

AN EXAMINATION OF THE EFFECT OF STRATEGIC PLANNING AND ECONOMIC DEVELOPMENT ON
U.S. LOCAL GOVERNMENT FINANCIAL PERFORMANCE

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Abstract

This paper examines how U.S. local governments use strategic planning and economic development and its effect on financial performance. The research consists of three parts: (1) a purposive sample of local government mayors/city managers, (2) a telephone survey of finance officer, and (3) a review of strategic plans and economic development policy. Face-to-face interviews were held with selected International City/County (ICMA) member local government managers to gather qualitative data on the planning and economic development relationship. The data reported in this paper is taken from a larger study of the relationship between strategic planning and financial performance in U.S. local governments. The findings have important policy implications because they provide evidence that local government strategic planning and economic development, when used in concert with comprehensive planning and the capital budget, may have a positive effect on financial performance.

INTRODUCTION

This paper examines how strategic planning, and economic development is used in U.S. local governments and its effect on financial performance. Local governments, like private and not-for-profit organizations, are facing the need to adapt to dynamic environmental change. The demand for high quality government services continues to grow as citizens' expectations about the quality and value of those services rise. Managers of U.S. local governments are increasingly under pressure to provide more and better quality services. They are being asked to accomplish this from a static or diminishing tax revenue base. Additionally, public interest in government performance has grown, driven in large part by taxpayers concern over the perceived value they receive from the taxes they pay (Beckett-Camarata, 1998).

Some local governments have successfully adapted to the dynamic changes in the environment with some success. Las Vegas, for example, is one of the fastest growing cities in the United States yet it has no major manufacturing plants and is not the home to dot.com companies. Some cities, not as large as Las Vegas, are growing because of a focus on economic development. Certain cities have been astute in economic development in housing, sports and entertainment complexes, making core city areas more interesting and habitable. Many small and medium size local governments have capitalized on the electronic era to become major players in the new economy. Resourceful small local governments have installed optic cable, developed partnerships with local colleges and universities and redeveloped their airports to pave the way for economic development.

Strategically managing all available local government resources efficiently and effectively will determine the financial viability and economic future of all local governments. Efficiency is

defined as value created in relation to productivity (Karlof, 1993). In economic terms, the concept of efficiency can be summarized as a question: what is the least-cost combination of inputs that will produce a given level of output? A local government will be viewed as efficient if its quality and quantity of services and goods are relatively high in comparison to similar organizations' outputs. However, the meaning of effectiveness depends on the definition of the term. Generally, effectiveness is defined as doing the right things (Bedeian and Zammuto, 1990, p. 61). Efficiency and effectiveness are complementary, but they are not interchangeable. An organization can be effective and not be efficient. Similarly, it can be efficient without being effective. For purposes of this paper, effectiveness is defined as the extent to which an organization attains its goals (Reddin, 1970, p. 3). Financial goals are defined as:

A sub set of corporate goals for which management can be held accountable, and which is concerned with the financial condition and performance of the corporate entity and with the related decisions and actions of management involving the acquisition, custody and disposition of corporate funds (Donaldson and Lorsch, 1983, p.35).

RESOURCE USE TO PROMOTE ECONOMIC EFFICIENCY

The emergence of any organization or organizational sub-unit, such as an Economic Development Office, influences the economic structure in which it is embedded as that structure shapes resource use decisions. The formal and informal constraints and incentives that accompany the organization's structure, policies and procedures collectively make up the institutional context that molds and shapes the institutional matrix and how that organization goes about shaping resources from its external environment (North, 1990). An institution's policy of funding economic development through the capital budget process is an example of a resource allocation decision

context created by the institution to formalize and support the institution (Barlett and Mohammed, 1995).

The trend toward the use of strategic planning in U.S. local and regional governments is increasing. Fifty seven percent of local governments surveyed in 1998 indicated that they use strategic planning citywide (Beckett-Camarata, 1998). Streib and Poister found in a 1990 study of local governments that only 26 percent used strategic planning citywide (Streib and Poister, 1990). At the same time, financial problems exist in many U.S. local and regional governments. These financial problems are caused by many circumstances. Four significant influences are: (1) eroding property tax bases, (2) rising expectations about local and regional government services, (3) dynamic changes in the American economy and, (4) globalization. Some local and regional governments have been successful in using selected private sector management tools such as strategic planning and economic development to deal with these individual circumstances. Yet, "there is a general level at which management is management, whether federal, state, local or regional and management techniques such as strategic planning and economic development can take on similar meanings in different settings" (Beckett-Camarata, 1998, p. 170).

Economic development in the U.S. has a long history and the trend has been increasing toward use of this tool as well. With the dynamic changes in the U.S. economy, local government officials have been responding to economic changes with a wide array of policies to enhance the economic well being of their communities. As a result, there has been increased competition among local governments to implement policies that give them a competitive advantage in attracting development and thereby enhancing their local tax base (Bowman, 1986). This competition has in turn fostered a growing literature that examines approaches to economic development activities of local governments.

Over the last several years, substantial research has also been conducted regarding strategic planning. A number of local and regional governments have used strategic planning as a management tool. They have also used economic development. Local economic development incentive techniques such as tax increment financing may influence urban economic growth and development directly by attracting new industries, facilitating the maintenance or expansion of existing operations, and encouraging more intensive land use. They may also affect economic development more indirectly by enhancing the overall business climate of a locality (Feiock, 1991).

The purpose of this paper is to explore:

- (1) local government 's use of strategic planning and economic development,
- (2) the effect of strategic planning and economic development have an effect on financial performance,
- (3) what institutional restructuring, if any, is necessary to effectively use both strategic planning and economic development,
- (4) what are the implications for public policy outcomes

Strategic Planning Use

Seasons (1989) examined the relationship between strategic planning and economic development in the Canadian City of Kitchener, Ontario. Seasons recognized the role of uncertainty in planning. He also recognized that accepting uncertainty can be the beginning of effectively planning and taking adequate actions in the face of the unknown and unknowable (Goldberg 1986, p. 4 in Seasons, 1989). Seasons drew on Mitroff and Mason (1981, p. 13) to stress the policy-making implications of planning in a complex environment. Seasons' research suggested that local government economic development would benefit from the application of strategic planning principles, practices and processes. He states "To achieve staff and departmental ownership of the process, future strategic economic development plans must evolve in-house. This

application of strategic, economic development planning indicates that a successful planning process draws from theory and experience in both the public and private sectors" (Seasons, 1989, p. 310). Seasons study also concluded that private sector strategic planning principles and practices have considerable applicability in the public sector, especially at the local level. Seasons found that strategic planning is an effective monitoring and evaluation component and is essential in that it identifies and incorporates change in the strategy making and implementation process.

Economic Development Use

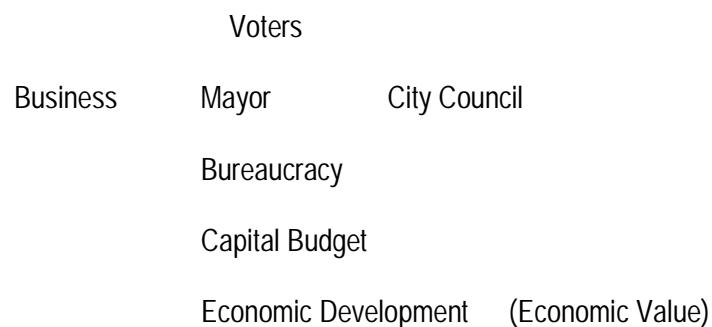
Case studies on the use of economic development report that revenue generated from new investment attracted by local economic development policy does not generally outweigh the revenues forgone by governments using these incentives. These studies are, however, often based on a narrow definition of economic policy benefits such as jobs or tax revenue created by the companies to which the incentives were aimed (Pascarella and Raymond 1982). McDonald (1983) argues that governments derive benefits from development policies even if the businesses that locate in that jurisdiction would have done so without the inducement.

There are approximately 15,000 to 18,000 organizations in the United States devoted to the promotion of local economic growth (Levy, 1990). They appear in many forms, governmental and quasi-governmental agencies, nonprofit corporations, and local development corporations. They range in size from chambers of commerce, with minimal budgets and no paid staff, to development corporations with large staffs and multi-million dollar budgets.

Some local governments consider economic development as a regular responsibility of government that should be incorporated into its organization structure. As such, an economic

development department is a very important part of the local government organizational arrangement. The following figure depicts an example of an economic development department in a medium size local government.

Institutional Model of Economic Development



Local economic development is an intensely competitive activity. Whether the economic development organization is attempting to bring in a firm or encourage an expansion, it is in competition with a very large number of other local governments. In any case it is the competition to attract firms or the competition between communities for a limited amount of development funding. The economic developer exists in a world just as competitive as that of the firms that are being sought after.

The justification for local economic development is that it is needed for reducing unemployment and poverty. Economic development is premised on that fact that people are less mobile than capital. If individuals were as mobile as capital, the loss of an industry would be followed by out-migration of workers and their dependents, preventing the unemployment rate from rising and the wage rate from falling. Conversely, the opening of a new industry would draw

enough workers to prevent the unemployment rate from falling and wage rates from rising. But perfect mobility is not the case. The population adjusts only slowly to economic change.

The full set of regulations, tax policies, public works and local government program expenditures is framed with long term economic development strategies in mind. A strategic view of planning at the local government level places economic development specialists at the focal point of capital budgets, tax policies and expenditure patterns. A strategic planning approach to economic development incorporates the strategic plan, the capital budget, and economic development in order to positively affect financial outcomes.

Capital Budgeting and Economic Development

Forrester concluded in his examination of municipal capital budgeting that new research is needed to find out how capital budgeting facilitates economic development in local governments (Forrester, 1993). He found that the process in local governments is more restricted to players within institutions, with limited targeted participation by the public and other external actors. Capital budgeting is important since it is generally regarded as a way of carrying out long-term capital spending plans to facilitate economic growth (Matson, 1976; McLain, 1981; ICMA, 1984, Doss, 1987; Fernandez and Laberge, 1986). The effectiveness of capital budgeting is shaped by the design of the program.

According to Forrester, to the extent that the capital budget is based in planning and economic theory, a government should use the capital budget to implement its economic development program and the development program should be directed by a central institution (Forrester, 1993). For the capital budget to be effective and contribute to economic development,

authority over final capital decisions may have to be strategically centralized. The coordinating entity must be viewed as accountable and legitimate and have a diverse set of skills and perspectives. Green and Fleischmann (1989 in Forrester, 1993) found that cities that have centralized responsibility for economic development activities are more likely to have a plan for guiding economic development. Centralization may expedite coordination of activities, symbolize to business that the local government is serious about economic development, enhance accountability, and facilitate “political credit-claiming.” (Green and Fleischman, 1989).

A Preliminary Strategic Planning-Financial Performance Model (Figure 1) shows the hypothesized connection between strategic planning, economic development and financial performance. The level of analysis used in the model is financial performance. The choice of the strategy level focus provides for a potentially tight linkage between the strategy process, economic development use and its outcome. This tight ordering is necessary in light of the many exogenous effects on performance (Pearce *et al.*, 1987). The particular use of strategic planning and economic development by the local government determines not only financial performance outcomes but also influences external stakeholders' assessments of local government financial performance outcomes.

Preliminary Strategic Planning-Economic Development Model

Strategic Planning

Schedule/Timeframe			
Mission Statement			
Environmental Scan			
Goals & Objectives	Capital	Economic	Financial
Action Plans	Budget	Development	Performance
Plan>One Year			
Evaluation Criteria			
Financial Plan			
>One Year			

1. Strategic Planning was measured by the use of a written plan which includes (a) a schedule/time frame, (b) a mission statement, (c) an environmental assessment, (d) goals

and objectives, (e) action plans, (f) plan for more than one year, (g) evaluation criteria, (h) a financial plan, and (i) period of time plan covers.

2. Capital Budget was measured by the presence and use of a capital budget.
3. Economic development was measured by the presence and use of written economic development policies.
4. Financial Performance outcomes were measured by (a) Bond Rating (BR), (b) Long-term Debt Per Capita (LTD), (c) General Fund Balance Per Capita (GFB), or (d) Own Source Revenue Per Capita (OSR).

How local governments use Strategic Planning and Economic Development

In order to determine how local governments used strategic planning and economic development, face-to-face interviews were conducted from a purposive sample of local government managers who are members of ICMA. A purposive sample is a non-probability sample chosen because they are representative of others in the field on a subject matter (Kalton, 1984). This sample was selected specifically based on (1) their availability and (2) their experience in local government administration. The local governments were stratified by section of the country and then as to whether or not they use strategic planning. The local governments were sorted according to local government Bond Rating, Long-term Debt Per Capita, Own Source Revenue Per Capita and General Fund Balance Per Capita. An analysis of this matrix with respect to these variables suggested the formation of two financial performance groups (i.e., high performance and low performance) on the basis of split halves (i.e., a median split on each of these variables). Based on the above actions, the four local governments selected were: (1) Elizabeth, New Jersey, (2) Kent County, Delaware. (3) Warwick, Rhode Island, and (4) Portsmouth, Virginia. Portsmouth, Virginia, and Warwick, Rhode Island, indicated in a mail survey that they do strategic planning; Elizabeth,

New Jersey, and Kent County, Delaware, indicated in a mail survey that they do not do strategic planning.

The objectives of the interviews were to gather additional qualitative data on (1) the strategic planning process used in the local government, (2) the use of economic development, and (3) the differences in financial performance. The interviews were also conducted to examine whether there were coordinated and integrated strategic planning and economic development approaches and the degree to which each local government actually used their strategic plans.

How Elizabeth New Jersey uses Strategic Planning and Economic Development

The first city described is Elizabeth, New Jersey. A face-to-face interview was held with the mayor of the City of Elizabeth, New Jersey. The Mayor was previously a member of City Council. He indicated that the city's strategic vision is growth through economic development, housing and education. The City does not have a written strategic plan, but rather the strategic plan is the Mayor's informal articulated agenda for the city's future. The informal agenda includes a written economic development strategy that has been implemented through Elizabeth's comprehensive plan. Examples of strategy implementation are Elizabeth's use of economic development strategy to award a contract to develop underutilized land for a shopping center and to eliminate and replace antiquated public housing.

The Mayor indicated that the City Council is not per se involved in agenda setting since they are strictly a legislative body. As such, the Mayor provides the leadership. The City Council in Elizabeth functions purely as a legislative policy setting body, working through the Mayor. The Mayor in Elizabeth is responsible for the management activities, such as strategic planning and economic development. Thus, the Mayor is the key individual to articulate and implement the

strategic agenda for the City. The comprehensive (master) plan is connected to the capital budget. The comprehensive (master) plan is not linked to the informal agenda. The Mayor's Agenda in effect is in the Strategic Plan for Elizabeth and serves as its formal planning mechanism. The city has had somewhat high financial performance.

How Kent County Delaware Uses Strategic Planning and Economic Development

The second local government selected for interview was Kent County, Delaware. Kent County uses comprehensive planning, in lieu of strategic planning, in conjunction with zero-based budgeting. Short-term goals and objectives are selected and are incorporated into the comprehensive plan. The County Administrator meets with the Governor of Delaware each year and reports on the results of their comprehensive short-term goals and objectives. The county manages its financial performance based on a short-term plan as opposed to a strategic plan. The focus on short-term financial management limits the county's use of capital budgeting and economic development policy and by implication, its use of long-term debt. The county's financial performance was somewhat low.

How Warwick Rhode Island Uses Strategic Planning and Economic Development

The third city examined is Warwick Rhode Island. A face-to-face interview was held with the Mayor of Warwick, Rhode Island. Warwick has used a combination of strategic planning and comprehensive planning for several years. The State of Rhode Island had mandated that local

governments have a written Comprehensive Plan beginning in 1991. The city uses line item budgeting. The Mayor indicated he views planning as very important and that he incorporates financial planning into strategy development. He used, as an example, Warwick's planning for the development of its airport. The Mayor indicated that the city ties economic development strategy into the strategic planning process. As a result, the mayor uses such strategies as transportation planning to open up the community and to expand economic development. The strategies are implemented through the comprehensive plan.

The Mayor felt that it is important for the city of Warwick to have such a strategic vision because the mayor is elected every two years and the strategic vision helps them keep continuity. He indicated that city of Warwick's approach to financial management is very conservative. Since the city council is not involved in strategy development, strategy implementation often becomes the subject of debate, resulting in budget discussions becoming opportunities for issues to coalesce around political rather than substantive strategic issue debate. While the Mayor incorporates a financial plan into the city's strategic planning, strategic management issues often are politically debated. This results in the city's strategy implementation becoming rather informal. The city has had somewhat high financial performance.

How the City of Portsmouth Virginia uses Strategic Planning and Economic Development

The fourth city examined was Portsmouth Virginia. The City of Portsmouth Virginia uses a two-tiered approach to planning. They use a written strategic plan called the 2005 Plan as their strategy; the comprehensive plan is the tactical plan for carrying out the 2005 Plan. The comprehensive plan is seen as a community plan, while the 2005 plan is seen as a blending of the organizational plan and the community plan for economic development. The city uses a team-based

approach to budgeting. In this local government, the citizens in the community work out their differences through the comprehensive planning process; the council and city management work out their differences through the strategic planning process. Both plans are then integrated. The Vision 2005 document is the strategic vision for the city. The comprehensive plan is the mechanism for implementation of the strategic vision. The City Manager includes state agencies in the strategic plan development. The City Manager indicated that Portsmouth uses the planning process to balance general fund revenue and expenditures. Long-term Debt is managed by adjusting reserves (fund balances). However, the City Manager indicated that since city council is very involved in the strategy development process, involving the council in strategy implementation is a smooth process since the council has been a part of the strategy development process. Thus, the city council appears to have a vested interest in the strategic planning outcomes. The strategic plan is implemented through the comprehensive plan and economic development is connected to the capital budget process. The strategic plan appears to be actively used and it was confirmed that action plans in the Comprehensive Plan are a reflection of the Strategic Plan. Portsmouth has had somewhat low financial performance.

Telephone Survey

All four of the local government finance officers indicated that strategic planning had a positive impact on economic development. Overall, these results do not differ from the face-to-face interviews in any significant way and lend further support to the importance of the use of strategic planning and economic development in influencing financial performance.

With the use of Wilks criterion, two of the four dependent variables, General Fund Balance and Bond Rating, were not significantly affected by Strategic Planning, Comprehensive Planning or Capital Improvements Planning. The Wilks criterion results did show a modest but significant association between the Capital Budget and General Fund Balance.

Table
Strategic Planning by Comprehensive Planning

	Value	F	Hyp.DF	ErrorDF	Sig.
Pillai's Trace	.192	1.456	8	110	.182
Wilks' Lambda	.811	1.488	8	108	.170
Hotelling's trace	.229	1.518	8	106	.159
Roy's largest root	.213	2.928	4	55	.029

Summary

In conducting the face-to-face interviews, several distinctive findings emerged. First, regarding strategic planning, the face-to-face interviews did determine that the three of the four local governments are doing strategic planning. Second, the interviews also established that strategic planning is being used to develop specific strategic planning strategies such as economic development, housing and education. Third, the interviews affirmed that having a written plan does influence the use of local government strategic planning use. One very interesting finding from the interviews was that one of the two local governments who said it does not do strategic planning (their plan is not in writing) does in fact do informal strategic planning. It is just that the strategic plan is called the agenda, which also served as the local governments mission statement. Closer examination of the local government's documents revealed that the city had done an environmental

analysis. However, while using some elements of the strategic planning process, they did not have a consistent, formal strategic planning process in place.

Three of the four local governments interviewed had written goals and objectives. However, the one local government that claimed that it does not do strategic planning had goals and objectives, but those goals and objectives were tactical, not strategic. Of the two local governments that do not do strategic planning, one local government manager indicated that the city council was purely legislative-policy making and not involved in the planning process. Another local government manager indicated that the council (or state government in Delaware) was very involved in planning. Two of the local governments that had a written strategic plan that included goals and objectives could articulate the actual use of the strategic plan in managing economic development. When used correctly, carefully monitored, actively supported by management, and tied to planning, goal setting can improve performance (Ivancevich and Metteson, 1993).

In examining the use of economic development by the four selected local governments, several unexpected findings were made. First, the local government's economic development plans are incomplete. For example, only one had a financial plan that is linked to the economic development policy document. Second, only one of the local governments that responded that they do strategic planning has a schedule/time frame for economic development planning.

In examining the use of strategic planning and economic development, strategic planning is being used to develop specific strategic planning strategies such as economic development, housing and education, but the implementation varies depending on how strategic planning is used.

Does the use of Strategic Planning and Economic Development have an effect on financial performance?

When interpreting the financial performance of the local governments that do strategic planning and have economic development policies, the findings are complicated and somewhat inconclusive. It does appear from the interviews and financial reports that strategic management of certain financial variables, General Fund Balance Per Capita and Long-term Debt Per Capita, can be accomplished through connecting the capital budget and the comprehensive plan to strategic planning and economic development.

Evidence from the face-to-face interviews suggests that local government strategic planning is, in fact, used in concert with the comprehensive plan and capital budgeting and economic development. It appears that local government managers use comprehensive planning for economic development strategy implementation and that strategic planning and comprehensive planning can be used jointly. This finding also supports the use of comprehensive planning and strategic planning reported by King and Johnson (1995) in their case study of the use of planning by Oak Ridge, Tennessee. In that study, King and Johnson found that strategic planning and comprehensive planning are not mutually exclusive, but rather can be successfully blended.

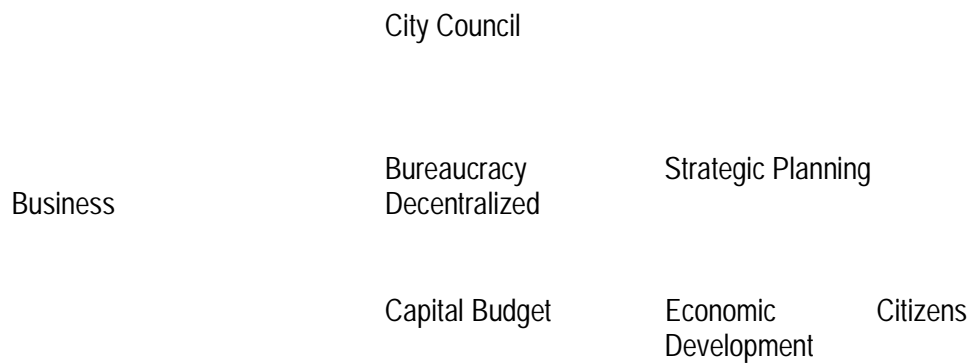
Local government managers are using different planning approaches for different purposes. They use comprehensive planning as the long-term plan for economic development, and the capital budget as the tactical plan for detailing the strategic resource requirements to support the comprehensive (master) plan. They also are using strategic planning to integrate and bring the planning approaches (such as the comprehensive plan) into harmony. The Mayor of the City of Warwick, Rhode Island, for example, uses such a coordinated approach.

Final Planning-Economic Development Model

Schedule/Timeframe	Comprehensive	Economic Development
Mission Statement	Plan	
Environmental Scan		
Goals & Objectives		<u>Financial Performance</u>
Action Plans	Capital	General Fund Balance
Plan>One Year	Budget	Debt
Evaluation Criteria		
Financial Plan		
>One Year		

INSTITUTIONAL RESTRUCTURING NECESSARY TO EFFECTIVELY USE BOTH STRATEGIC PLANNING AND ECONOMIC DEVELOPMENT

Combination–City Council, Business, Bureaucracy-
Capital Budget-Economic Development



The literature suggests that business models such as strategic planning can be interpreted generically and applied to government agencies (Bryson, 1995). Additionally, there has been a heightened interest in applying such private sector models in the public sector because the traditional lines of distinction between the public and private sectors are blurring. The blurring of the public/private boundaries means that local governments are entering a business world in which

no one organization or institution is fully in charge; and yet, many are involved or affected or have a partial responsibility to act (Bryson, 1995)

This is in part because public managers are judged by different performance criteria than are private managers (Allison, 1971). This is because the private sector planning process benefits from the centralized function of general management across the entire organization, while in local government the general management functions tend to be split or spread among a number of competing interest groups and individuals depending on the level of planning. For example, when strategic planning is focused on a local government organization level, it is quite likely that most of the key decision makers will be insiders and it will be easier to get staff together to decide important issues, reconcile differences and coordinate implementation. When strategic planning is focused on a task which crosses local government organizational boundaries or a community level, almost all the key decision makers will be outsiders and it may be more difficult to organize strategic planning and economic development in such a shared environment.

IMPLICATIONS FOR POLICY

Because both strategic planning and economic development are complex, iterative processes, and they both require time to develop. When the process of planning strategically for economic development is done in a coordinated manner, capacity is built into the structure. A shared vision is critical as a reference point. But a shared vision is not developed quickly or easily and it too is iterative (Schaeffer and Loveridge, 2000). Building community capacity through strategic planning and economic development has the potential to change communities as well as the market for community services. A tight connection between strategic planning and economic

development can accomplish more than each individually permits. Regardless of whether the lead organization is public or private, effective economic development must be a combination of planning and budgeting for resources. Information is imperfect and having both strategic planning and capital budgeting in the economic development process is an effective combination of resources.

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