# Benchmarking Small Business Performance: Barriers and Benefits

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## *Abstract*

Benchmarking is now a commonplace term in business and many definitions have been proposed. Despite its increasing popularity there is growing evidence that it is often used incorrectly. 'Benchmarking' seems to be confused with competitive comparison studies, which are simply a component part of benchmarking.

This paper reviews previous benchmarking studies in general, identifying the background to its growth, and benefits and barriers relating specifically to implementation by small businesses. Finally, the paper proposes strategies that can be adopted to make better use of benchmarking for small business.

There are a number of barriers preventing businesses implementing benchmarking processes and the types of barriers may vary with business size. Large businesses have adopted benchmarking in order to gain and maintain competitive advantage. Although large businesses are well placed to take on new quality improvement processes, smaller firms may question their applicability. Previous studies indicate that performance measurement is rarely used by small businesses, as there are many barriers that prevent small businesses from undertaking benchmarking. Some of these barriers relate to lack of time, cost issues, lack of knowledge and poor strategic planning.

Despite these barriers there are many benefits that can be derived from implementing benchmarking programs. Some of these benefits include identification of improved ways to meet customer needs and cost-effective collection of innovative ideas. This paper highlights that benchmarking is a huge and complex task, requiring dedication to ongoing effort and suggests that small businesses may require initial support in order to effectively implement benchmarking as a continuous improvement program.

## *Introduction*

Benchmarking has gained popularity since the 1970's and has become a common component of Total Quality Management programs taken up by large companies. Although small businesses are generally aware of the concept they often shy away from benchmarking because of time and cost issues. Yet benchmarking is appropriate for any business, small or large. Small businesses are faced with unique disadvantages when attempting to benchmark their performance but it is often easier for them to integrate new ideas and processes than larger businesses who tend to be held back by bureaucracy and red tape (Rothman, 1992).

There is also evidence that the term benchmarking is often incorrectly used (Monkhouse, 1995) and is confused with competitive comparison studies. It seems that once aspects of a business are identified, measured and compared against other businesses there is little attempt to take the next step to analyse practices in order to identify performance gaps (Massheder & Finch, 1998).

Most benchmarking in the small business sector is currently undertaken by third party bodies and often focuses too much on gathering information about the achievement of business results rather than about the processes and practices employed to accomplish those results. This paper argues that 'benchmarking' is important to ongoing business improvement and more needs to be done to assist small business to go beyond industry comparison activities. It is suggested that as well as providing industry profiles third party bodies also need to assist businesses to overcome benchmarking barriers in order to monitor and evaluate their own performance, particularly at strategic and global levels and to identify other businesses to establish benchmarking partners.

## *What is Benchmarking?*

### How it Began

The Japanese are given credit for inventing the concept of benchmarking through their practice of sending managers to visit other companies in order to improve their understanding of good business practices. However, Xerox is commonly associated with the development of the modern concept. In 1979 the Xerox Manufacturing Operations began a process of competitive benchmarking in order to combat increasing competition. The company compared their unit manufacturing costs of the copying machines with that of their competitors and used the data collected to identify performance gaps.

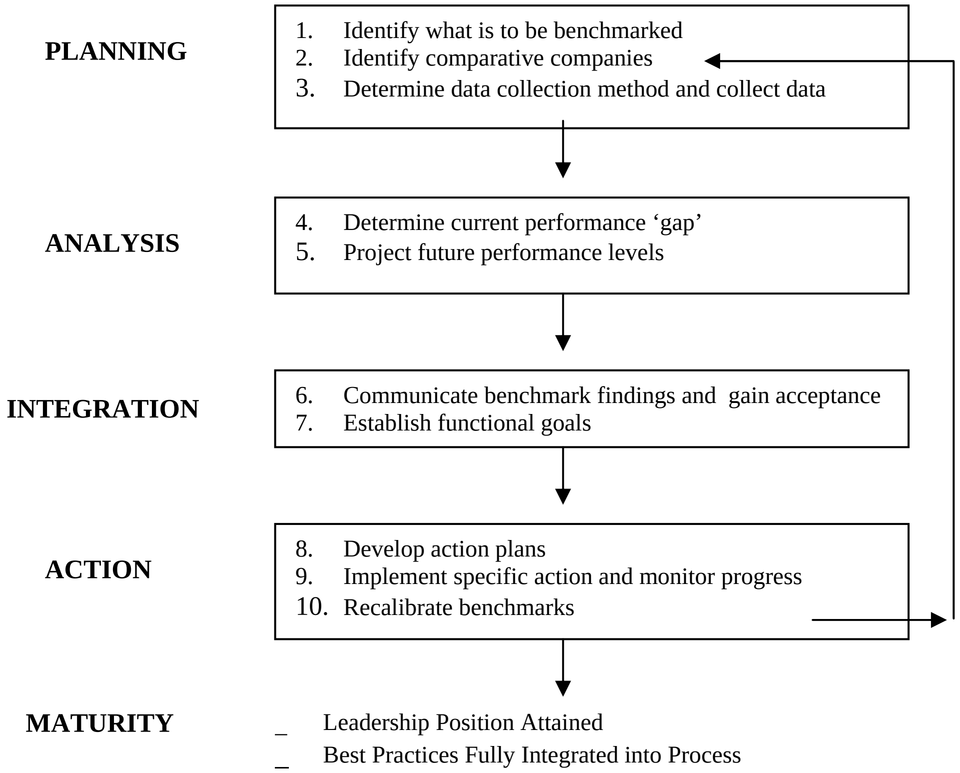
In undertaking this procedure Xerox gained a better understanding of their organisation. The Xerox success story encouraged others to consider the benchmarking process, which is illustrated in figure 1. Two important facets emerged:

1. Benchmarking could be used to better understand any organisation by the identification of common standards of measurement (metrics).
2. Rather than only concentrating on outcomes and products this approach looked at process issues, ie. how the product was produced.

(Massheder & Finch, 1998).

'For benchmarking to be successful, both of these elements are essential. It is impossible to understand why a performance gap exists purely from the metrics. Only the practices or processes on which the metrics are based will reveal why' (Massheder & Finch, 1998, p.2).

**Figure 1.  Xerox's benchmarking process steps**




Source: Camp 1989

**Definition**

Twenty years on we see that 'benchmarking' has become commonplace within business vocabulary. Current definitions for the term also focus on the process aspect and not only the end result:

'The process of benchmarking is more than just a means of gathering data on how well a company performs against others. Benchmarking can be used in a variety of industries – both services and manufacturing. It is also a way of identifying new ideas and new ways of improving processes' (Elmuti, 1998, p. 6).

'Benchmarking is an external focus on internal activities, functions, or operations in order to achieve continuous improvement' (Leibfried & McNair, 1992).

## *The Growth of Benchmarking*

Benchmarking has emerged as a means of gaining and maintaining competitive advantage. In the 1990's benchmarking has become an important and popular business management tool. Ernst and Young and the

American Quality Foundation conducted a study in the US in 1992 and found that 32 per cent of businesses regularly benchmarked their products and services and only 7 per cent reported never having benchmarked. Similarly a study of the UK's top–1,000 companies in 1994 provided evidence that 78 per cent of businesses were using benchmarking practices. These numbers rose to 95 per cent in a follow-up study in 1996 (Ahmed & Rafiq, 1998).

Previous research data suggested 'that managers of smaller organisations have absolutely no hesitation in recognising the potential of benchmarking as a tool for articulating and sharing their vision and for providing individuals with a clear sense of purpose, and a clear sense of what is possible, in their work' (Monkhouse, 1995, p. 47 ). Monkhouse also found that 83% of SME directors interviewed in his study thought benchmarking was worthwhile and 74% thought its use would spread significantly in the near future.

With this unprecedented level of attention comes some concern that 'benchmarking' and 'performance measurement' are being absorbed without a clear and common understanding of what they mean. Misuse, has the potential of destroying the credibility of these processes and negatively impact the gains that could be made. 'The problem is a familiar one: it seems the fate of every new management concept, including total quality management and business process re-engineering, to fall prey to misinterpretation' (Monkhouse, 1995, p. 41).

### *Benchmarking for Small and Large Businesses*

In today's competitive environment businesses cannot afford not to change. Trends towards globalisation dictate that companies need to be highly flexible and outward oriented. 'Benchmarking can be an effective tool for planning and implementing change processes that lead to organisational improvement when the knowledge gained is converted into a detailed action plan to improve competitive advantage' (Voss, Ahlstrom, & Blackmon, 1997, p. 2). Benchmarking can also be used as a goal-setting process, an aid in setting performance objectives to achieve performance improvements (Venetucci, 1992).

Implementing quality management programs can be time consuming and costly, so why do it? According to Smith (cited in Kozak & Rimmington, 1998, p. 185) the benefits of benchmarking include:

- identification of improved ways to meet customer needs
- cost-effective collection of innovative ideas

- identification of the organisation's strengths and weaknesses
- encouragement of continuous improvement processes

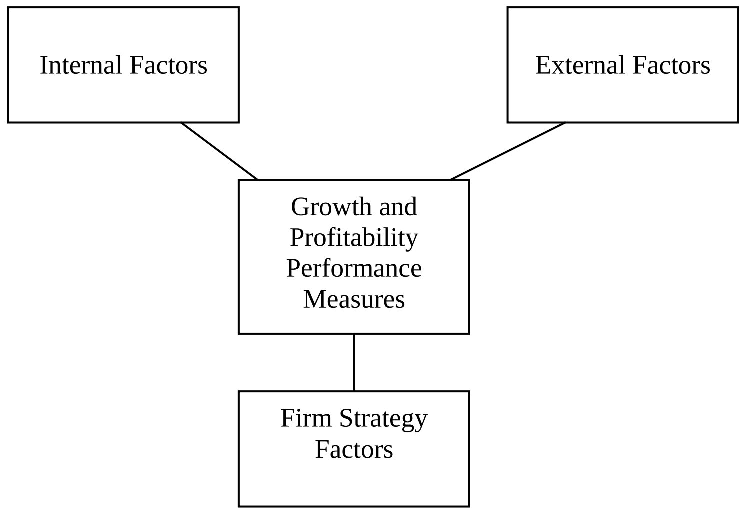
Although large businesses are well placed to take on new quality improvement processes smaller firms may question their applicability. Previous studies (Kozak & Rimmington, 1998; Monkhouse, 1995) indicate that performance measurement is rarely used by small businesses. There are many barriers that prevent small businesses from undertaking benchmarking. Some of these barriers relate to lack of time, cost issues, lack of knowledge and poor strategic planning (Monkhouse, 1995). Other barriers will be discussed in more detail later in this paper.

At present there is little evidence that benchmarking is initiated by individual small businesses. It is significant that the limited examples of benchmarking in small business, as with other quality management programs, are carried out by third parties which include, Government, industry associations and universities (Kozak & Rimmington, 1998). 'Benchmarks, accreditation, best practice and auditing often form part of, or are, industry-led development programs' (Issaverdis, 1999, p. 5).

Close examination of recent studies in this area provides evidence that efforts are being made to assist small business to undertake benchmarking. Mc Namee et al (1999) discuss a competitive analysis model (CAM) which was designed for the strategic development of small businesses. Their model measures performance in terms of growth and profitability and utilises performance measures such as, sales volume growth, employment growth, return on assets, return on sales and profit per employee. They also consider internal, external and firm strategy factors as illustrated in figure 2. However, it could be argued that most small businesses would find such analysis too theoretical and time consuming.

Work by Madu and Kuei, (1998) also attempts to support the implementation of performance improvement in small businesses. Their study is strongly data focussed and details the application of data envelopment analysis (DEA) to benchmarking which uses a linear programming-based approach to compute the efficiency scores for a number of companies.

**Figure 2: The Major Determinants of Performance in the CAM Model**




Source: Mc Namee, Greenan, & Mc Ferran, 1999

These studies have identified, measured and compared various attributes (often financial) of a business against other businesses yet there has been little attempt to take the next step to analyse practices in order to identify performance gaps. These studies tend to be data collection and analysis focussed rather than process driven. Although there is little evidence of the extent of use of the studies on benchmarking for small business Monkhouse (1995) suggested that the studies he reviewed in this area tended to be too theoretical, financially based and too broad and may not be readily taken up by small business.

In general third party studies have tended to be based on tangible performance issues and focus on best practice which has been founded on the success of a small number of large companies. These studies fail to address the needs of small businesses, which rely on intangible resources such as skills, ability to learn, creativity and flexibility (Monkhouse, 1995).

A number of these studies would be better described as sector profiles, competitive comparison analysis or inter-firm comparisons, which take a broad view of businesses in general.

### *Competitive Comparison-Analysis vs Benchmarking*

Competitive Comparison Analysis and benchmarking processes differ. ‘The former gathers information about the result a company achieved while the latter gathers information about how a company achieved those results’ (Smith, Ritter & Tuggle, 1993, p. 43). Specific differences are detailed in Table 1.

**Table 1. Characteristics of Competitive Comparison-Analysis vs Benchmarking**

| **Competitive Comparison- Analysis** | **Benchmarking** |
|---|---|
| Looks at results | Looks at process |
| Checks what happened | Checks how things are done |
| Comparisons with industry | May compare with another industry |
| Research without sharing | Research sharing for mutual gain |
| Always competitive | May not be competitive |
| Secretive | Sharing |
| Separate | Partnership |
| Independent | Cooperative/interdependent |
| Used to check out competition | Used to achieve improvement goals |
| Goal is industry knowledge | Goal is process knowledge |
| Focus on company needs | Focus on needs of customer |

Source: Smith, Ritter & Tuggle, 1993

Benchmarking is a powerful management tool and to be successfully implemented in small businesses should be undertaken in conjunction with the people within the organisation in order to be specific to the needs of that firm.

### *Barriers to Benchmarking*

There are a number of barriers both perceived and real, which prevent businesses implementing benchmarking processes. The types of barriers may vary with business size. Large businesses have taken to benchmarking to gain and maintain competitive advantage. However, small businesses are slower to adopt benchmarking in their own operations.

*Poor Planning and Evaluation*

Small businesses tend to be poor strategic planners and seldom and inconsistently review their business performance (Cassar & Gibson, 1999; Glen & Weerawardena, 1996). Monkhouse (1995) found that SMEs barely use non-financial measures let alone employ more complex and time consuming benchmarking techniques.

*Cost*

Small businesses are also unlikely to be able to employ consultants to assist with the process (Monkhouse, 1995). Cost also prevents smaller businesses from gaining membership to associations who may be pro-active in providing its members with benchmarking data. A study conducted by Mickelwright in 1993 found that expense was one of the most common reasons why small firms were prevented from benchmarking (cited Monkhouse, 1995).

*Lack of Awareness and Understanding*

Lack of understanding about how to go about benchmarking is also a problem. Within the small business sector there are many that feel the establishment of standards is important, but are challenged by the question of how to improve standards (Issaverdis, 1999, p. 7). As stated earlier many owner/managers are confused about what benchmarking actually means and have little understanding of how to utilise available data for business improvement.

*Staff Issues*

Many small businesses are micro businesses, ie employ less than five people. ‘Staff may be required to share a variety of roles including, administration, marketing, financial management and operations management. Such small businesses have limited resources and available time’ (Issaverdis, 1999, p. 5).

*Inability to Source Benchmarking Partners*

Another hurdle is to convince dubious managers of the potential benefits of benchmarking. Small businesses are reluctant to approach competitors for comparative purposes. ‘Perhaps the greatest obstacle blocking benchmarking is the inability of small businesses to easily identify and contact appropriate best-practice companies’ (Rothman, 1992, p.65 ).

*Lack of Accurate Data*

A number of other barriers may be common to both small and large businesses. Ethical aspects of benchmarking raise issues in relation to principles, guidelines and standards that define protocols for interaction. Businesses, understandably, are protective about internal operations and innovations, which make it difficult for third party researchers to collect ‘sensitive data’. This issue is discussed in detail below.

*Poor Skills and Attitude*

Lack of effective communication, fear of change, inadequate training, focus on the numbers not the process, loss of focus on the customer and resistance from employees are also considered to be serious impediments to successful benchmarking (Elmuti, 1998).

These barriers highlight that benchmarking is a huge and complex task, requiring dedication to ongoing effort.

## Benchmarking: Concerns and Issues

Third party bodies, in recent years, have undertaken benchmarking studies to provide data to assist improved business performance. However, these studies have been predominantly financially focussed which raises questions about the accuracy of data collected, given that the data supplied cannot be verified independently and that most businesses are protective about imparting sensitive information. Financial data gives some indication of business performance but without historic information does little to tell us about any improvements. Financial data alone does not assist in identifying gaps in performance.

The data provided in some industry benchmarking studies has been drawn from small sample sizes. In the case of one study the findings were based on the responses of only 25 businesses from Australia and New Zealand. In other studies representation on a state by state basis is sparse and comparisons of businesses are untenable when an entire state is depicted by only one business. The small sample sizes mean that the findings of the studies cannot be generalised beyond the study and so are not necessarily representative of the sector. Based on these limitations it is important to acknowledge that the results can only give an indication of what is happening in some businesses and certainly should not be used to set ‘benchmarks’ for an entire sector.

Industry studies tend to focus on end results and are not process driven. An example of such studies include data provided by the Department of Workplace Relations and Small Business (1997), which provides financial ratios such as turnover per employee and return on assets as an industry average. Although this data provides useful information by informing individual businesses of their performance relative to its competitors it tends to focus on business results rather than individual business processes and does little to provide the information needed to identify performance gaps necessary for business improvement.

### *What is successful benchmarking?*

Ahmed et al (1998) believe that successful benchmarking not only needs to be regular and continuous but also needs to be conducted by the organisation. The key to successful benchmarking is the implementation of improvement strategies and is not mere internal analysis of performance or gathering of information about external best practice or competitors. Benchmarking is part of business improvement processes and not a one-time project (Elmuti & Kathawala, 1997).

Benchmarking procedures should be applied to processes that are critical to the organisation's success. 'A key feature of successful benchmarking is therefore the ability to only benchmark those processes that are critical to the organisation's goals' (Massheder & Finch, 1998, p. 2). Some goals are more easily measured than others. For example, customer satisfaction measurement is less straightforward; however, it is essential that some form of metrics be applied in order to identify performance gaps.

'Benchmarking must be; purposive, externally focused, measurement based, information intensive, objective, and action-generating' (Leibfried & McNair, 1992) and in the long term is best driven by individual businesses rather than third parties.

### *Small Business Benchmarking Needs*

Even if small businesses already appreciate the importance of benchmarking they still have specific needs that should be met before they can successfully introduce new benchmarking measures. Monkhouse (1995) indicated that SME's require access to a range of techniques, which are proven to be flexible enough to cope with the idiosyncrasies of small businesses. Barriers, such as lack of accurate data, confidentiality, high costs and unknown competitors, need to be addressed specifically before the small business sector can fully embrace benchmarking particularly in relation to the use of non-financial indicators.

In order to successfully take on benchmarking small businesses firstly need to be aware of its applicability and importance. Much has been published and promoted about the benefits of benchmarking but little can be achieved unless small business is convinced of the applicability to their business. It is interesting to note that Monkhouse (1995) found many managers of small organisations viewed benchmarking as worthwhile irrespective of whether they were currently involved in the process. It seems that schemes facilitated by external agencies are effective in encouraging the take-up of benchmarking (Ogden, 1998).

External agencies may also initially assist small business managers to gain a thorough understanding of the process in order for them to implement benchmarking as a key part of their continual improvement plans.

It has been found that access to accurate data, both financial and non-financial, on the performance of competitors or similar businesses is a prime need for small businesses. It has been suggested that the establishment of networking partners should provide managers with much needed information for the evaluation and development of business performance.

Lack of management experience in this area highlights the need for the provision of assistance in analysis of data and development of strategies to implement change for improvement. Monkhouse believes that ‘access to a range of techniques, proven to be sufficiently flexible to cope with the idiosyncrasies of small business, will enable them to confidently introduce new benchmarking measures’ (1995, p. 47). Although small businesses face unique disadvantages when benchmarking it is often easier for them to integrate new ideas and processes than it is for lager companies (Rothman, 1992).

## *Conclusion*

It seems that SMEs rarely benchmark beyond informal comparisons, such as, competitor rates and prices. Such informal measures are limited as they do little to help business operators to identify performance gaps and implement improvement strategies. It may be that small business owners either lack management knowledge or are sceptical about performance improvement programs.

A number of small business benchmarking studies have been initiated by third party bodies and not individual businesses. It seems then that the third party bodies are probably the only beneficiaries of these studies. Detailed and / or prescriptive industry standards provided by government or industry associations fail to acknowledge that different activities occur in businesses within the same industry, and what passes for appropriate performance in one workplace may be inappropriate in another. Different business demographics such as, motivation, entrepreneurial characteristics, location and niche markets make it difficult to compare firms in similar sectors.

Performance measures and standards are only meaningful when they are contextualised in particular situations. Prescriptive uniform and behavioural standards only address enterprise needs where there is uniformity between enterprises, thereby limiting their effective use. The provision of standards alone ignores the need to take the next step to assist businesses in analysing their own business practices in order to implement improvement strategies.

We know that identifying, measuring and comparing various business attributes of a business against other businesses is only the first stage of the benchmarking process. So the challenge is to encourage small business managers to do more.

Businesses, particularly small businesses, are generally reluctant to look inward to evaluate performance and look for better ways to do business. However, benchmarking is appropriate for both small and large companies despite the hurdles confronting small business. At this stage it seems that third party groups need to continue to take on the role of investigators and initiators of business improvement programs in order to support and educate managers and staff to combine internal analyses with external studies. Therefore it is important that educational institutions, government and industry associations continue to review research programs in order to find better ways to, not only gather accurate and relevant data, but also to explore appropriate ways to share this information with business and to guide the implementation of the improvement practices uncovered.

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