by a given group as it learns to cope with its problems of external adaptation and internal integration*". According to Cameron and Quinn (1999), there are four basic types of organisational culture:

- *hierarchies*, which focus on formalising procedures and ensuring a coherent and well-coordinated business structure;
- *market culture*, where the major concern is with results and remaining competitive;
- *clan culture*, which emphasises the need for teamwork and high staff morale; and
- *adhocracies*, which are flexible, dynamic and willing to take risks to succeed.

The literature reveals that SMEs are most closely aligned with the adhocracy model, as they are considered to have flat structures with few management layers, be flexible and adaptable to changing market needs and have a high potential for innovation (Ghobadian and Gallear, 1997; McAdam, 2000; Yusof and Aspinwall, 2000b; Wiklund and Wiklund, 1999; DTI, 1994; Jennings and Beaver, 1997; Burns, 1996; Gunesekaran et al., 2000). However, the ability to operate effectively within a culture of adhocracy may be restricted by the fact that SMEs are also seen as suffering from "*resource poverty*" (Welsh and White, 1981), both in terms of human resources and financial stability and security (Abdul-Nour et al., 1998; Pelham, 1999; Wong, 2005).

There is little evidence of hierarchical culture within the SME environment, as it is commonly noted that SMEs are loosely structured, with informal operating practices and a lack of bureaucracy (Jennings and Beaver, 1997; Hyvarinen, 1990). However, there are certain characteristics which correlate closely with aspects of clan culture, including the fact that there can be a high degree of personal authority among staff and management who are visible and involved in the operations of the company (Storey and Sykes, 1996; Jennings and Beaver, 1997). Unfortunately, there are also recognised skills shortages amongst staff, along with a deficit in management expertise (McAdam, 2000; Curran, 1987; Huang and Brown, 1999) and with highly personalised, authoritarian management styles common (Storey and Sykes, 1996; McAdam et al., 2004).

4. Competitive environment

SMEs are considered to be flexible and adaptable to market changes (Ghobadian and Gallear, 1997; Yusof and Aspinwall, 2000b). This responsiveness is generally viewed as a positive characteristic and suggests that there is some correlation of SMEs to the market culture model. However, the root cause of this attribute is that SMEs often have only a limited overview of the markets in which they operate, leading to a lack of control over their competitive position (Wiklund and Wiklund, 1999; Huang and Brown, 1999; Pelham, 1999). They are unable to drive the market, but instead, must react and adapt to market changes over which they have no influence (Burns, 1996; Storey and Sykes, 1996; Hyvarinen, 1990). According to Miller and Whitney (1999), this suggests poor organisational configuration, which is detrimental to sustained competitive advantage. Configuration is defined as "*making choices about what a company will do and how it will do it, and…ensuring that the things a company does reinforce each other*". They argue that the lack of a focused competitive strategy is one of the key causes of poor organisational configuration.

However, the problem of organisational configuration is not just restricted to understanding