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THE EFFECT OF STRATEGIC MANAGEMENT BALANCED SCORECARD ON MICRO ENTERPRISES' (MIES) BUSINESS PERFORMANCE IN SURABAYA – INDONESIA WITH INTELLECTUAL CAPITAL AS AN INTERVENING VARIABLE

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Abstract: *In globalization era, all organizations, whatever they are, whatever they do, should perform a good strategic management practices to ensure that organizations fit within their environment. Strategic management not only considered as the key process but also has been considered as one of the most important practices the organizations should apply to achieve organizational vision, mission, strategy, and objectives, and moreover to differentiated one organization from another. There are a lot of argument noted that Micro Enterprises are crucial divers of economic growth and development of a country. This argument showed the important of this study. The study aimed to investigate the effect of strategic management by using Balance Scorecard (BSC) on Micro Enterprises (MIEs) performance in Surabaya-Indonesia, with Intellectual Capital (IC) as the intervening variable. To approach the aim of the study, practical data were collected by using a questionnaire. Result of the study showed that BSC have significant effect on IC, and IC has significant effect on MIEs performance.*

Keywords: *Strategic Management, Balanced Scorecard, Micro Enterprises, Intellectual Capital, Business Performance.*

INTRODUCTION

Organization for Economic Cooperation and Development (OECD) stated that Small and Medium Enterprises (SMEs) are the dominant form of business organization, represent more than 95% of enterprises and there for ensure 60-70% of the jobs. Furthermore, SMEs represent an essential source of economic growth, dynamic and flexibility in advanced industrialized countries, as for emergent and development economies. In development countries, SMEs can be considered as the backbone of an economy. SMEs are very important in promoting competitiveness and to bring new products or techniques to the market. The capacity to create a

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good environment for SMEs, which can supply quality services and competitive products at a low cost and in quantities that are adjusted to the market, can improve the performances and the development level of a national economy (Robu, 2013)[1].

As one of the development countries, SMEs in Indonesia is growing fast. In the period of 2011-2012, SMEs in Indonesia grew as much as 2.41% from total of 55.206.444 units to total of 56.534.592 (The 1st Meeting of the COMCEC Trade Working Group, 2013)[2]. From the total unit, more than 95% are composed by microenter prises (MIEs). These contributions have made MIEs become one of the key sectors to enhance Indonesian economy. MIEs, which are dominated by self-employment enterprises without wage- paid workers, are scattered widely throughout the rural areas, and, therefore, are likely to play an important role in developing the skills of villagers, particularly women, as entrepreneurs (Tambunan, 2009[3]).

Realizing the critical of MIEs, it is important to make sure that MIEs not only success, but also sustain. To be sustaining, MIEs need to focus on two main functions of strategic management: formulation and implementation strategy (Porter, 1996)[4]. MIEs need to set an objective for its activities and evaluate to make sure they are following this. Furthermore, MIEs can not only rely on the assessment of financial performance, but also on non-financial indicators.

In 1992, Kaplan and Norton developed the Balanced Scorecard(BSC) concept, and nowadays this concept is one of the most widely used management tools (Silk, 1998[5]; Malmi, 2001[6]). Many large companies are implemented it (Rigby, 2001[7]; Marr et. al., 2004[8]). However, even thoughit found to be popular in large companies,there are just few literatures reporting on theuses of BSC in SMEs. Since, most SMEs are not aware of this technique (Tennant& Tanoren, 2005[9]). However, McAdam (2000[10]), Andersen et. al. (2001[11]), and Kaplan and Norton (2001[12]) believed that BSCis as beneficial for SMEs as it is to large companies. However, BSC itself is not enough to guarantee SMEs success. To guarantee SMEs success, it needs another variable. According to Chien and Ting (2014), the effect of BSC implementation on company financial performance can be strengthen with two variables, which is: intellectual capital.

It is being recognized that intangible assets such as intellectual capital is the keys to attaining competitive advantage for the knowledge firms (Segelod, 1998[13]). Companies who owned knowledge-based assets are consider having the foundation for success in the 21st century. Wiig (1997[14]) argues that intellectual capital (IC) plays a fundamental role within modern enterprises as “packaged useful knowledge” (Klein & Prusak, 1994[15]).Furthermore, when enterprises face a more competitive market but can establish intellectual capital, then more commercial transactions will be developed and will make sustainable profits (Huang, 2008[16]).

LITERATURES REVIEW

Small and Medium Enterprises in Indonesia

Based on Small Medium Enterprises Act No. 20 of 2008 (*Undang-Undang Republik Indonesia Nomor 20 Tahun 2008 Tentang Usaha Mikro, Kecil, Dan Menengah*)[17], the definition of SMEs are as follows:

1. A micro enterprise is based in a traditional industry and is managed privately, andhas net assets of no more than 50 million rupiah (not including land or buildings) and annual sales of no more than 300 million rupiah.
2. Small enterprises are managed privately or by a corporate entity, but are independent from and are not the subsidiary or branch office of a medium or large enterprise. They have net assets of at least 50 million rupiah, and no more than 500 million rupiah (not including land or buildings), and they have annual sales of between 300 million and 2.5 billion rupiah.
3. Medium enterprises have net assets of between 500 million and 10 billion rupiah (not including land or buildings), and have annual sales of between 2.5 billion and 50 billion rupiah.

Table 1
SMEs Classification in Indonesia

No.	*Classification*	*Assets*	*Revenue*
1.	Micro Enterprises	Max. 50 mill	Max. 300 mill
2.	Small Enterprises	> 50 – 500 mill	> 300 – 2,500 mill
3.	Medium Enterprises	> 500 – 10,000 mill	> 2,500 – 50,000 mill

Note: Small Medium Enterprises Act No. 20 of 2008

Nature and Characteristics of SMEs

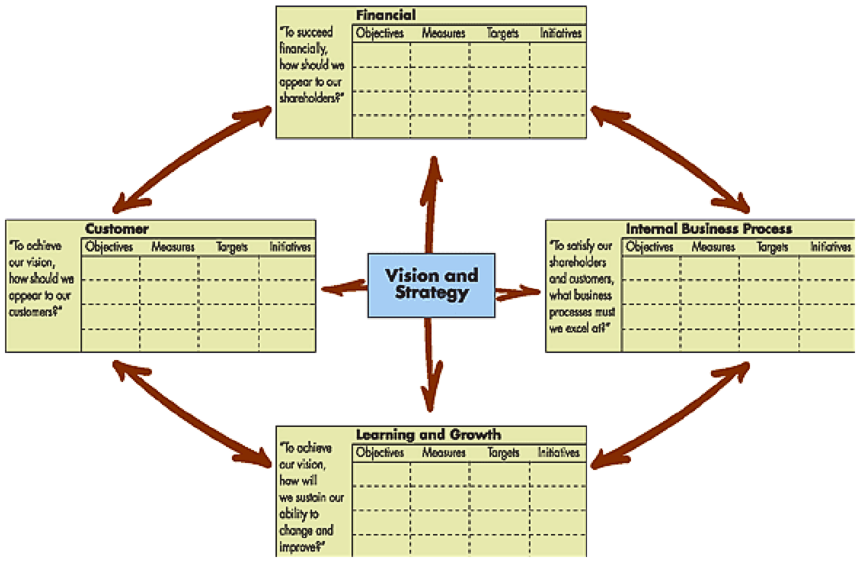
Much research had been conduct to identify the difference between SMEs and large companies. Among all the differences, two main characteristics of SMEs is that the owner plays a central role with a diversity of duties and close uniqueness with workforce, and a mixture of ownership, flexibility, control, and nobility (McKiernan & Morris, 1994[18]) and SMEs also show little separation between an enterprise's strategic thinking and decision-making and an enterprise's formal planning system (Lyles et. al., 1993[19]). This makes SME can be characterized as a simple structure. This structure can be explained in which the owner-manager directs the work of small number of operators with the help of few or no other "manager(s)". Since SMEs management process cannot be separated from the personality and experiences of the key role player (Beaver & Jennings, 2005[20]).

Balance Scorecard

The Balanced Scorecard is a concept developed by Professor Dr. Robert S. Kaplan from Harvard Business School and Dr. David P. Norton in the early 1990s. It first appeared in the article 'The Balanced Scorecard—Measures That Drive Performance' in the Harvard Business Review, in 1992. It started with the phenomenon that there is gradual increase of the inefficiency of traditional financial indicators that been used for years to assess their performance, so the research objective was to measure the ability to define and wealth-creating activities of modern organizations. The Balanced Scorecard approach success to addresses some of the weaknesses and vagueness of previous management approaches. It provides a clear prescription to what organizations should measure. The concept of Balanced Scorecard provide a comprehensive management tool that aims to integrated vision of company performance, in accordance with the financial perspective and non-financial perspectives. The four perspectives foreseen in the model are: (1) Financial; (2) Customers; (3) Internal Process; and (4) Learning and Company Development. Those four perspectives are focus on the critical internal process and activities where priority is given to create a conducive climate to innovation, to change, growth and implement the improvements in order to get a return on investments and shareholder satisfaction together with customers satisfaction and loyalty

The Balance Scorecard concept requires the process of translating strategy into action and turning the company's strategic vision into clear and understandable objectives based on those perspectives. Olve et. al. (1999[21]) suggests four processes to establish this strategic management system: (1) translating the vision; (2) communication and linking; (3) business planning; and (4) feedback and learning. The whole process will helps managers to build a consensus around the company's strategy and express it in terms that can guide action at the local level. Next step is managers need to communicate their strategyup and down the organization and link it to unit and individual goals to enables companies to integrate their business and financial plans. Final step consists of gathering feedback, testing the hypothesis on which strategy was based, and making the necessary adjustments.

Figure 1: The four perspectives of the balanced scorecard



Note: Kaplan & Norton, 1996

Balanced Scorecard to the Management of SMEs

Russo (2006[22]) argues that SMEs in their growing process have distinct company and management needs. When companies are still small, are managed by a leader (usually the owner), with some or no support from managers and with a small number employees. As the company grows and the number of workers increases, the management model becomes inefficient. They need to increase the hierarchical structure. This situation increases the complexity and difficulties in communication and coordination of internal procedures. In this case, the implementation of the Balance Scorecard can make an essential contribution to the development of SMEs by ensuring the strengths of SMEs, which are simplicity, flexibility, and low cost of structure to prevent the complexity increase of the hierarchical structure, and resolving the difficulties of communication and coordination due to their growth.

Intellectual Capital

The New Wealth of Organizations: Intellectual Capital, written by Stewart in 1997, lists many cases to explain the three elements of intellectual capital: human resource capital, structure capital and customer capital. Stewart (1997[23]) argued that IC includes these three types of capital and defined human capital as the sum of innovations, employees' mindsets, seniority, turnover rate, work experiences, and learning ability; structural capital as the existing knowledge efficiently collected, tested, organized and integrated, with irrelevant components sifted out for further diffusion; customer capital as the way a specific organization deals with all relevant parties, which involves the satisfaction, retention rate and loyalty of customers.

Edvinsson & Malone (1997[24]) also held that the intellectual capital included human resource capital, structure capital and customer capital, in which the human resource capital referred to individual abilities, knowledge, skills, and experience of all employees and managers, including company creativity and innovation; structure capital was a kind of supporting structure that could specify and empower human resource capital, including a tangible system that conveyed and stored intellectual materials; customer capital referred to customer satisfaction and loyalty, price sensitivity and financial condition of long-term customer. The same with Abeysekera (2003[25]) which identifies three classes of intellectual capital, those are: human capital, structural capital and relational capital, where intellectual capital refers to intangibles capital which are not recognized in the financial statements.

Another definition of capital intellectual is proposed by Bukh et. al. (2001[26]). It stated that intellectual capital is the aggregate sum of intangible assets which comprise both human and structural capital. Edvinsson (2013[27]) defines intellectual capital as the possession of knowledge, applied experience, company technology, customer relationships, and professional skills that provides a company with a competitive advantage in the market.

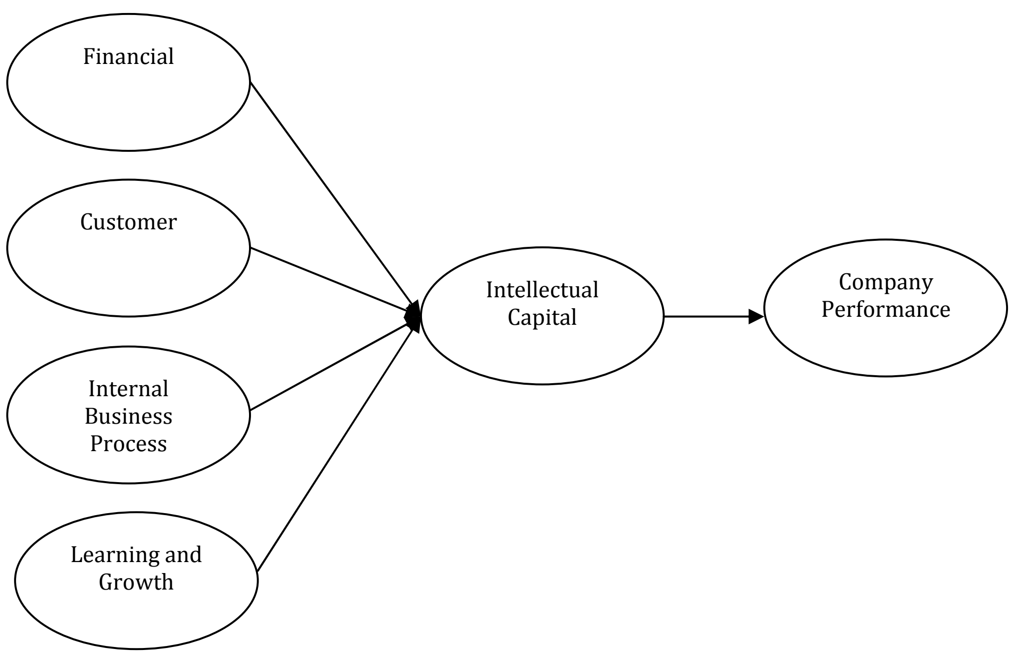
Company Performance

In many years, the concept of company performance had been improved so many times. In the 50's, company performance was defined as the extent to which organizations, viewed as a social system fulfilled their objectives (Georgopoulos & Tannenbaum, 1957[28]), and there for the evaluation process was focused on work, people and company structure. Then, in the 60's and 70's, company performance was defined as an organization's ability to exploit its environment for accessing and using the limited resources (Yuchtman & Seashore, 1967[29]), and there for organizations have begun to explore new ways to evaluate their performance.

The years 80s and 90s were marked by the realization that the identification of company objectives is more complex than initially considered. Managers began to understand that an organization is successful if it accomplishes its goals (effectiveness) using a minimum of resources (efficiency). Thus, company theories that followed supported the idea of an organization that achieves its performance objectives based on the constraints imposed by the limited resources (Lusthaus & Adrien, 1998[30]). In this context, profit became one of the many indicators of performance.

RESEARCH METHOD

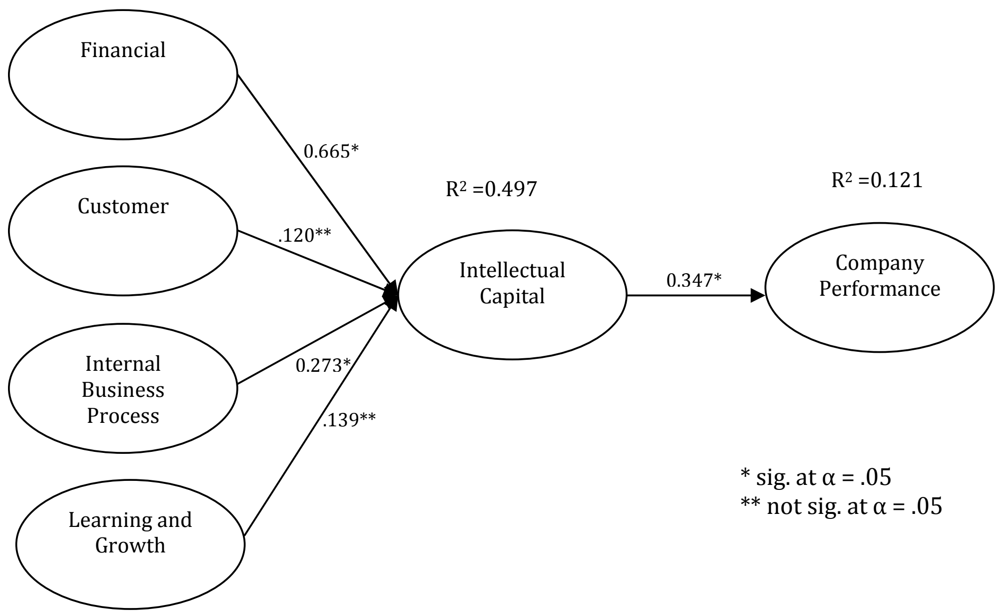
Figure 2: Research Model



The objective of this paper was to investigate the implementation of the BSC in Indonesian MNEs. A survey research design was adopted in order to allow an in-depth and representative analysis to be conducted. Only companies which were already operated for 1 – 2 years; have maximum assets of 50 million and maximum revenue of 300 million per year were included. For each sampled firm one person at the management level, preferably the owner was chosen as the respondent. Semi-structured questionnaires were employed to collect primary data. In total 90 companies agreed to participate.

FINDINGS

Figure 3: Result



Research findings revealed that 49.7% of I Ccan be explained by BSC. While, only two variables from BSC can significantly affect IC, those are: Financial by 0.665 and Internal Business Process by 0.120. In the other hand, 12.1% of Company Performance was explained by IC, which means 77.9% are explained by other factors.

DISCUSSION

Research findings revealed that, though differently, most of the MNEs develop their IC through employees' skills and performance. Even though it done in simple way, most of the owner of MNEs stated that they invest in training and innovation. Most of the MNEs owners also agree that the four perspectives of the BSCare important drivers of a company's success. Most MNEs owners strongly agreed that improvement in one of BSC perspective lead to improvement in the other perspectives, like IC.

The findings also show that the Financial and Internal Business area are the most important factors affected MNEs IC. These are acceptable since most of MNEs are focusing on operational and financial aspects. Performance measurement in

MNEs usually concentrates on financial and short term objectives. Furthermore, operational aspects are very essential for MNEs. When MNEs focus on their Internal Business Process, it will lead to higher efficiency, and by the end improved customer satisfaction and increased market share, which in turn lead toan increase in the company's performance.

Furthermore, establishment of a more flexible measurement (BSC) has allowed MNEs to quickly adapt to a changing environment. But, even though a well-formulated BSC is an important thing to do in order to make sure companies sustainability, strengthening BSC with IC of the companies is an important thing to do.

CONCLUSION

BSC usually take a long time to effect, especially in MNEs. Many forces, such as the departure of key people and change agents,and the costs of maintenance can stall the process of change when still far short of the finish line, which in any case is hard to determine. The BSC is thus arguably never really complete. Rather, because the business environment is dynamic and constantly evolving, an organization's scorecard needs to be constantly re-conceptualized to reflect developments outside the framework. These can include volatile forces such as new competitors and changing customer demands that can affect a firm's strategy. As the business environment changes, current strategies will be challenged and new strategies may need to be formulated. Similarly, the indicators (measures) in the scorecard will need to be reviewed to ensure the indicators continue to reflect strongrelationships with performance.

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