THE INTERNATIONAL JOURNAL OF BUSINESS & MANAGEMENT

# Strategic Management, Organizational Context and Firm Performance: A Critical Review of the Literature

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***Abstract:***
*Does strategic management have an effect on firm performance and is this affected by the organization's context. This paper seeks to establish the current results of empirical studies on the relationship between strategic management, organizational context and firm performance. The anchoring theories for this review are Contingency Theory, Resource Based View, Dynamic Capabilities Theory and Industrial Organization Theory. From review of the Literature, a conceptual framework emerged, with strategic management as an independent variable, firm performance as a dependent variable, and organizational context as a moderating variable. The components of strategic management include objective setting, defining vision and mission, strategic analysis, strategy formulation and implementation and monitoring and evaluation. Firm performance factors are financial and non-financial indicators. Organizational context factors are public, private and others e.g. environmental factors. From the empirical review of the Literature it was noted that the unresolved issues include divergent views on the link between strategic planning, strategic management and firm performance as results of studies done have not had agreement on the nature of the relationship. It was further noted that there is need to empirically investigate the role of moderating variables e.g. organizational context in the relationship between strategic management and firm performance. The emerging propositions point to the need to ensure a close linkage between strategic management and on-going performance management. There is also a need for leaders to effectively implement strategy and manage performance.*

***Keywords:*** *Strategic management, Organizational context, Firm performance, Strategy*

## 1. Introduction

Strategic management is a broad concept that embraces the entire set of managerial decisions and actions that determine the long run performance of the organization (Koteen, 1989). Poister and Streib (2005) noted that strategic management as being concerned with deciding in advance what an organization will be doing in future (planning) determining who will do it and how it will be done (resource management) monitoring and evaluating ongoing activities and operations (control and evaluation). Strategy is the direction and scope of an organization which achieves advantage for the organization through configuration of resources within a changing environment to meet the needs of markets and to fulfill stakeholder expectations (Johnson and Scholes, 1999).

Organizations operate within different contexts and these affect the managerial contexts which impact on strategic management processes within the organization. Aosa (1996) in his research, noted that the managerial context in Africa is different from that of developed countries. He further noted that there are various contextual factors that influence managerial processes. He noted that there are a broad range of environmental factors that influence managerial processes. These include social, cultural, economic, political and legal, and technology factors.

As firms compete in the market, performance measures become important to assess respective firm's competitive advantage. The key perspectives of performance relate to organizational goal accomplishment and effectiveness and efficiency in resource utilization. Performance indicators include financial e.g. return on investment and gross profit margin and non-financial indicators e.g. market growth, market position and technology efficiency.

Studies that have been done on the relationship between strategy and organization performance have resulted in divergent views on the nature of the relationship between strategy and performance. Greenley (1986) in his study of the relationship in relation to manufacturing companies concluded that data is far from conclusive on establishing a relationship.Arasa and K' Obonyo (2012) performed a study on the relationship between strategic planning and firm performance giving attention to the strategic planning steps. From their study they concluded that correlation analysis results indicated the existence of a strong relationship between strategic planning and firm performance. This paper seeks to establish the current results of empirical studies in the relationship between strategic management, organizational context and firm performance.

The anchoring theories for this study are Contingency Theory, Resource Based View, Dynamic Capabilities Theory and Industrial Organization Theory. The Contingency theory notes that best practices are derived from the contingencies of the situation. The Resource based view focusses on the firm and how the firm is able to utilize its resources for competitive advantage. Dynamic capabilities are concerned with how resource configurations of capabilities by organizations are done with a view to gaining competitive advantage in a dynamic environment.

From review of the Literature, a conceptual framework emerged, with strategic management as an independent variable, firm performance as a dependent variable, and organizational context as a moderating variable. Strategic management has various components. These include setting objectives and goals, determining the organizational vision and mission, environmental analysis, formulating and implementing the strategy and monitoring and evaluating. As highlighted earlier firm performance indicators are both financial and non-financial. The organizational context factors include public, private and others e.g. environmental factors.

From the empirical review of the Literature it was noted that the unresolved issues include divergent views on the link between strategic planning, strategic management and firm performance. This is due to the fact that results of studies done have not had agreement on the nature of the relationship. It was further noted that there is need to empirically investigate the role of moderating variables e.g. organizational context.

The emerging propositions point to the need to ensure a close linkage between strategic management and on-going performance management. This is with a view of ensuring that strategic plans are monitored and evaluated with corrective action being taken based on results. There is also a need for leaders to effectively implement and monitor strategy and review performance results with a view to realigning the strategy where necessary.

## 2. Theoretical Foundation

### *2.1. Introduction*

Theoretical frameworks are explanations about phenomena (Camp, 2001). They are sets of concepts that propose the relationships among these concepts. Theoretical framework is the structure that can hold or support a theory of a research study. A theory includes a set of basic assumptions and axioms as the foundation and the body of the theory is composed of logically interrelated, empirically verifiable prepositions. This paper will be based on contingency theory, resource-based view, dynamic capabilities theory and Industrial organization theory as discussed below.

### *2.2. Contingency Theory*

The Contingency Theory is premised on the fact that the contingencies of a situation determine best practice. It is further noted that a contingency is a relationship between two phenomena. Due to this relationship, conclusions can be drawn in relation to the two phenomena.

Drazin and Van de Ven (1985) noted that central to a structural contingency theory is the proposition that for the organization to survive or to be effective then the structure and process of an organization must fit its context (characteristics of the organization culture, environment, technology, size). They noted that organizational performance depends on the fit between organizational context and structure and process. They noted that there are multiple and conflicting contingencies within which organizations operate. Shepard and Hongland (1978) noted that the contingency view reviews the interrelationships within and among subsystems as well as between the organization and its environment and defines patterns of relationships or configurations of variables. They noted that the contingency view focusses on the multivariate nature of organizations and reviews how organizations operate under varying conditions and in specific circumstances. It is noted that there are internal and external factors that influence the organizational context and ultimately decision making in strategic management. The strategies adopted by the organization are reflected in the organizational performance.

### *2.3. Resource Based Theory*

The resources-based theory (RBT), also known as the resource-based view of the firm is concerned with how firms achieve and sustain competitive advantage over time. Researchers have noted that when firms have resources that are valuable, rare and inimitable and non-substitutable (VRIN attribute) they can achieve sustainable competitive advantage. This is through development and implementation of strategies that cannot be easily duplicated by competing firms. Wernerfelt (1984) noted that resources include brand-names, in-house knowledge of technology, employment of skilled personnel, trade contacts, machinery, efficient procedures and capital. He noted that these resources can result in increased profits.

Focusing exclusively on the resource-based view of strategic alliances, Eisenhardt and Schoonhoven (1996) found essentially that alliances are more likely to be formed when both firms are in vulnerable strategic positions (i.e., in need of resources) or when they are in strong social positions (i.e., possess valuable resources to share). A resource-based theory of strategic alliances focuses on the four components: rationale, formation, structure, and performance. These four components are integral to a general theory of alliances, because they have been the main focus of alliance research.

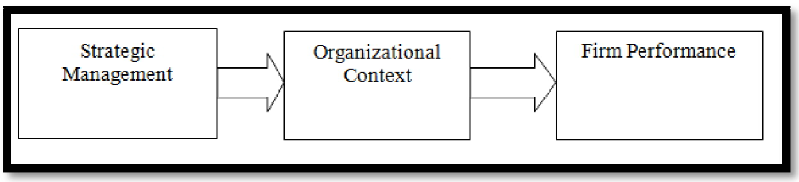


*Figure 1: Schematic of Exposition, (Das and Teng, 2000)*

The resource-based rationale emphasizes value maximization of a firm through pooling and utilizing valuable resources. That is, firms are viewed as attempting to find the optimal resource boundary through which the value of their resources is better realized than through other resource combinations. The argument is that resource integration can be accomplished regardless of industry affiliation (Hennart & Reddy, 1997).

Miller and Shamsie (1996) suggest that, based on the notion of barriers to imitability, classified resources into two broad categories: property-based resources and knowledge-based resources. Property-based resources are legal properties owned by firms and these include physical and human resources and financing capital. Owners enjoy clear property rights to these resources or rights to use the resources, so that others cannot utilize them without the owners' consent. Property-based resources are legally protected through property rights in such forms as patents, contracts, and deeds of ownership (Miller & Shamsie, 1996).

Knowledge-based resources refer to a firm's intangible know-how and skills. Due to knowledge and information barriers these are not easily imitable. Due to their intangible and sometimes ambiguous nature they cannot be easily imitated. These include patents and licenses to reputation and know-how. (Hall, 1992).

### *2.4. Dynamic Capability Theory*

Dynamic capabilities are concerned with the organization capacity to create or modify its ability to integrate and reconfigure internal and external competencies to address rapidly changing environments. The value of dynamic capabilities for competitive advantage lies in the resource configurations they create and not the capabilities themselves as these can be duplicated across firms.

Wang and Ahmed (2007) noted that the emergence of dynamic capabilities has enhanced the Resource Based View by addressing the evolutionary nature of firm resources and capabilities in relation to a dynamic environment and enabling identification of firm or industry specific processes that are crucial to firm evolution.

They noted that dynamic capabilities are a firm's behavioral orientation constantly to integrate, reconfigure, review, and recreate its resources and capabilities and most importantly upgrade and reconstruct its core capabilities in response to the changing environment to attain and sustain competitive advantage. Dynamic capabilities include well known organizational and strategic processes like alliancing and product development whose strategic value lies in their ability to manipulate resources into value creating strategies. (Eisenhardt and Martin, 2000). Dynamic capabilities are promising both in terms of future research potential and as an aid to management endeavoring to gain competitive advantage in increasingly demanding environments. (Teece et al, 1997).

### *2.5. Industrial Organization Economic Theory*

This theory is concerned with how firms compete with each other. It focuses the firm's behavior (conduct strategies) as a determinant of both market structure and firm performance. Hansen and Wernerfelt (1989) noted that Industrial Organization Economics has proven extremely useful to researchers of strategy content in providing a basic theoretical perspective on the influence of market structure on firm strategy and performance. They noted that industry selection and positioning within an industry are important contributors to performance and those economic and organizational effects are independent.

## 3. Strategic Management, Organizational Context and Firm Performance

### *3.1. Strategic Management*

Strategic management is the formulation and implementation of strategies to achieve organization success. It involves defining the mission, vision and goals of an organization, undertaking strategic analysis and strategic choices and implementing the formulated strategies. (Aosa, 2000).

Strategic management involves managing an agency from a strategic perspective and on an ongoing basis to ensure that strategic plans are relevant and that they are effectively driving the management process, Poister and Streib (1999). Strategic Management requires the following: continual monitoring the dynamic environment and tracking external trends and forces that are likely to affect the organization; shaping and communicating to both internal and external stakeholders a clear vision of the type of organization the organizations is striving to become; creating strategic agendas at various levels, and in all parts of the organization and ensuring that they become the driving force in decision-making; and guiding all other management processes in an integrated manner to support and enhance these strategic agendas, Poister and Streib (1999). Strategic management therefore seeks to ensure that the environmental factors, which include opportunities and threats, that affect the operations of the organization are addressed by the organization in its strategic planning and implementation process. Poister and Streib (2005) noted that, over the years conventional strategic planning process has evolved based on approaches developed by Bryson(1995), Nutt and Back off and others (1992) and Koteen (1989), which typically involves clarifying mission and values, defining the organization's vision and analyzing external threats and opportunities, assessing internal strengths and weaknesses and developing strategic goals and objectives, identifying strategic issues, defining strategic choices and developing action plans. The whole process of strategic management has to include monitoring and evaluation to determine whether the strategy is being implemented effectively and to take action where necessary.

Strategic management ensures that a clearly defined strategic plan guides the organization's operations. It also ensures that strategy formulation has taken into account environment factors and that the strategic issues facing the organization have been addressed. Continuous monitoring and evaluation are crucial to ensure prompt detection of any deviations from the formulated strategy so that corrective action can be taken and the strategy be realigned if necessary.

Nerul and Natarajan (2005) traced the evolution of the intellectual structure of the strategic management field during the period 1980-2000. They noted that strategic management has multidisciplinary intellectual linkage. Nerur and Natarajan (2005) noted in their analysis of the period 1980 to 1986 the following five factors: strong influence of organization theory, emergence of distinct strategy school, industrial organization and industrial economics, emphasis on decision making and beginnings of agency theory. Nerur and Natarajan (2005) noted that in the period 1987 to 1993 there was increase in the factors with inclusion of the following: influence of institutional economics, mainstream corporate strategy research with focus on diversification and research on the relationships between firms' attributes and organization environment.

Top management should be familiar with the whole process of strategic management for its implementation to be successful. They should be familiar with the internal and external environment within which the organization operates. (Mintzberg, 1996). It is noted that the environmental analysis is important. The configuration of the firm's resources is also important for effective strategy implementation. This is linked to the Resource Based view of the firm. Management has to choose strategies that are most appropriate to remain competitive in a rapidly changing environment (Muturi, 2011). The strategy formulation and implementation process are important, to benefit the organization and to enhance organization performance.

*3.2. Organizational Context*

The organizational context has various factors which impact strategic management. This in turn affects decision making. It is therefore important to have an understanding of the context of the organization during the strategic management process.

Aosa (1996) noted that in relation to social cultural factors, these related to the people's values, attitudes and beliefs whereas the political and legal factors related to factors related to government controls and regulations. He noted that in relation to infrastructure there was need for adequate infrastructure in order to foster economic growth and in relation to technological factors there was still a skills gap as challenges were faced in understanding technology needs and how to appropriately meet these needs.

There are also contextual factors in relation to the ownership structure of the organization i.e. if the organization is public or privately owned. Bozeman (1987) identified the following variables that encapsulate the extent to which an organization is public or private: ownership, the level of state funding and the degree to which the behavior of managers is constrained by political forces rather than market forces. Boyne and Walker (2010) noted that strategy in the private sector is often viewed as a way of attaining competitive advantage whereas in the public sector strategy is aimed at improved service delivery and performance. They further noted that one of the most important functions of public organizations is to provide services to the public that are efficient, effective and equitable.

It is noted that public organizations are likely to be regulated by the political sponsors that provide their funding (Hood et al. 1999). The regulatory instruments that can be wielded by governments include performance indicators, planning systems, inspections, audits, budgetary controls and annual reports (Ashworth et al., 2002). Such regulatory frameworks are likely to constrain public sector strategy content in two ways: through placing actual limits on strategic decisions and through restricting managerial decision making by public managers (Boyne and Walker, 2004). This therefore can constrain the ability of public sector managers from making strategic choices based on the limitations placed on their operations by the regulatory framework.

Effective and efficient public administration in the age of performance-oriented management requires public agencies to develop a capacity for strategic management (Poister and Streib, 1999). They note that strategic management is concerned with strengthening the long-term viability and effectiveness of public sector organizations in terms of both substantive policy formulation and implementation and management capacity. This highlights the key role of strategic management in effective management of these organizations.

Strategic management integrates all other management processes to provide a unified and effective approach to establishing, monitoring and reviewing an agency's strategic objectives. Given the dynamic environment within which many public agencies operate an effective strategic management capability is essential for maintaining and strengthening the fit between the organization and its external stakeholders and managing for results within a clearly defined context of mission, mandate and vision (Poister and Streib, 1999). Strategic management is therefore influenced by the organizational context as management seeks to ensure effective strategy formulation and implementation.

Vinzant and Vinzant (1996) characterise strategic planning as the cornerstone of strategic management.

Poister and Streib (1999) note that the overall purpose of strategic management is to develop a continuing commitment to the mission and vision of the organization (both internally) and in the authorizing environments, nurture a culture that identifies with and supports the mission and vision, and maintain a clear focus on the organizations strategic agenda throughout all its decision processes and activities.

Poister and Streib (1999) note that strategic management provides a framework that skilled leaders can use to involve stakeholders in creating a vision for the organization, build commitment to strategic objectives and focus organizational resources on advancing the organization's strategic agenda. They conclude by stating that many government agencies have some of the framework in place but relatively few have developed full-fledged strategic management systems that truly integrate all major functions and management processes and direct them towards defining and advancing the organizations' strategic agenda. It is therefore evident that the organizational contexts affect strategic management imperatives in the organization and the related performance. Various factors affect the strategic decision-making process and this is linked to the contextual framework.

### *3.3. Firm Performance*

Performance is geared towards accomplishment of organizational goals. It is viewed in relation to whether the resources are utilized in an efficient and effective way. It is important to clearly understand the organization goals and strategies in order to effectively measure performance. Both financial and non-financial indicators are used to measure performance.

Financial indicators include gross profit margin and return on investment. Return on investment is computed by dividing net income before taxes by the amount invested in the company. Performance of companies listed on the stock markets can be measured using stock market indicators. These include earnings per share, dividends per share and average stock price.

Qualitative indicators include; market position, market share, new products, product service quality, market effectiveness, investment intensity, innovation, manufacturing, productivity and technological efficiency. Market share is the portion of market controlled by a company or product. Market position is a marketing strategy that focusses on making a brand occupy a distinct position relative to the competing brands in the mind of the customer. Johanson and Mattson (2015) noted that the market position is an important concept and that at each point in time the firm has a certain position in the network which characterizes its relations to other firms.

Both quantitative and qualitative indicators of performance should be used in determining the relationship between strategic planning and firm performance as no single measure is adequate to discern strategic performance (Namada, 2011). Poister J.H (2010) observed that there is a need to shift emphasis from performance measurement to a focus on performance management. He notes that performance management is the process of setting goals for an organization and managing to achieve those goals and the desired outcomes.

Beard and Den (1981) noted that from their study that corporate level strategy and business level strategy are important in explaining firm's profitability hence depicting a positive relationship between strategy and firm's performance when profitability was used as an indicator. Leitnem and Goldenberg (2012) noted that Porter (1985) argues that generic strategy has to be followed over a long period of time to pay off and that the choice of generic strategy is a fundamental decision that will not change often. Performance of the firm is important as firms seek to compete effectively within the industry. Organizational performance may be typified as being mutable (composed of different criteria at different life stages), comprehensive (including a multiplicity of dimensions), divergent (relating to different constituencies), transpositive (altering relevant criteria when different levels of analysis are used) and complex (having non-parsimonious relationships among variables).

Organizational performance is important from three perspectives: Theoretically because effectiveness of strategies is tested by the level of performance they cause; empirically because there are many constructs that have been employed to capture performance, and managerially as a measure of quality of decisions that managers make on a day to day basis. Since there are different views on the link between strategic management and firm performance there is a need to do further study on the relationship between strategic management and firm performance considering organizational context.

### *3.4. Strategic Management and Firm Performance*

Strategic management is largely a matter of utilizing and coordinating all of the resources and revenue at top management's disposal in the interest of advancing the strategic agenda (Poister and Van Slyke, 2002). In reviewing the link between strategic management and firm performance it is important to also review what empirical studies have noted in relation to the relationship between strategic planning and firm performance. It is noted that strategic planning is an important component of strategic management. It is noted that the ability of the firm to gain competitive advantage according to Porter (1980; 1985) rests mainly on how well it positions and differentiates itself in an industry. Arasa and K'Obonyo (2012) in their study on the relationship between strategic planning and performance gave attention to the specific steps that make up the strategic planning process. They noted that the manner and extent to which each of the steps is practiced could have implications on the expected strategic planning results. They noted that correlation analysis results indicate the existence of a strong relationship between strategic planning and firm performance when review is done based on the strategic planning steps. They note that all the strategic planning steps (defining firm's corporate purpose, scanning business environment, identification of firm's strategic issues, strategic choice and setting up of implementation, evaluation and control systems) were found to be positively related to company performance.

Miller and Cardinal (1994) in a synthesis of more than two decades of research noted that strategic planning positively affects firm performance. They noted that planning was found to be strongly and positively related to growth in studies in which industries 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. They noted that planning is very positively related to profitability when an informant source of performance data is used, planning is measured without reference to written documentation, the quality of the assessment strategy is high and the environment faced by the firm in a sample are turbulent.

In studying generic strategies and firm performance in Austrian SME's Leitner and Goldenberg (2010) noted that firms with a combination strategy (cost-efficiency and differentiation) will achieve a greater financial performance and growth than those with no strategy. They however noted that there was no empirical evidence that firms SMEs that pursue a cost-efficiency or differentiation strategy (pure strategy) significantly outperform SMEs with no strategy in financial terms. It is noted that Greenley (1986) noted in relation to his study that data is not yet conclusive on establishing a relationship.

It is noted that there is need for further studies on the link between strategic planning, strategic management and firm performance due to the divergent views. It is also noted that there is need to empirically study the iterative process between strategic management and performance management.

*3.5. Strategic Management, Organizational Context and Firm Performance*

Poister and Streib (1999) noted that effective public administration in the age of results-oriented management requires public agencies to develop a capacity for strategic management'. They noted that strategic management is concerned with strengthening the long-term viability and effectiveness of public sector organizations in terms of both substantive policy formulation and implementation and management capacity. They noted that strategic management is an iterative process in which planning generates a strategic agenda that must not only be implemented but also monitored, evaluated and reviewed through continued external and internal monitoring.

Pearce and Robinson (1987)noted that there is empirical support to the value of formalized strategic planning as a means for improving a firm's financial performance. They noted that increased emphasis on formal strategic planning activities appeared to be an effective method of achieving improved financial performance and irrespective of the grand strategy ultimately selected, strategic planning formality was an important factor in organizational performance.

It is noted that there is need for further studies on moderating variables e.g. organizational context.

**4. Summary of Knowledge Gaps**

Strategic management is important for effective management of organizations. Strategic management therefore ought to lead to improved firm performance for the process to be justifiable. However, as revealed in this paper, no consensus has been arrived at among scholars on whether or not there is a systematic relationship between strategic management, organizational context and firm performance. Summary of knowledge gaps identified in the paper are as shown in table 1 below.

| **Author** | **Title** | **Research Gaps** | **Proposed Remedy** |
|---|---|---|---|
| Greenley, G. (1986) | Does Strategic Planning improve Firm Performance | The study noted that the relationship between strategic planning and firm performance is yet to be determined. | There is need to empirically investigate the link between strategic planning, strategic management and firm performance considering the organizational context. |
| Bryson and Roering (2007) | Applying Private-Sector Strategic Planning in the Public Sector. | The study noted the need to research contingent models for public strategic planning. | There is need to empirically investigate contingent models for public strategic planning. The models should specify key situational factors governing use e.g. how collaboration and competition is to be handled. |
| Poister T.H. (2010) | The future of Strategic Planning in the Public Sector: Linking Strategic Management and Performance | This study noted the need to link strategic management and ongoing performance management more closely in a reciprocating relationship. | There is need to empirically investigate the iterative process between strategic management and performance management. |

*Table 1: Summary of Knowledge Gaps Identified in the Paper are as Shown*

**5. Conclusion**

*5.1. Conceptual Framework*

From the empirical review of literature, a conceptual framework has emerged with strategic management as the independent variable while the dependent variable is firm performance and organizational context is the moderating variable.

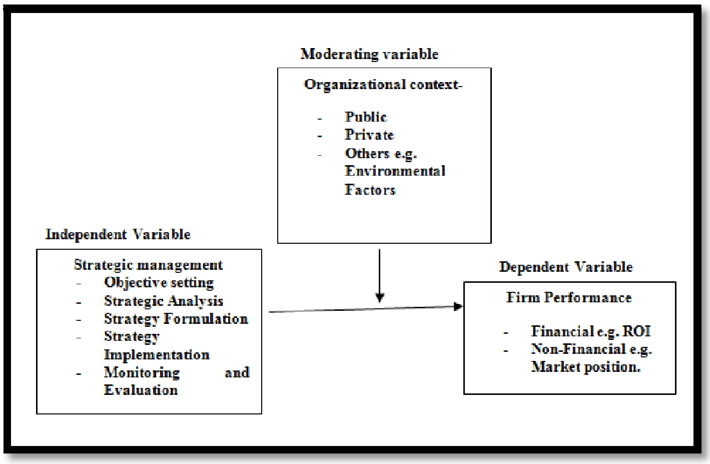


*Figure 2: Conceptual Framework*

*5.2. Emerging Propositions and Areas for Further Research*

From the foregoing there were a number of emerging propositions. Poister TH (2010) noted that there is need for transitioning from strategic planning to the broader process of strategic management, which involves managing an agency's overall strategic agenda on an on-going rather than an episodic basis as well as ensuring that strategies are implemented effectively. He noted that there is also a need to shift emphasis of the performance movement from a principal concern with measurement to the more encompassing process of performance management in order to focus more proactively on achieving strategic goals and objectives. He further noted that organizations will need to link the strategic management and ongoing performance management process more closely in a reciprocating relationship in which strategizing is aimed largely at defining and strengthening overall performance while performance monitoring helps to inform the strategy process. This therefore points to a continuous iterative process between strategic management and performance management.

It is further noted that although various studies have been done on strategic planning and firm performance, not many studies have been done on strategic management and firm performance and the nature of the relationship. It has been noted that contextual factors influence the strategic management process. However, more studies need to be done on how the strategic management context affects the firm's performance. This is a gap for further study.

It is also noted that there have been differing views on the nature of the relationship between strategic planning and firm performance and this is a gap for further study. Some scholars note that results of empirical studies have not been conclusive on the nature of the relationship whereas some scholars indicate that there is a positive relationship.

Poister (2010) observed the crucial need for leaders who are organizational entrepreneurs and who create successful visions for the future, and develop effective strategies for pursuing those visions and efficiently mobilize support both internally and externally for those visions and strategies, but who also fully appreciate the value of efficient and effective management systems and demonstrate a personal commitment to utilize them to implement strategy and manage performance.

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