

A Stakeholder Perspective of Strategy Formation

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Strategy formation traditionally involves the use analytical tools and highly structured processes (Heracleous, 1998; Wilson, 1998; Mintzberg 1994; Porter, 1980). This approach continues to assist in surfacing the ‘wicked’ nature of strategic issues and testing of assumptions in strategy making, (Christensen, 1997; Mason and Mitroff, 1981), however theorists and practitioners in the past decade have identified a shift to more emergent characteristics in the strategy making process combining stakeholder considerations and strategic conversations during strategy formation with select stakeholders (Moss Kanter, 2002; Liedtka 1998a, 1998b; Heracleous, 1998; Christensen, 1997). The first acknowledgements of the approach to consider stakeholder needs in strategy formation date back to Freeman (1984). This paper presents case analysis of field investigations of strategy formation processes on two organizations. In both organizations the principal author facilitated strategy development processes with board members, senior executives and staff. A core theme in the strategy making process for each organization was the strong emphasis on stakeholder considerations in strategic thinking (Ohmae, 1982; Heracleous, 1998; Liedtka 1998a, 1998b) and also in developing strategic plans using emergent practices to supplement traditional planning process in strategy formation (Christensen, 1997; Mintzberg, 1994; Mintzberg and Waters, 1985).

Field of Research: Strategy, Strategy formation, Stakeholder theory, Ethics.

1.0 Introduction:

The principal author was involved in a number of separate consultancies to two organizations from different industries and differing strategic circumstances over the period 2002 to 2005. The aim of the consultancies was to facilitate strategy formation processes towards developing strategic plans for each organization

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The consultancies involved a series of planning sessions to surface up key strategic issues, environmental and industry factors and stakeholder impacts relevant to assessing mission and capabilities for the future. The organizations represent the extremes of Australian economy. Organization A is a small not for profit organization in the psychiatric health care arena and Organization B is a leading Australian forestry company with \$A100 million in market capitalisation

The lead author undertook consultancy roles with these organizations to assist in furthering their strategic development. The authors jointly reviewed the action research data derived from the consultancies to assess the following: Firstly the strategy formation process undertaken in each instance with particular attention to stakeholder considerations in strategy making. Secondly, to analyse the interactions, processes and final strategy development outcomes in terms of planned and emergent processes in strategy making.

1.1 Context of this research on strategy formation

A critical area of focus for these consultancies was the inclusion of stakeholder considerations (Freeman, 1984; Goodpaster, 1991) either through direct involvement of stakeholder groups in the strategy formation process or considering critical stakeholder needs in the strategic conversations within strategic planning sessions. Strategic planning sessions and ensuing contact with key staff were designed to surface up the key strategic issues facing the firm now and into the future and to develop an effective strategy formation process. The strategy formation process followed “a learning by doing” process of strategic conversations (Christensen, 1997. p.141). The aim of this approach was to identify and manage key strategic issues to capitalise on the opportunities present in the firm’s environment, to limit adverse competitive impacts, to identify and develop a collaborative approach to business operations with internal and external stakeholders, and finally build continuing value adding capabilities and to focus operational activities in line with strategy (Christensen, 1997; Dale, 2002, de Wit and Meyer, 2005).

The research paper considers stakeholder theory in connection to strategy formation, particularly in regards to the context of a wider array of internal stakeholders such as board, senior management and employees within the context of the strategic conversations of strategy formation. The paper also considers the connection of external stakeholders with reference to strategy formation particularly in regard to changing emphasis of stakeholder claims and impacts within dynamic strategic environments.

2.0 Literature Review

The past fifty years has seen a number of dramatic changes in the practice of strategy. Gluck Kaufman and Walleck (1980) identify four distinct phases, moving from modest financial planning through a forecast based planning era in the 1960s. These early phases were then followed by, the externally oriented planning approach of the 1970s and finally the more integrated strategic management approach of the 1980s. O'Shannassy (2003) drawing on the key writers on the movement towards strategic thinking, (Heracleous, 1998; Liedtka, 1998a and 1998b; Wilson, 1998; Mintzberg, 1994), identifies a fifth phase in the development of strategy, the strategic thinking phase.

The strategic thinking phase in the evolution of strategy making is characterised by synthetic, divergent and creative thought processes interwoven with analytical, convergent and logical thought (Heracleous, 1998), to more effectively deal with a complex, uncertain and rapidly changing external environment (Quinn, 1978; Mintzberg and Waters, 1985; Stacey, 1993). In working with organizations formulating strategy, the principal author assisted clients to develop strategic thinking approaches and to engage with the emergent aspects of modern strategy making within their industry contexts. Stakeholders featured prominently in the emergent strategy formation process in terms of the level of inclusion of stakeholders in the strategy making process, the impacts of stakeholder needs on the framing of strategy and, finally the impacts of the firm's strategic decisions on various stakeholders.

The modern strategy literature displays a decided move from considering strategy formation as a process to an ongoing practice. Liedtka (1998a; 1998b), following from Mintzberg, (1994), points to a development of strategic thinking throughout the entire organization as a practice; Wilson (1998), commenting on both the constancy and depth of strategic change stemming from the environment points out that strategy can no longer be a "sometime practice" (p. 508). Similarly, Eisenhardt and Brown (1998) suggest that capability in strategic change is now a key business driver with the need for businesses to strategically develop and adapt "relentlessly over time" (p. 788).

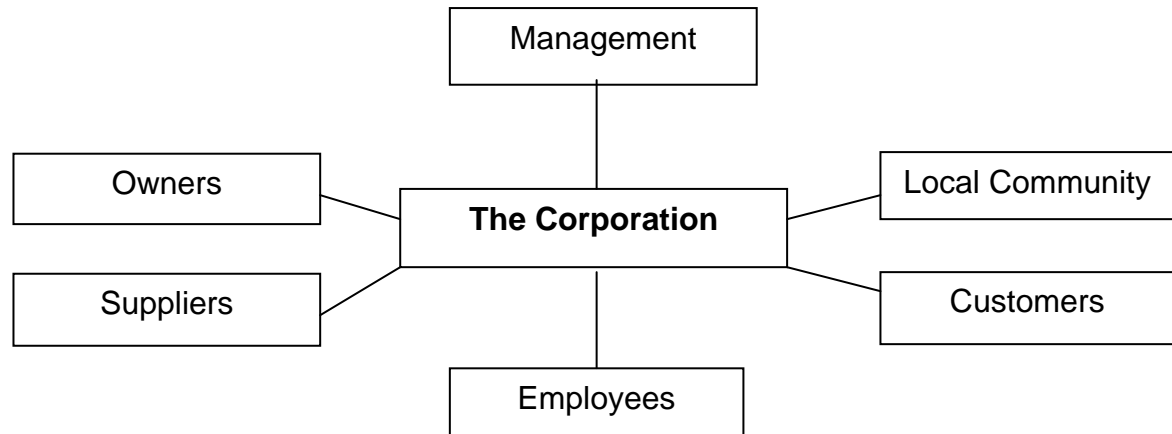
Recent literature supports a shift towards a blend of analysis and intuition (O'Shannassy, 2003; Liedtka, 1998a; 1998b; Heracleous, 1998; Wilson, 1998; Christensen, 1997; Mintzberg, 1994), with some writers suggesting more emergent strategy practices are needed for successful strategy formation. These more emergent strategy practices are needed to effectively deal with the frequent and fast paced disruptions occurring in industries and the general business environment, (Moss Kanter, 2002; Eisenhardt and Brown, 1998; D'Aveni, 1994) and the competitive focus of the more successful companies to proactively shape their environment through their internal capabilities, business offerings and processes, (Miles and Snow, 2003; Miller, Eisenstat and Foote, 2002).

A key issue in modern strategy making is the degree of involvement of stakeholders in the strategy formation process. Mintzberg (1994) identifies

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internal stakeholders including line managers, internal strategy consultants amongst others as having a role to play in strategy formation. Freeman and Reed (1983) identify two definitions of stakeholders. The narrow definition considers those groups vital to the firm's survival and continued success. The broad definition considers any group or individual who can affect or can be affected by the firm. Freeman (1999) argues for a stakeholder theory of the modern corporation discussing the narrow view of immediate stakeholders such as outlined below in figure 1.

Figure 1. A Stakeholder Model of the Corporation (Freeman, 1999)



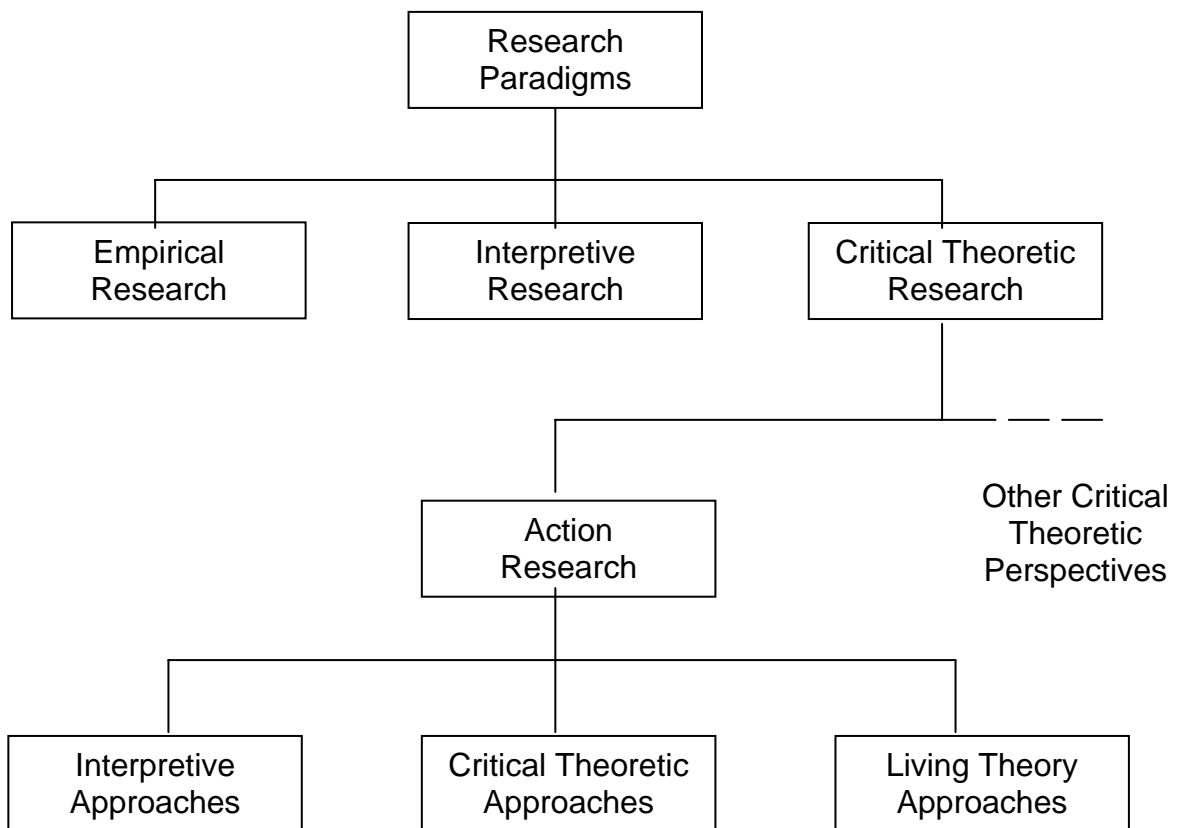
Goodpaster (1991) suggests that stakeholder analysis is the collection of information about the decision options available, the short and long-term implications that must be considered as part of the decision-making process. The stakeholder approach does not seek to overturn the concept of the organization and its obligations; rather it seeks to achieve a balance between the risks and rewards associated with business activity for the greater good (Donaldson, 1999; Donaldson and Preston, 1995).

Building on Freeman (1984) and also Freeman and Evan (1990), Van der Ven and Jeurissen (2005, p. 299) have suggested that the firm itself is a nexus of stakeholders "When we define the responsibilities of a firm in stakeholder terms, we should realize that the firm itself is a nexus of stakeholders. A firm is a co-operative venture for mutual benefit, a coalition of participants (clients, employees, share owners, suppliers), who are all economic stakeholders of each other, and who all depend on the continuity of the firm for their wealth and well-being" Van der Ven and Juriessen (2005, p. 299) further argue that firm survival is 'an important *instrumental* moral goal, in view of the legitimate interests and rights of many stakeholders.' Strategy and the business activities supporting strategy being aimed at the continuity of the firm, should therefore be considered morally justified activities. They conclude that "the continuity of the firm is an important moral value, albeit of an instrumental nature" (Van der Ven and Juriessen, 2005, p. 299).

3.0 Methodology

The methodology applied for this research paper follows a critical theory informed action research approach to develop case study evidence. According to McNiff and Whitehead (2000, 2002) the three approaches to action research sit within an overarching critical theory research paradigm. Mc Niff and Whitehead (2000) indicate action research as one of many approaches under a critical theoretic research paradigm. This relationship is presented in Figure 2 below.

Figure 2. Action research approaches under a critical theoretic paradigm. (Adapted from McNiff & Whitehead, 2000, p. 200).



Consistent with the critical theory perspective, the approach to research undertaken in this project, aspires to achieve the aims of action research methodology as espoused by Carr and Kemmis (1997) to improve and to involve. According to Carr and Kemmis (1997), 'there are two essential aims of action research: to *improve* and to *involve*. Action research aims at improvement in three areas: firstly, the improvement of a *practice*; secondly, the improvement of the *understanding* of the practice by its practitioners; and thirdly, the improvement of the *situation* in which practice takes place' (p. 65). Continuing the theme of understanding of practice through action research, O'Brien (2001) in defining action research indicates an essential characteristic of this research approach, declaring that action research is "learning by doing" (p.3). Action

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research therefore accords with concepts within a modern strategy formation process as learning by doing and crafting strategy (Christensen, 1997; Mintzberg 1987).

Under critical theory informed action research, the authors gathered data from the records of strategic planning sessions, client emails, observation records and research memos maintained in researcher field notes (Zuber-Skerritt, 1991). This rich stream of thick description (Stake, 1995) was developed into case reports as advised by Yin (2003) in addressing descriptive issue of what happened and explanatory issue of how it happened in the manner that it did (Yin, 2004).

The cases conform to Eckstein's (1975) classification of case studies with both cases representing *configurative-idiographic* studies (. In the *configurative-idiographic* study 'material is largely descriptive' representing the pattern of circumstances in the case (Mitchell, 2000, p. 172). According to Mitchell (2000), under this category of case study the account can provide insight into relationships amongst case elements but does 'not lead to direct general theoretical interpretations' (p. 172).

4.0 Case Analyses

4.1 Case Study 1 - Strategy formation in Organization A

Organization A is a small not for profit organization in the psychiatric health arena. The strategic challenges for this organization were around the nature of organisational purpose and the strategic focus needed in determining its client group, client needs and structuring of services.

One of the more interesting aspects of the strategic business planning sessions and discussions with this organization was that the management and employee team and governing board had never worked together on any project. This offered the opportunity for board, management and employees as key stakeholders to see the business from different perspectives. It also offered the possibility to identify common values, the key enablers and distinct barriers to both strategy and operations that existed at the governance level and operational level. It was also an opportunity to move thought and action from an operational focus to a more strategic focus, (Heracleous, 2003; Porter, 1996).

Strategy formation processes for Organization A therefore, aimed to surface assumptions, identify constraints imposed by government grants and regulatory needs, challenge notions of core and peripheral clients in provision of services and access to facilities, determine key external drivers of change and clearly identify the internal value creating capabilities for the future success of the organization. The consideration here accord with a narrow view stakeholder group involved in strategy formation but including the wider stakeholder view in terms of stakeholders impacts and needs considered in the strategic conversations and strategy formation processes. This approach again mirrored a strategy as learning by doing approach (Christensen, 1997). It was largely an

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improvisational approach dealing with emergent strategy drivers within the organization, (Board values and constraints and Management values and constraints) and key strategic drivers for change outside the organization such as State government health departments as a key stakeholder and the wider Church community which supported and underwrote the organizations operations (Moss Kanter, 2002; Eisenhardt and Brown, 1999; Christensen, 1997; Mintzberg and Waters, 1985).

Key results from the strategic planning session were a realisation by the board management and employee group of which services created value regardless of funding and were easily maintained within a tight budget and also which services and activities represented core strategic activities for both funding and consolidating the identity of the organization in provision of psychiatric health care. The approach taken here represented several characteristics of strategic thinking, as espoused by Liedtka (1998a; 1998b). These characteristics included strategic intent and intelligent opportunism (seeking new emergent opportunities as they appear in line with a core strategic direction) and also a hypothesis driven approach to consider 'What if?' scenarios. The strategic business planning sessions therefore were able to present a more holistic approach to developing strategy (Wilson, 1998), and secure strategic insight to types of operations and capabilities that would lead to success for the organization. The sessions and processes resulted in improved levels of focus for the organization, in:

- Limiting activities to core government funded activity and other activities with the greatest client value that involved minimal expense given limited finances. This resulted in greater focus on service delivery to the key client stakeholder group.
- Determining which activities and relationships needed to be discontinued and those that needed further development at both a relationship level and pursuit of alternate funding. This resulted in delimiting service or access to facilities to the wider stakeholders in the community who were not in need of psychiatric support.
- Focusing psychiatric support and services targeted to the client group. The strategic intent of Organization A was reclaimed through revitalizing the core business operations.

4.2 Case Study 2 - Strategy formation in Organization B

Organization B was a leading Australian forestry company with \$A100 million in market capitalisation. There were several challenging strategic issues to consider during the strategy development sessions. Firstly, the company had moved from a private corporation to a listed company on the Australian Stock Exchange (ASX). Secondly, significant pressure was beginning to bear on the company by stock market analysts. These analysts had categorized companies engaged in olive, macadamia and forestry plantations together as a highly speculative investment sector. This meant that all companies were labelled together in an agribusiness industry segment without consideration of previous reputation or differentiation in business model or for that matter any standards maintained in operational performance.

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Taking these issues into account, the nature of the strategic business planning sessions were highly emergent as external forces and events shaped the nature of investment take up by institutional and larger private investors. These investors represented the key stakeholder group emerging from the initial Public Offering (IPO) on the Australian Stock Exchange (ASX). In terms of strategy formation there was a notable focus on an external relations subsystem, (Quinn, 1978), driving discussion and strategic thinking in the sessions. Whereas Quinn in the context of the 1970s discusses a simpler model of government and external activist groups creating forces that shape strategy making, the experience of Organization B was far more complex and convoluted displaying significant interdependence amongst stakeholder groups. These were chiefly, government agencies, multiple stakeholders in the organization's value chain and social and political activist groups interested in forestry related environmental issues. In moving from a private company with limited partner investment to publicly listed company, there was a pronounced shift in the amplitude and scope of stakeholder impacts.

Key stakeholders creating strategic pressure for the organisation included, the Australian Securities and Investment Commission (ASIC), the ASX, a range of stock broking analysts, financial journalists, and institutional investors from investment banking, superannuation funds and insurance funds. These newer stakeholders were gaining levels of influence based on purely economic interests (Freeman, 1999) whereas the previous traditional stakeholders, such as forestry industry growers, loggers, rural communities for which forestry activity was a major economic input and various green groups such as the Australian Conservation Foundation (ACF) were concerned with economic and instrumental connections to the firm (Donaldson and Preston, 1995).

Under private ownership the major stakeholder had been the growers. This represented aspects of the narrow view of stakeholder theory (Freeman, 1999). There had also been some negotiations and involvement with green groups that represented a more broad level view of stakeholder theory stakeholders (Freeman and Reed, 1983). The stakeholder relationship with growers was one of supply. The relationship with the green groups was one of negotiation and advocacy regarding acquisition land for plantation forestry and clearance activity for plantation forest. In such an environment strategy is temporary, complicated and unpredictable with the organization's needs driving strategy with a capacity for strategic foresight, anticipation and coordinated focused actions and stakeholder management providing competitive edge, (Eisenhardt and Sull, 2001; Eisenhardt and Brown, 1999)

In undertaking the strategic planning for Organization B, each meeting produced more discussion and surfacing of external forces and internal characteristics of processes to respond to changing external turbulences (Ansoff, 1990). Mintzberg and Waters (1985) concept of intended strategy and emergent strategy forces to create a realized strategy was particularly consistent as theory reflecting practice in this instance.

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Key events dealt with in the strategy formation process followed a learning by doing model (Christensen, 1997), and included,

- Initial Public Offering (IPO) on the ASX and compliances with ASIC and ASX
- Shift of internal resources focused on pursuit of sales of hard wood forestry tranches to investors.
- Continuing business analyst reports and media stories discussing the speculative nature of this category of agribusiness.
- Responses to missed targets for sales of tranches affecting share prices and further announcements by analysts and financial media
- Image management difficulties in attracting institutional investors
- Realigning Organization B's business systems and practice to align with Principal stakeholder as institutional investor rather than forestry grower as in the past.

The recognition of stakeholder considerations in terms of the narrow view and also the wider view to consider regulators such as ASIC and ASX, business analysts in their work informing the business and wider community of industry and organization performance and also the wider stakeholder set of green environmental groups, was a key activity in strategy formation in Organization B.

As with Organization A strategy formation and strategy implementation for Organization B were seemingly largely intertwined, (Heracleous, 2003; 1998), demonstrating that the organisation had a bias for strategic action and creation of new strategic potentialities through strategic thinking, (Eisenhardt and Brown, 1999; Liedtka, 1998a; 1998b; Ohmae, 1982).

5.0 Discussion – Strategy Formation and Stakeholders

In 1998 Ian Wilson pointed out that the strategic landscape was shifting for all firms as economic environments and industry structures became more complex and also prone to rapid and radical change. 'Radical change, however, of the kind that we are now experiencing, requires a radical rethinking of strategic direction and a transformation of capabilities, production, structure and relationships. ...Andy Grove, the chairman of Intel, argues that virtually every industry now confronts a series of 'strategic inflection points'- crisis moments when the tectonic plates of the business landscape shift.' (Wilson, 1998, p. 508).

Evident from the Case Studies above is the fact that each firm faced strategic inflection points disturbing the business environment, (Wilson, 1998). In terms of each organization, a number of characteristics to a modern approach to strategy formation stand out. Each organization faced an immediate reactionary need to comprehend and strategically think through the environmental challenges impinging upon its business particularly in relation to changing stakeholder needs and accountabilities of each organization to key stakeholder groups.

In the case of Organization A the emphasis shifted from a broad range of vulnerable persons in the broad community to focus on specific funded care and value adding initiatives to those community members with acute psychiatric needs. In the case of Organization B there was a shift in attention and impact to

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investors from a previous emphasis on suppliers. These shifts were consistent with Jensen's (2002) concept of value maximising within stakeholder theory.

Each organization in dealing with a strategic inflection point adopted new insights and behaviours to continue development of a more strategic approach to its business development. These characteristics are consistent with the concept of strategy as continuous, incremental and emerging from chaos as it appears in the strategy literature first commencing in the late 1970s and 1980s with Quinn (1978), thereafter Mintzberg and Waters, (1985) and continuing on with Christensen, (1997), Liedka (1998), Heracleous, (1998), Eisenhardt and Sull (2001), and Moss Kanter (2002), in more recent years.

5.1 Emerging Strategy Formation in Organization A

Organization A demonstrated a similar experience to Organization B in that both board of directors and management were involved in developing strategy. The organisation during the strategic business planning session and ongoing discussions from the sessions began to adopt a very clear pattern of taking the insights from strategic thinking and developing immediate actions to implement changes.

Such was the rapid pace that strategy, operations and the nature of board and management relations were changing continuously towards a more focused business delivery. This adaptation of strategy formation to emergent practice due to pace and depth of external forces and opportunities is consistent with Eisenhardt and Brown, (1999); Wilson, (1998); Liedtka, (1998a) and Christensen, (1997). A keen sense of making the best out of the compliance aspects of state funded psychiatric health delivery and identifying critical value adding services and methods to fund and execute these became critical driving forces to constantly audit strategic activity and stimulate further strategic thinking for further effectiveness of the business.

5.2 Emerging Strategy Formation in Organization B

Organization B from the outset possessed high-level strategic capabilities within its management team. The challenge represented in the organisational investigation above was dealing with strategic change of high impact and wide scope across multiple stakeholder domains. New capabilities and strategic practices needed to be developed in order to focus operations towards new primary stakeholders and key stakeholder interaction requirements. These capabilities would enable the firm to build its reputation and identity as above the rest of the pack in the speculative industry domains that it was perceived as operating within. This approach was consistent with Eisenhardt and Sull, (2001) in developing strategy as simple rules. Boundary, priority and timing rules operated in a continual stream in dealing with new key stakeholder needs and balancing a wider stakeholder set than was previously the case.

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The organization moved to a rapid action orientation and has now succeed in positioning itself well as a listed company and has forward integrated to forestry product manufactured goods to develop further shareholder wealth. For this organisation emergent strategic forces are a continuing business situation. It adopts a strategy as structured chaos approach in a complex industry sector, where timing is critical and organisational actions drive strategy, (Eisenhardt and Brown, 1999)

6.0 Conclusions drawn from the Case analyses

Working with each organization it became apparent to the researcher-facilitator, that nature of industry, cultural characteristics of the organization, and the relationships amongst the executive group created quite individual needs and preferences for planning and emergentness in the process of strategy making. Each organization was moving from a deliberate planning approach to a more emergent planning approach frequently ushered in by significant disruption in its external strategic environment or restructuring of critical internal systems and processes, and sometimes both, (Eisenhardt and Brown, 1999; Wilson, 1998, D'Aveni, 1994).

As a consequence of developing an emergent and incrementalist approach to strategy formation, (Mintzberg and Waters, 1985; Quinn, 1978), the organizations have adopted greater levels of continuing strategic thinking behaviours and practices consistent with a more highly evolved 21st century practice of strategic thinking as continual and holistic throughout organization levels and also greatly focused on a mixture of rapid response and proactivity, (Moss Kanter 2002; Heracleous, 1998, 2002; Eisenhardt and Brown, 1999; Liedtka, 1998a, 1998b)

In terms of stakeholder theory in strategic management (Freeman, 1984) and in particular stakeholder approaches with strategy formation, the involvement of stakeholders such as board of directors, senior management and inclusion of employees as occurred in both case studies affirmed the conceptualization of a convergent view of stakeholder theory (Jones and Wick, 1999). Jones and Wick (1999) suggest a normative theory and instrumental theory convergence under stakeholder theory that mutual collaboration and trust between management and stakeholders leads to competitive advantage. As both firms A and B have prospered through collaboration and trust with internal stakeholders and focused on the needs of their respective key external stakeholders more fully the convergent theory based on collaboration and trust would appear to hold true under both case studies.

Specific conclusions drawn from the case study analyses relevant to insights on strategy formation under stakeholder theory:

- Stakeholder considerations were a prominent component of the strategy formation process.

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- The impact of stakeholder considerations ranged from a base level of acknowledgement of interest and impact to levels of involvement in the strategy formation process.
- Strategic thinking involved in shaping modern strategic business plans was both analytical and creative in nature within the two organizations (O'Shannassy, 2003; Heracleous, 1998).
- As evidenced from the case analyses strategy formation can accord to a *learning by doing process* (Christensen, 1997), as mental models of strategy and strategy formulating practice are challenged (Senge, 1990).
- Based upon the case analyses strategy formation still largely follows a planned and emergent process as identified by Mintzberg and Waters, (1985) with stakeholder considerations acting as key aspects of emergent strategy to affect the course of any deliberate strategy to become the pattern of actions in a final realised strategy.
- A modern 21st century strategy formation process can consider stakeholder needs and impacts through sophisticated processes such as thinking in time and intelligent opportunism (Liedtka, 1998a; 1998b) that are underpinned by double loop learning processes to challenge prevailing perceptions and assumptions (Heracleous, 1998; Argyris, 1985).

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