



STRATEGIC CHOICE, ORGANIZATIONAL LEARNING, TOP MANAGEMENT TEAM PROCESSES AND FIRM PERFORMANCE: A CRITICAL LITERATURE REVIEW

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ABSTRACT

Organizations are in a constant search for ways of distinguishing themselves from rivals and competitors in a bid to outperform them and secure sustained competitive advantage. It has been argued that organizations that will truly excel in the future will be those that discover how to tap people's commitment and develop the capacity to learn at all levels in an organization. The advantage may be seen as resting in the strategic choices that these organizations make including the choice to engage in organizational learning and to ultimately transform into learning organizations. Strategists (TMTs) within a strategic group must share commonalities in determining strategic direction of their firms and in nurturing and deploying resources to realize chosen strategies. It is explicit that organizational outcomes including organizational culture, organizational learning and performance are a function of the strategic choices that organizations make. These strategic choices have been termed by population ecologists as response strategies to environmental opportunities and threats. Other researchers have taken the stance that strategic choices are constrained by the environment in the environment dependence and determinacy framework. It has been separately argued and determined that strategic choices are to a great extent influenced by leadership, goal agreement, the level of cohesion and the collective vision of TMTs. These TMT processes have a bearing on organizational learning and consequently performance. Various conceptual linkages have been identified between the variables of the study. However, these linkages have neither been concretized nor integrated. This paper seeks to verify the conceptual linkages between the variables and to develop a conceptual framework for interrogating the joint influence of Organizational Learning (OL) and TMT processes on the relationship between strategic choices and firm performance.

KEYWORDS: Strategic Choices, TMT Processes, Organizational Learning, Firm Performance.

INTRODUCTION

Organizations that will truly excel in the future will be those that discover how to tap people's commitment and develop the capacity to learn at all levels in an organization (Senge, 1990). Organizational learning theory (Huber, 1991) provides insights on how firms understand and evaluate their environment as well as how they develop capabilities to cope with the environment. Strategic group theorists argue that firms within the same strategic group are similar in their behavior and in their performance as they manage their efforts to maximize the level of joint profit of the group members (Porter, 1979; Oster, 1994). Implicit in this theory is that strategists (top managers) within a strategic group must share commonalities in determining strategic direction of their firms and in nurturing and deploying resources to realize chosen strategies (Pegels et al., 2000). Under these conditions, top managers may possess substantial discretion in determining strategic direction of their firm, and thus the formation of strategic groups are largely the result of strategic choices by top managers rather than by environmental choices (Finkelstein and Hambrick, 1990). The arguments in this conceptual study paper are anchored by a number of prominent theories.

The Upper Echelons Theory (UET) links observable demographic characteristics of top executives to a variety of organizational processes and outcomes (Hambrick and Mason, 1984; Finkelstein and Hambrick, 1996). Strategic choice, organizational learning and performance are underpinned by the Resource Based Theory (RBT) (Helfat and Peteraf, 2003) and the dynamic capabilities theory (Teece et al., 1997). Strategic choice is underpinned by the Industrial Organization (IO) economics theory whose key paradigm is the Structure-Conduct-Performance (SCP) (Mason, 1939; Bain, 1951). IO economics explains environmental determinance in making strategic choices based on industry competition and path dependence in organizational learning while overall industry attractiveness is the basis for superior profitability (Grant, 2001).

Organizational learning (OL) is an area of knowledge within organizational theory that studies models and theories about the way an organization learns and adapts. It is a process by which managers try to increase employees' capabilities in order to better understand and manage the organization and its environment, to accept decisions that increase organizational performance on a continuous basis (Jones, 2000). Organizational learning is underpinned by the knowledge based, dynamic capabilities (DCT) and

organisational development (OD) theories. The knowledge based theory posits that knowledge creation involves developing new content or replacing existing content within the organization's tacit and explicit knowledge (Pentland, 1995) which fosters entrepreneurial and innovative activity while the DCT suggests that private wealth creation in regimes of rapid technological change depends in large measure on honing internal technological, organizational, and managerial processes inside the firm. Organization development theory pays attention to the larger environment in which the business operates and aims at helping businesses accomplish their strategic objectives, in part through organizational alignment with the environment (Putnam, and Bartunek, 2001).

According to the Upper Echelons Theory, leaders are typically confronted with a vast amount of information that demands attention (Mintzberg, 1983). They decide on appropriate responses to important stimuli and discard information that is less important (Weick, 1979) according to their interpretation of the situation, applying their beliefs, knowledge, assumptions and values (Finkelstein and Hambrick, 1990). Those who argue for the predominance of strategic adaptation emphasize the role that managers play in monitoring environmental changes and modifying organizational strategy to better match environmental contingencies (Child, 1972).

Strategic-choice theorists argue that top management teams in firms have substantial discretion in determining the future strategic contour of firms (Pegels et al., 2000). Upper-echelon theorists also argue that top managers are the strategists who set the direction of firms and the pace of competition in the industry. Further, they argue that top management team characteristics are an important element that determines the market niche in which a firm competes and the strategic direction a firm follows. Rooted in strategic choice theory (Child, 1972), upper echelon theorists (Hambrick and Mason, 1984) argue that top managers have a powerful influence over forming and developing the strategic contour of firms and that TMT processes influence strategy-making activities within organizations.

Based on this logic, researchers have investigated the link between TMT characteristics and the behavior of firms such as organizational learning (Bantel and Jackson, 1989), strategic choice (Finkelstein and Hambrick, 1996; Grimm and Smith, 1991; Michel and Hambrick, 1992), and firm performance (Michel and Hambrick, 1992). The strategic choice perspective argues that the analysis of firm strategy must recognize the exercise of choice by

organizational decision makers. The boundaries between an organization and its environment are defined by the kinds of relationships which its decision makers choose to enter (Child, 1972). Researchers have argued that executive change; in particular, change in a company's chief executive and top management team is an important mechanism for overcoming inertia and political resistance (Ocasio, 1993).

Upper-echelon theorists (Hambrick and Mason, 1984) argue that top managers are the strategists in the industry who set the direction of firms and the pace of competition. Further, they argue that top management team characteristics are important elements that determine the market niche in which a firm competes and the strategic direction a firm follows (Finkelstein & Hambrick, 1996).

Some scholars argue that the organization's knowledge and learning capabilities are the main source of its competitive advantage (Kogut and Zander, 1992; Prahalad and Hamel, 1990; Starbuck, 1992). But a number of other authors (Huber, 1991; Walsh and Ungson, 1991) have argued that the literature is fragmented and that these concepts need considerable refinement before they can be of real consequence to practitioners or organizational theorists.

Leroy and Ramanantsoa (1997) define organizational learning as the collective phenomenon of the acquisition, development, and dissemination of knowledge and skills within the organization to positively influence organizational outcomes. This definition underscores the role of organizational learning on shaping firm performance. Such conceptualization sees organizational learning as a significant antecedent of organizational outcomes, such as performance, efficiency, and competitive advantage (Templeton et al., 2002). In fact, it is now a common strategy for companies to use organizational learning both to solve existing problems and to enhance the companies' status in the face of changing conditions (Kim, 2003). Firm performance relates to the efficiency and effectiveness of the firm in converting inputs into outputs (McCann, 2004).

Performance differences in firms are often the subject of academic research and government analysis (Verreynne and Meyer, 2008). The underlying motivation for this kind of research is the quest for those factors that may provide firms with a competitive advantage and hence drive firm profitability (Houthoofd, 2009). One of the major discussions in strategy concerns the determinants of firm performance. Academics from various backgrounds have

focused on explaining firm performance and on identifying the sources of inter-firm performance differences (McGahan and Porter, 1997). Performance measurement includes financial (profit, ROI, market share, EPS) and non-financial measures (balanced scorecard (BSC), sustainable balanced scorecard (SBSC) and profit impact of market share (PIMS)). There is increasing focus on triangulation from multiple measures of multidimensional performance (Richard et al., 2009).

Researchers and practitioners have identified several conceptual linkages between the variables of study. Barker et al., 2001 and Finkelstein and Hambrick, 1996 argue that the relationship between strategic choices and TMTs is reciprocal. TMTs decide on strategic choices which determine organizational outcomes such as performance which in turn determine the fate of TMTs. According to Hambrick and Mason (1984) managers have a great impact on the decisions made in firms and ultimately on the outcomes achieved by firms. Oregon and Ghobadian, 2004 established that particular leadership styles impact profoundly on performance than others. It is evident from the findings that there are conceptual and empirical inconsistencies in the literature regarding the conceptual linkages between the variables. Secondly, these linkages have not been validated into an established paradigm implying that there is room for refinement and concretization of the linkages. This paper seeks to integrate and validate or refute these tentative findings.

LITERATURE REVIEW

Strategic Choices:-

Strategic choices involve the options for strategy in terms of both the directions in which strategy might move and the methods by which strategy might be pursued (Johnson et al., 2008). Strategic decision making requires managers to engage in a variety of cognitively demanding activities. They must assimilate large amounts of information about their own organization, the environments in which they do or might operate, and possible actions of their competitors, allies, and regulators (Bukhszar and Connolly, 1988).

They must generate projections about future states of those matters and formulate plans that will maintain or improve the fit between their organization and its future environment, considering periods of as long as 25 years. The exact mix of activities involved and their relative importance has been the subject of vigorous debate (Miles, 1982; Porter, 1980; Quinn, 1980). Strategic management includes understanding the strategic position of an organization, making strategic choices for the future and managing strategy in action (Johnson et al., 2008).

The strategic choice perspective was originally advanced as a corrective to the view that the way in which organizations are designed and structured is determined by their operational contingencies (Child, 1972). This view overlooked the ways in which the leaders of organizations, whether private or public, were able in practice to influence organizational forms to suit their own preferences (Child, 1997). Strategic choice drew attention to the active role of leading groups who had the power to influence the structures of their organizations through an essentially political process. Miles and Snow (1978) identified three fundamental characteristics of the strategic choice perspective. Managerial or strategic choice is the primary link between the organization and its environment. It focuses on management's ability to create, learn about, and manage the organization's environment; and encompasses the multiple ways that organizations respond to environmental conditions. A number of schools exist within the strategic choice perspective. These schools vary with respect to their conception of the degree and type of deliberateness by which strategies are formed (Mintzberg, 1990). Most strategy scholars have agreed that for specific strategic decisions, there is first a formation, or pre-choice, phase of strategic activity, followed by an evaluation, or post-choice, phase (Fredrickson, 1983).

Such strategies may be conceptualized and measured according to a variety of traditions, notably the comparative (Venkatraman, 1989), and the configurational (Miller, 1996), both of which locate firms along sets of relatively well-established strategic dimensions. The strategic alignment between resources, strategic choices and performance ensures the implementation of the strategy at process level, and gives the opportunity to develop interactively both products and associated processes. This is particularly true in the case of differentiation strategies, where it is needed a good coordination to deliver multiple product characteristics (Chenhall, 2005). Most writers in the area appear to agree, however, that the development of strategic decision-making skill demands experience and the extensive study of earlier strategic decisions through cases and managerial histories as well as through reflection on the manager's own record.

It is the effectiveness of such learning from experience and study that concerned us in the present research. Barker and Duhaime (1997) found that firms change strategies in response to declines in performance. The degree of change depends on the need for change (degree of decline; external events) and the capacity for change (management changes, firm-specific factors;

resources). As such, firm's strategic choices are informed, at least in part, by their past performance (Barker and Duhaime, 1997). Barker et al. (2001) found that high levels of top management team replacements are positively associated with changes in a firm's competitive strategy during turnarounds. Top management team replacements vary with amount of time a strategic orientation has been in place. The relationship between strategic choices and TMTs is reciprocal, TMTs decide on strategic choices which determine organizational outcomes such as performance which in turn determine the fate of TMTs (Barker et al., 2001; Finkelstein and Hambrick, 1996). Competitive strategy consists of complex sequences of strategic choices, actions and responses which influence financial returns of companies (Bettis & Weeks, 1987).

Strategic choice takes place at corporate level, business level or functional level. Corporate level strategy is the desired long-term outcomes that an organization seeks to achieve for its various stakeholders and is concerned with identification of the mission and the vision of the firm (Johnson et al., 2008). The people responsible are the CEOs and the board of directors. Business level strategy is concerned with how the organization competes successfully in a particular market. Functional level strategy is the implementation of an organization's strategic plan and is the work of middle level managers. The focus of this paper is the corporate and business level strategy which is predominantly driven by the Upper Echelons of the organization. This is because the corporate and business level strategies impinge directly on and influence organisational learning, TMT process and firm performance.

Organizational Learning:-

Jones (2000) emphasizes the importance of organizational learning for performance, defining it as a process by which managers try to increase employees' capabilities in order to better understand and manage the organization and its environment, to accept decisions that increase organizational performance on a continuous basis. Snyder and Cummings (1998) contend that learning is defined in a broad sense as the acquisition of new skills and knowledge that results in changed behavior. Scott (2011) defines learning in organizations as a multilevel process whereby members individually and collectively acquire knowledge by acting together and reflecting together.

As that knowledge is captured, spread and embedded in organizational features, such as strategies and protocols, it becomes part of an organizational context,

or code that, in turn, influences what and how groups, communities, and individuals learn. Huber (1991) sees it as a combination of four processes: information acquisition, information distribution, information interpretation and organizational memory. Argyris and Schön (1996) contend that organizational learning emerges when organizations acquire information (knowledge, understandings, know-how, techniques and procedures) of any kind by any means. The dominant paradigm for understanding organizational learning has taken very much from the information-processing perspective of organizations (Cyert and March, 1963). According to it, the organizations interact with the environment constantly to capture information (Hong, 1999).

Learning is emphasized and valued and as such, training and learning are high priorities. Ellinger et al. (2002) found a positive association between organizational learning and firms' financial performance. Hernalux et al. (2008) found a strong, statistically significant, positive relationship between organizational learning and organizational performance. According to them, organizations which develop their learning processes congruently increase their performance. The research also showed that employees' measures are the most strongly related with organizational learning process.

Senge (1990) suggests that the organizations that will truly excel in the future will be those that discover how to tap people's commitment and develop the capacity to learn at all levels in an organization. The literary work identifies the key building blocks of a learning organisation as systems thinking, personal mastery, mental models, building shared vision and team learning. These building blocks are all built and centered on people and processes which implies that learning is a deliberate and active process which we can term as a strategic choice. Whether organisations learn well or poorly is to a greater extent a function of the strategic choices made by TMTs through TMT processes. True proactiveness comes from seeing how we contribute to our own problems. The researchers examine the direct influence of OL on organisational outcomes. This paper seeks to interrogate the influence of organisational learning, which we propose is facilitated through TMT processes, on the relationship between strategic choices and firm performance.

Top Management Team Processes:-

Hambrick and Mason's (1984) upper echelons theory suggests that top managers have a great impact on the decisions made in firms and ultimately on the outcomes achieved by firms. Hambrick and Mason state that the characteristics of the TMT members are

determinants of strategic choices and, through these choices, of organizational performance. Priem et al., (1999) conclude that the upper echelons perspective has been empirically operationalized by researchers measuring demographic differences in the TMT as an explanation of organizational performance.

Hambrick and Cho (1996) found that TMT heterogeneity in functional background, education, and tenure was positively related to a greater propensity of action by the TMT.

Scholars have raised serious criticism of demographics-focused TMT research (Priem et al., 1999; Reger, 1997; Smith et al., 1994). This paper seeks to address this gap by reviewing the role of TMT processes in the determination of organizational outcomes. TMT agreement about other characteristics of the organization, its boundaries, its means of competing, its values, or its strategic decision process may be important as well (Enz and Schwenk, 1993; Falcione and Wilson, 1988; Dess, 1987). Uncertainty reduction theory (Berger, 1979) provides a valuable theoretical basis for explaining the likely relationship between TMT agreement about the strategic decision process and organizational performance.

Firm Performance and Its Measurement:-

A firm's performance may be viewed in terms of the expected customer oriented results and can be measured by the level of customer satisfaction, loyalty, frequency of purchase and repurchase of a firm's products. According to Hofer (1983) performance is a contextual concept associated with the phenomenon being studied. In the context of organizational financial performance, performance is a measure of the change of the financial state of an organization, or the financial outcomes that results from management decisions and the execution of those decisions by members of the organization. Dess and Robinson (1984) posit that regardless of the framework chosen to conceptualize organizational performance, it is apparent that organizational performance is a complex multidimensional phenomenon.

Most studies of organizational performance define performance as a dependent variable and seek to identify variables that produce variation in performance. Thompson (1967) and Schendel and Hatten (1972) suggest that the success of an enterprise seldom depends upon a single factor. Rather, it largely stems from the ability of administrators to reach and maintain a viable balance among a combination of different factors. According to Lenz (1980) empirical studies address particular aspects

of this broad problem of managing multiple dependencies. Financial measures of performance include financial ratios, cash flow or liquidity measures, activity ratios among others. Financial ratios may be calculated in different ways, using different figures (Gibson and Cassar, 2005) and measures include profitability ratios (gross profit, net profit, return on investment, earnings per share), growth in sales, market valuation, total assets, liquidity ratios etc.

According to Kaplan and Norton (1996) a growing number of firms are replacing their financially-based performance measurement and compensation systems with the balanced scorecard, incorporating multiple financial and nonfinancial indicators. Proponents of the balanced scorecard concept contend that this approach provides a powerful means for translating a firm's vision and strategy into a tool that effectively communicates strategic intent and motivates performance against established strategic goals (Kaplan and Norton, 1996).

The BSC main pillars are financial, internal business processes, customer and learning and growth (Kaplan and Norton, 1992; 1996). Based on the notion that firms were responsible for more than just creating economic value, in 1997 the Triple Bottom Line (Elkington,

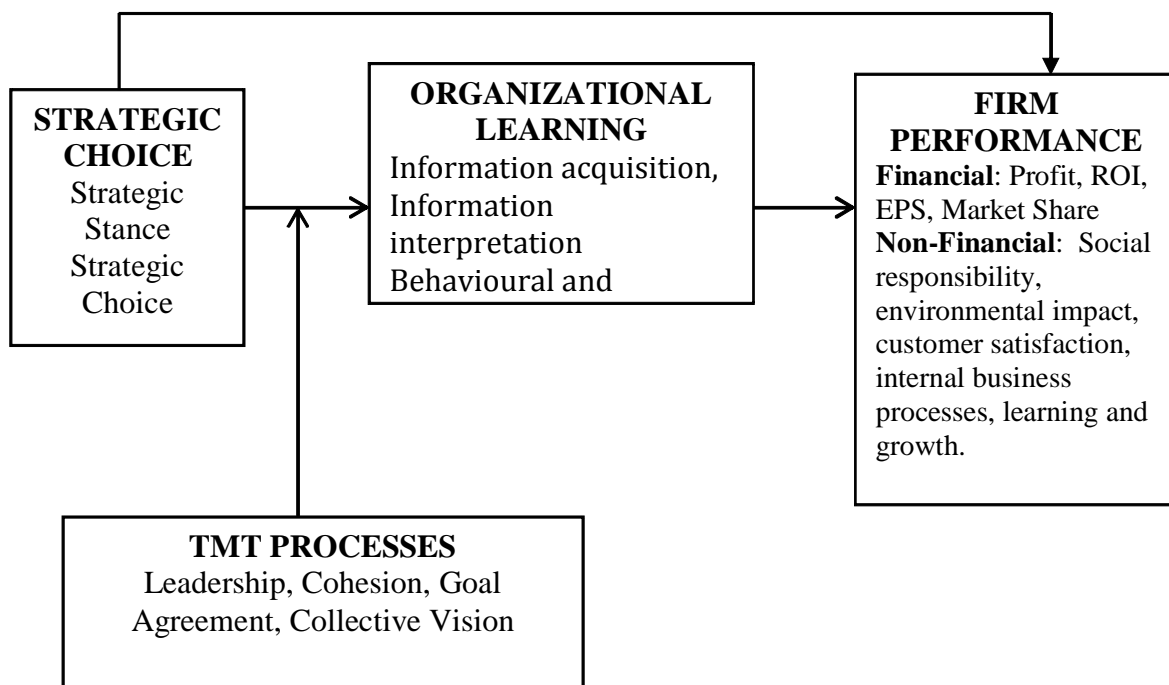
1997) emerged as a new tool for measuring organizational performance which expanded the boundaries of the BSC to cover economic, social and environmental aspects of the organization. This has been translated into the sustainable balanced scorecard (SBSC) which requires companies to contribute to sustainable development by improving corporate performance in all three dimensions of sustainability; economic, environmental and social, simultaneously (Hubard, 2009).

This paper seeks to investigate the effect of OL and TMT processes on the relationship between strategic choices and firm performance taking into account both financial and non-financial variables.

CONCEPTUAL MODEL

The conceptual model represented in Figure 1 below is based on the review and synthesis of extant conceptual and empirical literature. The operationalisation of the independent, intervening, moderating and dependent variables is anchored in the literature. The model suggests the existence of a direct relationship between strategic choices and firm performance based on the literature review. The model also suggests that the relationship between strategic choices and firm performance is jointly influenced by organizational learning and TMT processes.

Figure 1: Conceptual Model



Source: Author (2014)

DISCUSSION AND CONCLUSION

It is apparent from the review of extant literature that there is a relationship between strategic choices and firm performance. A number of scholars have established this link (Child, 1972; Rangone, 1999) explicitly arguing that despite the fact that a number of contingency variables such as environmental determinacy affect strategic choices, strategic choices in themselves are a means to an end. They play a key role in determining organizational performance by acting as a critical link between the organization, its objectives and the external environment. These pro-strategic choice scholars contend that organizational resources may increase the flexibility in strategic choices, by allowing firms to benefit from new opportunities enhancing firm performance. There is near concurrence in the literature that strategic choices in themselves are influenced by the TMTs of the organization but also create path dependencies that influence organization culture including organization learning.

Senge and Nonaka opine that the organization's knowledge and learning capabilities are the main source of its competitive advantage and that in volatile environments the capacity to learn faster than competitors may be the only SCA. From the review of extant literature it can be argued that learning precedes superior sustained performance and is an outcome of deliberate strategic choices by the TMTs. Based on this reason organizational learning is an intermediate outcome based on strategic choices and as such affects the strategic choice-performance relationship. We have established so far that strategic choices including organizational learning are influenced by a number of contingency variables key among them TMT processes.

Hambrick and Mason (1984) argued a strong case for the role of TMTs in shaping organizational outcomes; their upper echelons theory has been tested and empirically validated. Focus by scholars has however been on TMT characteristics, heterogeneity, experience among others. The model developed hopes to fill in this gap by proposing that the relationship between strategic choices and firm performance is affected by organizational learning and TMT processes. This paper proposes a conceptual model which can be adopted to guide empirical research to address the gaps identified and described in this paper. This model is presented in figure 1 above.

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