

# Impact of Strategic Planning on Financial Performance of Companies in Turkey

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## Abstract

Strategic planning is important for strategic management of companies. The purpose of this study is to explore the impact of strategic planning on financial performance of Major Industrial Enterprises of Turkey. Our findings show that many domestic and foreign firms in our sample have a strategic process in place. It is an annual process and considered a very important organizational activity. This paper is one of the few studies to examine the strategic planning process in a sample of firms from a transitional economy. It can be considered a longitudinal study because it examines a set of institutions to identify changes in their performance over time, as they incorporate the use of strategic tools in a dynamic competitive environment. The findings of this study provide a contribution to our understanding of the nature and practice of strategic planning in Turkish companies and possibilities of correlations between their efforts and performance.

**Keywords:** Strategic planning, Financial performance, Turkey

## 1. Introduction

Even though the concept of strategy may have had its original underpinnings in the military and its war efforts, over many decades it has become a mainstay and a major process (organizational activity) in for-profit and not-for-profit organizations. These organizations have refined and used the process to understand issues which they cannot control but have a significant impact on their survival and success, and use their limited resources and competencies to improve their competitive positions. It was hypothesized that by consciously using formal planning, a company could exert some positive control over market forces, create competitive advantages, improve organizational effectiveness, and improve its performance.

As a result, new concepts and tools were developed and added to company repertoires over time, and they were used to bring formality and uniformity to strategy development in organizations. Because one of the objectives of this process is to develop competitive advantages leading to superior organizational performance, the relationship between the firm's strategic planning efforts and firm performance received considerable attention from academics, researchers, and business executives. However, despite the large number of studies examining this relationship, the findings have been inconclusive and present a mixed picture. Even though the majority of studies have reported a positive relationship between strategic planning and firm performance (Sapp and Seiler, 1981; Wood and LaForge, 1979), several studies found no relationship (Robinson and Pearce, 1983; Kudla, 1980), and a few reported a negative relationship (Fulmer and Rue, 1974). A recent study by Gibson and Cassar (Gibson & Cassar, 2005) cast doubt on the causal relationship between planning and performance, even in small firms.

The purpose of this paper is to extend the previous findings by examining the nature and practice of strategic planning in a different environmental context, that of the developing transitional economy of Turkey and the impact of these practices on the performance of the companies which utilize these practices. This context provides the novelty to the study as most prior studies on the strategic planning process have examined evidence from firms in mature market economies. To achieve this objective, we will briefly discuss why we consider and classify Turkey as a "transitional economy", review and discuss the few research studies and their findings

conducted in similar economies, and present the findings of our research study of top 500 companies in Turkey. This will help to generalize the previous findings and will be instructive in comparing the strategic planning processes of firms in a developed market economy and those located in a transitional economy. By identifying and documenting the levels of strategic process and the types of strategic tools employed by the companies in differing stages of transitory economies and identifying the impacts of these processes on the companies, we can develop a roadmap and incorporate this knowledge to educate and prepare the managerial talents in these economies.

## 2. Turkey as a Developing Country and an Economy in Transition

Until recently, the primary focus of researchers of strategic planning had been United States and developed economies of Europe. As the economy in United States and Great Britain developed and evolved, various models and methodologies were developed and serious discussions of these methodologies and concepts were conducted on improving competitiveness of businesses in these economies. Very little research was done to examine the understanding and usage of these strategic planning concepts and tools in developing countries and the organizations which form the foundations of these economic systems. One could argue that among the causes of this lack of research were semi-closed state of these economies, the dominant legal ownership (state owned) and the associated governance of majority of medium to large-scale organizations, and the lack of sophistication of the managers of these organizations. Furthermore, the structure of these economies did not present the same competitive issues which dominate open and developed economies and may not have necessitated the use of strategic planning to gain additional competitive advantages.

Last decade and a half has seen major developments in communication technologies and resulting globalization of all types of industries and business processes. The businesses from developed economies have extended their reach to all corners of the globe in search of cheaper costs and new markets, bringing a greater dynamism and heightened level of competitive behaviors to these previously fairly stable economic environments. Furthermore, the increased “foreign direct investments” (FDI) and the associated ownership and governance of new and foreign based competitors have forced the executives of the local enterprises to develop or acquire talent in their managerial ranks and increase their sophistication of the dynamic competitive forces of their business environments. Some countries which were considered undeveloped/developing have been impacted by these changes much more significantly than others. The governments of these countries have taken steps to use these developments as means to accelerating their economies’ transition from an underdeveloped to a developed economy, while opening their local businesses to increased competition and forcing them to adjust their organizational processes to sustain themselves in unfamiliar dynamic environments and increased uncertainties. As evidenced by the World Economic Forum global competitiveness index, Turkey has moved from 71st (out of 131 countries ranked) for 2005-2006 to 59 for 2006-2007, and to 53 for the 2007-2008. The sophistication of company operations and strategy ranking for 2007-2008 is 41 out of 127 countries ranked. (*The Global Competitiveness Report 2006-2007*; Porter, 2007) The World Economic Forum’s annual *Global Competitiveness Report* evaluates the potential for sustained economic growth of over 130 developed and emerging economies and ranks them accordingly. It was first released in 1979.

The characteristics of the Turkish economy make it an interesting case to examine the nature and role of the strategic planning process in its largest businesses. Since the early 1980s, government policies in Turkey have focused on developing a free market economy and have encouraged an outward-oriented export-led economic development strategy. Significant progress has been made in the liberalization of trade and investment policies and the pursuit of macroeconomic stability and economic growth. This policy stance has also contributed to a substantial increase in inward foreign direct investment (FDI) to Turkey. Turkey has climbed to 16<sup>th</sup> place among top FDI attracting countries in 2006, up from 22<sup>nd</sup> place in 2005, 37<sup>th</sup> place in 2004 and 53<sup>rd</sup> place in 2003. It was ranked 5<sup>th</sup> among the developing countries. The level of FDI inflows to Turkey has increased from an average of 853 million USD during the 1995-2000 period to 9.8 billion USD in 2005 and to 20.1 billion USD in 2006. As of first five months of 2007, FDI inflows reached 11 billion USD, reinforcing the predictions for FDI inflows of 25 billion USD and plus for the year-end. (YASED, 2007) Turkey is ranked as 17<sup>th</sup> largest economy in the world and 6<sup>th</sup> largest in EU and has averaged an annual GDP growth of 7.4%/year since 2002. As another outcome of this increased FDI and transition of the Turkish economy, demand for translations into Turkish language has grown 36% over the last year, placing it at number 9 in the world after Chinese and Russian. Top six is composed of former Eastern Block countries which have joined or in the process of joining EU. (Ewing, 2007)

Over a decade ago, due to its high economic growth and rapidly growing population, the US Department of Commerce placed Turkey among the ten big emerging markets (Garten, 1996). As the developments to date

have shown, this classification was very much on target. Turkey's five years' (prior to global economic downturn) growth rate average of around 7 percent puts it into one of the world's best-performing economies. Turkey ranked 22<sup>nd</sup> among the exporting countries and with 16% increase in exports during 2006, is on par with average export growth rates of global economies. Its exports to Europe have grown an average of 24% for the past three years and with 55% of the country's total exports, EU remains the nation's leading export market. (McCathie, 2007)

By looking at the stages of the basic needs of a nation's population, Martinez and Haddock present another approach in identifying transition economies and the nation's evolution from a developing one to an industrialized one. They identify and argue that a nation's basic needs evolve through survival (obtaining adequate food, shelter, and clothing) to quality (seek better quality in food, shelter, and clothing) to convenience (time-saving appliances, packaged foods, etc.), and finally to customization (goods and services which satisfy individual tastes and desires). According to these authors, sub-Saharan Africa is in "survival" stage, China and India and Turkey are in "quality" stage, Eastern Europe and Latin America are in "convenience" stage, and finally, North America, Japan, and Western Europe are in the "customization" stage. Their model places Turkey and Brazil clustered around the start of the "convenience" stage. (Martinez and Haddock, 2007)

All these different economic and sociological measures place Turkey at a very unique stage of its economic development and as a country which is rapidly moving from a sheltered static economy to a dynamic and extremely competitive developed economy. Of course with this transition comes the additional competitive pressure for its home-grown privately owned organizations, with responsibilities to their stockholders, and increased turbulence caused by foreign based competitors entering their markets. Furthermore, these Turkish firms' desires and attempts to enter foreign markets require them to develop sophisticated managers, development and use of tools to understand these new markets, and effective and efficient processes to be able to compete in these developed markets.

### **3. Earlier Studies on Strategy and Performance**

As we stated earlier, the relationship between firm strategic planning efforts and firm performance received considerable attention. However, despite the large number of studies examining this relationship, the results have been inconclusive, with findings ranging from positive relationships to no relationships to negative relationships.

Several researchers have attempted to understand these contradictory findings. Armstrong (1982) published one of the first such papers. His analysis of 14 studies generally supported the hypothesis that formal planning was useful but, noted that there were "serious research problems" with the studies. He was very much concerned with the lack of description or definition of the strategic planning process provided to the study subjects. He concluded that "without a description of the planning techniques, it is not possible to assess the value of planning in a scientific manner". (p. 204).

Pearce, Freeman, and Robinson (1987) also concluded that the evidence that formal strategic planning enhances a firm's financial performance is "inconsistent and often contradictory." They had concerns about the methodology's limiting impact on the researchers' ability to understand the effect of strategic planning on performance. Their conclusions were based on a review of the results of 18 papers which examined the relationship between formal strategic planning, using a definition similar to Armstrong (1982) for strategic planning, and organizational performance. They were concerned about the "lack of consistent definition" of strategic planning, how the strategic planning construct was "measured", and the "impact of corporate context" and the factor of business size. Venkatraman and Grant (1986) noted that there is no widely accepted definition of strategy and that the inability to measure the strategic planning construct has hindered research attempting to identify substantive relationships between independent and dependent variables. Boyd (1991), based on the results of his meta-analysis of 21 studies published between 1970 and 1988, including 29 samples and 2,496 organizations, concluded that there were modest positive correlations between strategic planning and financial performance. However, he was concerned with the significant measurement errors in these studies and concluded that this most probably resulted in an underestimate of the true strategic planning-performance relationship. However, one significant work, Miller and Cardinal (1994), seemed to put the issue to rest: they concluded that "Planning was found to be strongly and positively related to growth in studies in which industry effects were controlled, an informant source of performance data was used, planning was defined as not requiring written documentation and the quality of the assessment strategy was high". (Miller & Cardinal, 1994, 1660)

A study by Sarason and Tegarden (2003) focused on the configuration theory and firm's resource based view to understand the relationship between strategic planning and the firm's performance. Their findings also provide

partial support for a positive relationship between strategic planning and performance. However, they concluded that this relationship is moderated by organizational stage of development and that it is beneficial to early stage firms. The underlying premise for these conclusions are based on the development competitive advantages provided by the structure and the future thinking incorporated into the strategic process and the non-sustainability and erosion of these advantages in late stage firms, whose processes are more prone to imitation.

Realizing the complexities of defining the strategic planning construct and the measurement issues identified and discussed by earlier researchers, we decided to identify specific strategy analysis/development tools available to companies, their use by these companies, and compare it to the financial performance of these companies over a 3-year time frame. By focusing on the companies in a transitory economy (companies most likely to be in their early stages in competing in open economies), we tried to identify the frequency of the use of these tools and adaption of other strategic planning mechanisms on the relative performance of these companies.

#### **4. Research Study**

Our research sample was drawn from the Turkish Chamber of Industry database which listed the top 500 manufacturing firms in 2006. The survey questionnaire was mailed to the CEO of each company with a letter requesting that the CEO, or his/her senior executive in charge of strategy development within the organization, to complete it. The survey was also made available on the Internet, thus providing the respondents an option to return the paper copies or fill out the questionnaire electronically. The overall response rate was 14.2 percent. Of the 71 returned responses, seven (9.86%) were completed online. There were no duplicates between the paper and electronic returns.

The highest ranked respondent company was ranked as number 2 and the lowest was ranked as number 497. The company rankings were based on their 2006 annual manufacturing revenues (these firms had both manufacturing and non-manufacturing revenues), which ranged from highest TRY 5.606billion (USD 3.742billion) to lowest TRY 83.690million (USD 55.86million), with total revenues of TRY 6.456billion (USD 4.309billion) and TRY 95.294million (USD 63.610million), of the same companies respectively (Note 1). The number of employees ranged from highest 9,780 to lowest 66 with 1,197 as the average.

Over ten industries were represented in the sample and textile industry had the largest representation with nine firms. The respondent companies ranged from 12.68% (9 firms) classified as “single business” (95% or more of their revenues coming from one business segment), 80.28% (57 firms) classified as “dominant/focused business” (70% to 95% of revenues coming from one business segment, to 7.04% (5 firms) classified as “multi-business” (with revenues less than 70% from any segment). All of the seventy-one firms were privately owned (had stockholders), sixty (84.5%) of domestic origin (Turkish) and eleven (15.49%) foreign-owned. The respondent firms ranged from wholly-owned independent companies to subsidiaries of divisions of large organizations.

#### **5. Discussion of Results**

Our findings show that a large number of domestic and foreign firms in our sample have a strategic process in place, it is considered a very important organizational activity (by 86.26% of domestic firms and by 100.00% of foreign firms), and it is an annual process. Because of earlier researchers’ concerns about “lack of description or definition of the strategic planning process provided to the study subjects”, we decided to look at the impact of “the use of process” (identified with the use of generally accepted components of a strategic process), “focus/objectives of the process” (what are the companies trying to accomplish), and “the use of strategy development tools and models” (e.g. what-if analysis, SWOT analysis, etc.) on company performance. Following is the presentation and discussion of our findings.

When we looked at the impact of different components/activities in a strategic process and their impact on company performance, the only two that were correlated (positively influenced) and statistically significant were “involvement of top management in the process” and “having a mission statement”. Both of these strategic process components identify and define the importance of the process in the organization and had significant impacts on the profitability of the firms in our study. Even though all of these companies had seen large sales growth rates and growth in exporting their products, two processes (top management participation and mission statement) had resulted in higher average yearly profits over time. These findings are summarized in Table 1. These findings highlight and reinforce the importance of “top management’s active involvement in providing direction” to the organization and “having their and organization’s role and position in the economy and the society” clearly articulated, formalized, and used as a guide for the organization’s activities and processes.

Even though significant number of respondent firms focused on strategic issues, only few of these issues had an impact on the firm's performance. The performance measures, average sales growth per year, average profit per year, and average export growth rate per year were positively influenced. As can be seen from Table 2, average profit per year was correlated to focus on "organizational capabilities" (a better knowledge of what the firm is capable of) and focus on "similar markets" (expanding capabilities to where the firm has experience in). Interestingly, the only significant correlation between the average export growth rate per year was the firm's focus on "contingency plans. We did not inquire (the questionnaires were not followed-up with interviews) and cannot speculate why there is such a connection. As can be seen from the table, less than half of the companies in our study focused on contingencies and majority of these firms were subsidiaries of foreign companies.

Companies involved in strategic process use different tools for their analysis of their internal capabilities and external changes and issues. These tools were developed over time and their extensive uses are researched and documented by many. In our study, we selected the tools which we identified as being the ones which are most commonly used and analyzed our data to find out if use of these tools, or lack of use, had any significant impact on performance of the firms in our study.

As can be seen in Table 3, even though there were some differences between the users and non-users of these strategic tools, none of the findings were statistically correlated. Except for profitability, both the average sales growth (which was significantly higher) and the average export growth were higher for the firms which did not use any of the strategic tools or used them very infrequently. This is contrary to what we expected as an outcome and cannot explain it. We could only assume that the significantly higher growth rate for non-users might be a sign of the aggressive market positions these companies might be taking (without considering any consequences and using a scatter-shot approach) or expanding into new products/markets with high entry costs, and might explain their significantly lower average profits. If this is the case and if their profitability increases, as they consolidate their positions in these new markets and slow down their growth, the findings present even a greater lack of usefulness of the strategic tools which organizations routinely use and have come to rely on to improve their competitive positions and effectiveness of their operations. This would be very contrary to the foundation, teaching, and practice of "strategy as a process and as a tool".

Even though our findings show a much greater attention to the competitive environment and its dynamics, the use of strategic and analytical tools is very limited and significantly lower in the domestic firms as compared to the subsidiaries of foreign firms. For the domestic firms participating in our study, the top three most popular (used frequently or always) strategy analysis and development tools were "critical success factors analysis" (38.60%), "economic forecasting" (36.84%), and "SWOT analysis" (36.21%). Foreign based firms seemed to prefer "SWOT analysis" (81.82%), "critical success factors analysis" (72.73%), and "BCG growth share matrix analysis" (55.56%). The "frequency of use" response means (on a scale of 1 = not used to 5 = always used) for "SWOT analysis" were 2.914 (domestic firms) and 3.909 (foreign firms), and for "critical success factors analysis" were 2.860 (domestic firms) and 3.727 (foreign firms). The mean response for the "Economic Forecasting" was 2.737 for domestic firms and 3.200 for foreign firms. Even though "BCG growth share matrix analysis" was used frequently or always by over half of the foreign firms, its popularity was not uniform among all foreign firm respondents. It was preceded by the mean response for the "value chain analysis", the third highest with 3.400 and by the mean for the "core capabilities analysis", the fourth highest with 3.300.

Because of this selective use of strategy analysis tools, we also wanted to see if use of any of these tools were positively correlated with the performance of the firms in our study. The findings are summarized in Table 4. As can be seen, of the most common nine strategy analysis tools used, only three were significantly correlated to firm's performance. Even though 37.32% of the respondents used "economic forecasting", average profit per year was directly correlated ( $p < .10$ ) with the use of this tool. The other two strategy analysis/development tools, "what-if/scenario analysis" (used by 22.39% respondents) and "growth share matrix" (used by 20.90% of respondents) were also positively correlated with the "average sales growth per year" ( $p < .05$  and  $p < .10$ , respectively).

Finally, access to sources of funds and the amount of funding available differ between independent companies and subsidiaries of large firms. This in turn may influence performance and ability to attract high quality managers and subsidiary firms may need to 'deliver' a performance objective, objectives based on financial criteria, formulated by the holding or parent company. As a result, given the importance of expected quarterly and annual positive results, subsidiary firm managers may be less likely to engage in risky and/or longer-term projects (Dierickx and Cool, 1989; Ghemawat, 1988). Given that our respondent firms included independent domestic (Turkish) firms and foreign based firms (subsidiaries of foreign companies); we wanted to see if there were any differences between the performance measures and the ownership type of the firm. When we look at

performance measures and ownership, even though they are not statistically significant, our findings show that subsidiaries of foreign firms have lower returns, supporting the findings of earlier studies. These findings are summarized in Table 5.

## 6. Conclusions

This paper is one of the few studies to examine the strategic planning process in a sample of firms from a transitional (developing) economy. It can also be considered a longitudinal study because it examines a set of institutions to identify any changes in their performance over time, as they incorporate the use of strategic tools in a dynamic and evolving competitive environment.

Even though the findings show a significant increase in the importance and use of strategic tools and processes in Turkey, a transitional (developing) economy, the basic question about the link/positive correlation between the use of strategic tools and company performance remains somewhat unanswered. Even though, through our findings, we have identified some links between the use of strategic tools and company performance, because of the small number of respondents and lack of follow-up interviews to look at some findings in greater detail, we cannot make any generalized statements or reach definitive conclusions. However, we are encouraged to see that the local firms in our study have increasingly adopted the techniques and tools of strategic planning more commonly employed by foreign firms. They have increasingly involved their top management in the process, allocated more resources to it, and incorporated greater formality into the process. It is quite interesting to see that over time the importance of this organizational process in Turkish firms have come to more closely resemble those of foreign firms. We attribute these changes to increased competitive pressures brought upon these firms as the Turkish economy has opened up and free market forces have come into play as it has begun its transition from an underdeveloped economy to one that is developing. We expect these changes and increased focus on the use of strategic tools and processes to continue as Turkey's market economy continues to develop and competition from foreign firms increase as globalization proceeds. Unfortunately, we cannot expect and make similar statements about their increased usage of these tools will lead them to stronger and sustainable financial results.

While the findings of this study provide a contribution to our understanding of the nature and practice of strategic planning in Turkish companies and possibilities of positive correlations between their efforts and their performance, there are a number of potential areas for future research. First, it would be a useful contribution to investigate the use of planning techniques and the pervasiveness of the process in service organizations (all the firms in our sample were manufacturing firms) and broaden the study sample by focusing on second-tier companies (our sample was drawn from the top 500 firms list of Chamber of Industry). With a larger study population, we could also try to understand the relationships between strategic process and firm performance in different business sectors. Unfortunately, because of the small sample size and the small number of firms from a given sector, we could not analyze the data to see if there are any differences between and among sectors. By focusing on specific sectors, we might have been better able to determine if there are significant differences between the companies that employ the tools and are using strategic planning process and the ones which do not. Finally, we hope that our study will interest and encourage similar studies not only visit the same unresolved issues but also focus on developing countries and the competitive issues faced by the firms which are the foundations of these countries and their economies.

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#### Note

Note 1. TRY was converted to USD for demonstration and reference purposes and, if the conversion rates of late 2006 or early 2007 were used, the USD numbers will be different. The conversion rate used was TRY 1 to USD 0.667512, the effective rate on January 1, 2010.

Table 1. Use of strategic process and performance (n = 71)

	Avg. Sales Growth/Yr	Avg. Profit/Yr	Avg. Export Growth/Yr
Top Management Participation in the Process(1)	24.29%	8.01%**	54.52%
Priority Activity - Conducted Annually	24.81%	6.15%	46.04%
Allocate Resources Specifically to the Process	25.26%	6.98%	36.18%
Follow Established Set of Procedures	24.81%	5.99%	39.97%
Mission Statement	26.06%	7.12%*	42.26%
Effectuated Managers Participating in the Process	26.63%	6.14%	47.72%
Quantified and Verifiable Written Objectives	25.19%	6.05%	49.19%

(1) Always responses. All others are yes responses. (Company Performance is for 2003-2006 years.)

\* p<.01, \*\* p<.05

Table 2. Focus on strategic issues and performance (n = 71)

Comparing Companies With No/Very Low Focus vs. High/Very High Focus				
	Avg. Sales Growth/Yr	Avg. Profit/Yr	Avg. Export Growth/Yr	Percent Responding (high or very high)
Quantitative Objectives	25.02%	6.90%	51.51%	86.15%
Organizational Capabilities	25.09%	6.80%***	48.24%	84.62%
Organizational Objectives	24.68%	6.43%	46.54%	84.62%
Similar Markets	26.52%	7.08%**	50.91%	71.88%
Changes in Environment	33.07%	7.60%*	53.81%	70.77%
Variations from Prior Plans	23.55%	6.20%	47.91%	70.77%
New Markets	26.52%	7.40%	52.78%	56.92%
Contingency Plans	14.49%	7.07%	13.62%**	43.48%

\* p<.01; \*\* p<.05; \*\*\* p<.10 (Company Performance is for 2003-2006 years.)

Table 3. Users vs. non-users of strategic tools

	Mean for Never or Very Infrequently (1)	Mean for Very Frequently or Always (2)
Average Sales Growth/Year	23.92%	18.28%
Average Profit/Year	4.82%	12.29%
Average Export Growth/Year	84.90%	81.44%

(1) Do not use any of the tools; (2) Use all the tools (Company Performance is for 2003-2006 years.)

Table 4. Using strategic analysis tools and performance (n = 71)

	Avg. Sales Growth/Yr	Avg. Profit/Yr	Avg. Export Growth/Yr	Percent Responding (very frequently or always)
Critical Success Factors	24.14%	8.08%	35.64%	44.12%
SWOT Analysis	24.53%	8.69%	40.59%	43.48%
Economic Forecasting	24.55%	8.87%***	38.04%	37.31%
Value Chain Analysis	21.25%	8.59%	30.09%	25.00%
PEST/STEP Analysis	27.56%	9.86%	39.29%	23.53%
What-if Analysis	17.71%**	10.46%	14.54%	22.39%
Core Capabilities Analysis	22.20%	11.02%	34.43%	22.06%
Growth Share Matrix (BCG)	20.44%***	6.96%	45.46%	20.90%
Porter's Five Forces Analysis	28.19%	7.66%	66.91%	11.94%

\*\* p<.05; \*\*\* p<.10 (Company Performance is for 2003-2006 years.)

Table 5. Country of ownership and firm performance (n = 71; domestic = 60, foreign = 11)

Performance Measure	Domestic Firms	Foreign Firms
Average Sales Growth/Year	26.28%	17.15%
Average Profit/Year	7.03%	3.34%
Average Export Growth/Year	49.04%	38.04%

(Company Performance is for 2003-2006 years.)