

**HOW TO GOVERN GENERIC  
MARKETING ORGANIZATIONS**

**With special focus on National Tourism Organizations (NTOs)**

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## **Abstract**

The purpose of this thesis is to investigate various governance alternatives for National Tourism Organizations (NTOs), and how they can be used to create positive incentives and working conditions for NTOs. An ideal governance scenario can enhance NTOs' market orientation, allow NTOs to adopt a long-term planning perspective, and give NTOs operational freedom to work on their required tasks. We believe these aspects will have significant importance for NTOs' market performance and the performance of the tourism industry NTOs promote.

Based on the analyses of a 14-country survey including NTO, NTA, and industry representatives; researchers and consultants; along with a comprehensive theory review, we have attempted to make policy recommendations that we think will be usable for both NTOs and National Tourist Authorities/Administrations (NTAs). We are quite confident that these recommendations will be of interest for the formation of tourism policy in most OECD countries, and other countries interested in these issues.

We have also included some suggestions for further research on NTO governance and for similar organizations and settings.

## **Preface**

The international travel and tourism market is a market with an impressive growth over the past few decades, providing much valued profits, employment, tax revenue, and investments for many countries. At the same time the international tourism market is a volatile market with increasing competition among countries and regions. Thus, efficient and effective use of the National Tourism Organizations' (NTOs') resources is of utmost importance for countries that have ambitions to perform well, and reach other important goals of the organization and its stakeholders.

In this thesis we<sup>1</sup> will discuss how governing stakeholders (i.e., the government and the tourism industry) can provide NTOs with the right incentives and working conditions to make NTOs become as effective and efficient as possible. First of all, since NTOs are in fact marketing organizations, we believe NTOs need to be market-oriented and have a *market focus*. Secondly, NTOs need a *long-term perspective* to be able and willing to engage in long-term planning, projects and activities. Lastly, NTOs need some degree of *operational freedom*, allowing NTOs to craft their own professional strategies and carry out activities without undue intervention and pressure from stakeholders and interest groups.

In this thesis we will argue theoretically, as well as provide some empirical evidence that *how NTOs' budgets are determined* (activity/behavior-based); from *which source NTOs are financed* (industry vs. government); and *who owns/controls NTOs* (government vs. industry/stockholder); will have an impact on these incentives and working conditions. These are important premises for NTO operation that can be designed to set the stage for improved market performance of NTOs.

Personally, I would specifically like to thank my colleagues Professor Sigurd Villads Troye and Associate Professor Einar Breivik. They have both made strong effort with the initial project this thesis is based on, and I truly appreciate their help and guidance along the way with the thesis work. In addition, I would also like to thank Associate Professor Erik W. Jakobsen at the Norwegian School of Management for his useful comments and suggestions, and Eric Lofquist for help with proofreading the text.

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**Bergen, October 2003**

**Eivind Farstad**

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<sup>1</sup> In this thesis the author will, for the most, part use the plural noun "we" since some parts of thesis contains contributions of my colleagues involved with the original OECD-project this thesis is built on.

*This thesis is dedicated to my parents Aagot and Einar*

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## **1.0 Introduction**

In this chapter we will describe the background of the thesis and the research context, state the research questions, explain our research approach, and provide an overview of the thesis.

### **1.1 National Tourism Organizations<sup>12</sup>**

Almost every nation in the world has a national organization officially responsible for tourism marketing, often operated as a part of the national government or as a special independent body created by a legislative act. These are often referred to as National Tourism Organizations (or Offices) (NTOs). Generally, these organizations play a leadership role for tourism in their respective countries; drawing together fragmented pieces of the industry and the often loosely coordinated national, regional, and local government bodies. According to one source (Choi, 1993) there are about 175 NTOs worldwide, employing between 500-700 branch offices abroad.

National Tourism Organizations are set up in virtually every country in the world that has a tourism industry of any significance. The NTOs' main roles are to market their nations abroad as tourist destinations in order to attract international visitors. Many of these NTOs have both international and domestic responsibilities in tourism policy, planning, development, and international marketing. These activities often require substantial budgets, several of them surpassing 100 million Euros in budget size, and have large staffs. For instance, the Greek NTO maintains a staff of more than 750 full-time employees. NTOs are traditionally organized and controlled by the national government through a department or ministry responsible for tourism matters, often referred to as the National Tourism Authority (NTA).

NTOs are in many regards similar to other non-profit organizations in other industries formed to market or promote an industry, business interest, or cause on behalf of an industry or group of businesses. Some other examples of such similar entities are national marketing organizations for the export of seafood (Norway), kiwi or wool products (New Zealand); or domestic industry marketing organizations for meat, poultry, or dairy products (Norway, USA etc).

NTOs' main purpose is to market their country's travel industry's products and services, and facilitate the sale of these to incoming tourists. Considering that NTOs are first of all *marketing organizations*, it is beneficial for the tourism industry and other involved stakeholders that NTOs spend the majority of their resources in the most efficient and effective way to *market their country as a tourist destination* in order to attract

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<sup>1</sup> Adapted from Morison, Braunlich, Kamaruddin, and Cai (1995).

<sup>2</sup> Adapted from: "Towards New Forms of Public-Private Sector Partnership – The Changing Role, Structure, and Activities of National Tourism Administrations". *World Tourism Organization - Special Report*, January 1996.

international tourists<sup>3</sup>. Ideally, one would want to avoid a situation like the case of the World Health Organization, which is an international organization formed to promote worldwide health. For the WHO, 35% of the budget goes to supporting the organization's headquarters, and another 40% to running regional offices. The remaining funds are then leaving only one and a half cent (0.015 US\$) for health per person in the various targeted regions (Peabody, 1995). In the case of NTOs, one would want to avoid that resources are wasted on excessive administration, lobbying activity, and justification efforts rather than productive tourism marketing effort. It is therefore crucial that the bulk of NTOs' resources are spent on tourism marketing, and not on supporting the internal operation of the NTOs and other non-productive activities.

Paradoxically, at the same time when governments' recognition of tourism's importance to national economies is probably at an all-time high, many governments are questioning the rationale for their continued involvement in tourism. This is particularly the case in Europe and North-America.

Given the increasing constraints on public sector budgets generally, governments are concerned about how they can continue to justify the use of taxpayers' money to support and promote tourism when there has generally been a decline in support for such funding in other industries.

A number of countries are also concerned that the effects of governments assuming a promotion and marketing role – one which in other industries has been seen as a private sector responsibility – may be a misallocation of government funds. Moreover, they admit that it can also result in a marketing organization (NTO) that is less responsive, efficient and entrepreneurial than it should be.

As a result, tourism administrations are looking more and more to the private sector to take on some of the promotion and marketing functions traditionally assumed by the government, usually in some kind of partnership with the public sector. Consequently, it is quite possible that a larger portion of the budget of the NTOs will have to be funded by the private sector in the future. This generally results in private enterprises having a greater say in the development of the NTAs' tourism policy and NTOs' operational strategies, as well as how NTOs' budget funds are spent.

Shifting the responsibility for funding and control of the NTO, more from the government towards the tourism industry, could have some desirable, as well as, unwanted consequences. Despite the great responsibility and considerable size of the budgets of many NTOs, they have not been subject to much academic research to date, especially with respect to their international operations as well as the governance of them. As Choi (1993) has pointed out, very few studies have attempted to analyze NTOs and

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<sup>3</sup> Some NTO are also marketing the country's tourism industry to domestic tourists to retain this business within the country. These activities are also beneficial for the country's domestic tourism industry, and can be considered "favorable" from an NTO efficiency and effectiveness standpoint. NTOs have also have roles and tasks in addition to promotion and marketing in general, but international marketing is their most important activity. See also Table 3.2 in Chapter 3 for a more comprehensive overview of typical NTO activities and goals.

their operating environment in particular. Even fewer, if any, have studied the different funding- and control principles used for NTOs and their potential consequences.

## 1.2 The purpose and focus of the thesis

The research problem we study in this thesis stems from our casual observations of a few NTOs and how they seem to behave and operate in the real world. For instance, these observations were made through direct contact with NTOs, through news media features, promotional material and other information from the NTOs themselves, as well as presentations regarding NTO matters on business seminars and academic conferences.

It is important to emphasize that NTOs are first of all *marketing* organizations. They are operating in an environment where they market products and services that face competition in the marketplace from e.g., other NTOs and commercial tourism marketers. Let us for now and for the sake of argument assume that the NTOs are operating in a competitive environment, where organizations need to be truly concerned about efficiency and effectiveness to survive and prosper in such an environment. Under such circumstances one could maybe expect that a typical NTO would strive to be market-focused, e.g., focusing on market research and adapting the organization and the products it promotes to the tourism market, and move swiftly to counter the actions of any market competitors or competing destinations. They could also be expected to engage in both the kind of short-term, as well as long-term, plans and activities needed to have success in a competitive market. Moreover, they would be expected to craft their own strategies relatively autonomously based on their supposedly unique professional expertise. It is then puzzling to observe that some NTOs do not seem to be particularly market-focused, and their planning- and activity-level seems to be mainly of more short-term character. Furthermore, some of the NTOs we have observed also appeared to be somewhat focally oriented towards their sponsors and owners and their products and agendas, and prone to spend time, money, and other resources on lobbying and justification efforts. That is, many NTOs seem to have a *product-, owner-, or sponsor focus* rather than a *market focus*. At the same time some NTOs are complaining about the restrictions put on them by these sponsors and owners - which again are hampering NTOs' abilities to do what they consider optimal from a business perspective. These observations do not correspond well with our expectations of an ideal NTO as being market-focused, have a long-term perspective, and autonomous and dislodged enough from its owners and sponsors to make professionally sound decisions. We believe those positive organizational traits would be characteristic of an efficient and effective marketing organization, which is perceived necessary to survive and to be successful in a competitive market.

We then began to wonder what might cause such sub-optimality on the part of some NTOs. For instance, is there anything that differentiates NTOs from commercial companies operating in a competitive environment? First of all, it became obvious that most NTOs are financed and governed in a way that differentiates them from commercial organizations; they are predominately non-commercial organizations owned and financed by non-profit-maximizing owners (the governments), and their budgets are not predominantly performance-based, i.e., dependent on sales of products and services in a competitive marketplace.

One could then question the competitive-environment assumption. Is there anything in the way NTOs are financed or governed that effectively shelters them from market competition, allowing them to survive and expand regardless of their apparent sub-optimal operation? Furthermore, we began to question the assumption of NTO management discretion and (beneficial) decision autonomy. Are NTOs somehow enticed or forced to be product/sponsor/owner-focused rather than market-focused? Are their incentives and working conditions set in a way that they are forced to focus on short-term activities and plans? Are their sponsors and owners influencing or forcing the NTO to accept agendas different than what is professionally sound? Are NTOs, at the same time as they are operating in a business world, governed based on a political agenda rather than business agenda? These questions altogether raise at least one fundamental question, a question that will be the main focus of our study: Are there ways to finance and govern NTOs that will reduce the probable impact of politics and self-interest, and motivate and allow the NTOs to be more business-oriented, effective, and efficient?

We will start our abductive research approach (as explained in detail later in Section 1.5) by looking at the decisions the governing stakeholders will have to make when they create and govern NTOs. We believe the outcome of those decisions will influence NTOs' incentives, abilities, and behaviors. When a given nation or state wants to organize a new National Tourism Organization or reorganize an existing one, the people responsible will have to make a few important decisions: First of all, the organizers will have to decide on **how the organization's budget should be determined**, that is, to determine the financing mechanism for NTO's budget. Should the budget be based on some kind of market-performance (NTO's results), should it be based on the estimated cost of the activities the NTO is set to carry out, or the goals to be achieved (NTO's behavior), should the NTO simply be allocated a lump-sum payment each year (fixed-sum transfer), or any other criterion?

Furthermore, they will have to decide on how to fund the NTO or i.e., finance the budgets of the organization, since it is not a type of organization likely to generate enough funds on its own to be self-sustained. This is, for the most part, due to the *common/collective goods problem* of generic tourism marketing (as we will discuss in Chapter 2). The issue is then to determine **what source the organization should get its funding from**. Should financing the NTO be a government responsibility, a tourism industry responsibility, or should the money come from a combination of those two sources?

A third issue is **what entity should have ownership or the formal control of the NTO**. Should the NTO be organized as a government bureau or agency, an industry-led non-commercial organization, or simply a commercial operation owned and controlled by its shareholders?

These three issues, *budgeting*, *funding source* and *ownership/control* are all very important. We believe that the outcome of those decisions, i.e., which governance principles are applied, will have an impact on how the organization is likely to behave, its organizational focus, its efficiency and effectiveness - and in turn, its ability to generate the desired tourism influx. Through the use of an ideal combination of these three

variables, we believe the organizers can stimulate the organization to achieve better market performance.

First of all, we hold that this combination of principles will influence the organization's ability and willingness to have a strong **market focus**. There is already quite a lot of empirical evidence from previous research showing that strong market orientation is beneficial for an organization's performance (e.g., ref. Appendix 1).

Second, we believe the organizational principles applied will influence the organization's ability and willingness to adapt a **long-term perspective** in its operational strategies, in addition to its evident short-term planning and operations. This will allow the NTO to make strategic plans and engage in long-term activities and projects, which is necessary in the kind of work an NTO is carrying out.

Third, we believe that the principles applied will influence the organization's autonomy, or its **operational freedom**. We reason that an organization like an NTO will need to be sheltered from undue intervention from stakeholders with strong self-interests. In that way the NTO could be left free and uninhibited to make operational decisions on a professionally sound basis. We will later discuss how an NTO will be more efficient and effective if it is allowed (under certain restrictions) to make its own decisions about how to invest its resources and to organize and carry out its tasks.

It is thus conceivable that how NTOs' budget are determined, from what source budgets are allocated, and by whom the organizations are owned or controlled - will have an impact on the organizations' focus, planning time-horizon, and operational freedom, which in turn is likely to impact the NTOs' market performance.

Therefore, the main purpose of the thesis is to evaluate how different principles for organizing and governing NTOs can affect the likelihood of improved market performance of NTOs. By the term "*market performance*" we refer to the degree of ability of NTOs to positively impact the level of incoming tourism, and to function optimally given the resources they have available. That is, the means of governance the government and/or the tourism industry can employ to control and motivate NTOs. We believe that these aspects can somehow impact the ability of the NTOs to reach the market-performance goals they need.

The reader should be aware that we are *not* primarily concerned with the *internal* organization of NTOs in this study, as outlined in Figure 1.1 later in this section. Of course, there are also operational decisions other than the ones we have mentioned, which are relevant in the NTO context. For instance, practical issues like: who should be the NTO manager; how many employees to hire for the NTO; what background and compensation system staff should have; what kind of headquarters, branch offices, and equipment the NTO should have; and the nature of internal structure of the NTO; etc. are also important decisions that will have to be made. However, we will not discuss these internal issues here - getting into all the operational decisions and details would clutter our discussion in principle. We also believe that the factors we are concentrating on here

will have strong influence on how NTOs will behave and thus make their internal structure and operational decisions as listed.

### 1.3 Research problems of the study

In the following section we will outline the research problems addressed in this thesis and briefly introduce the variables we believe have an impact on the NTOs' incentives and working conditions. In turn, we believe that optimizing these incentives and working conditions will be important for effective and efficient NTO operation, and to assure that all NTOs' overall stakeholders' interests are safeguarded in the best possible way.

As mentioned earlier, a few crucial decisions will have to be made when the tourism authorities (NTA) and/or its industry constituents want to set up or reorganize such an organization. The decision alternatives outlined in Figure 1.1 below can be formalized in various *principles* for NTO-governance, which in different combinations will have varying effect on the organization's incentives and working conditions.

The principles we assess later in this study differ with respect to the following aspects:

- what are the principles for determining the *budgets* of the organizations i.e., are the budgets to some extent tied to the NTOs' (i.e., industry's) market performance, or based on some other criterion?
- who *owns* the NTOs (government vs. private sector)?
- what is the *source* of income (public vs. private sector)?

The issue we address is to what extent these aspects may influence the NTOs' market performance indirectly through their impact on the organizations':

- Market Focus<sup>4</sup>, i.e., NTOs' willingness to take the market as a premise for their actions
- Long-Term Perspective of plans and activities
- Operational Freedom, i.e., its ability to make decisions based on own professional judgments

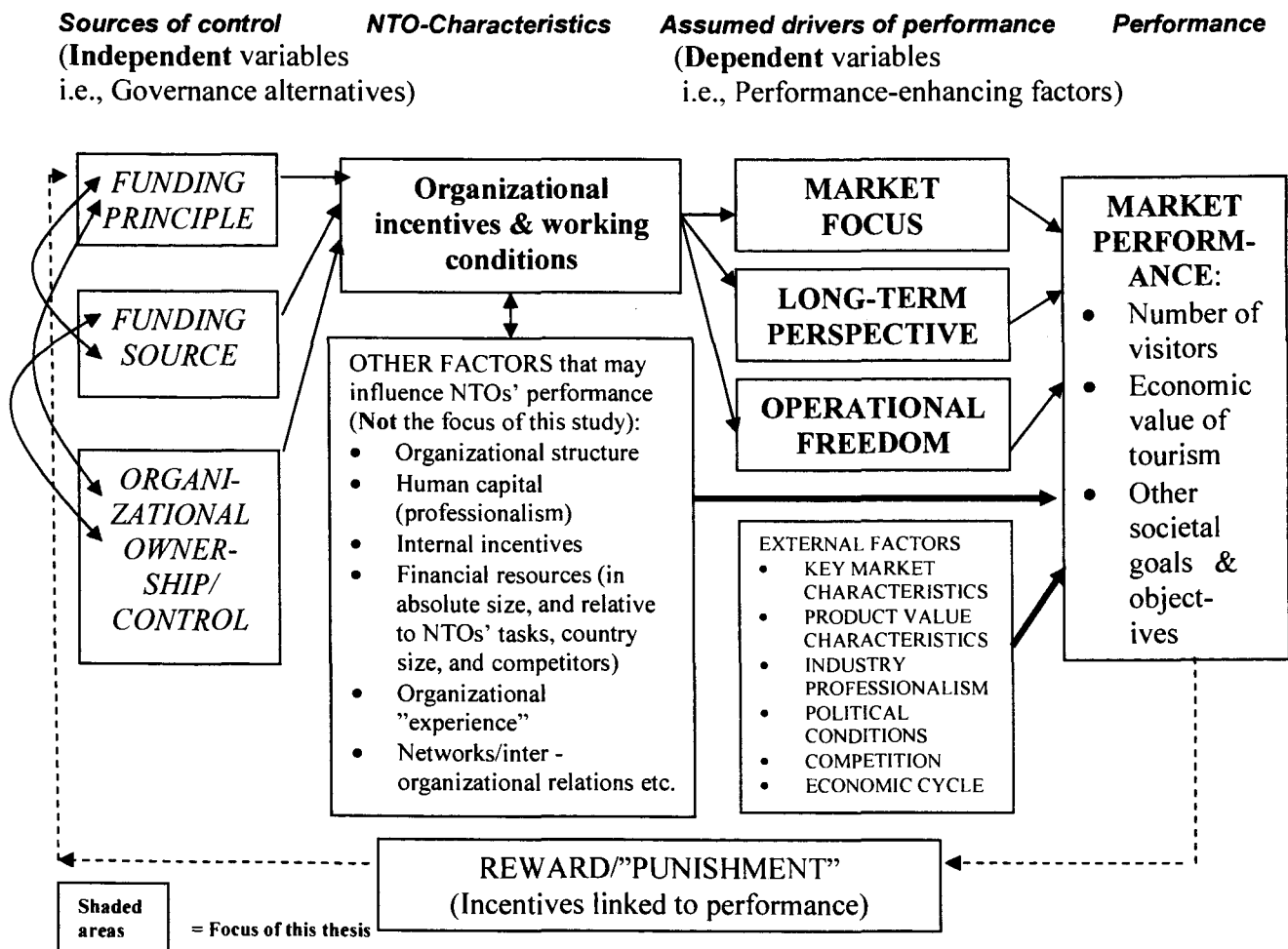
We propose that these decisions and their actual implementation will influence the NTOs' incentives, focus, and abilities. Because the budgeting principle may or may not give the right incentives for Market Focus and optimal production, we believe the budgeting principle or ownership constellation will be important for the NTOs' organizational focus; that is, its tendency to focus on marketing tasks rather than, for instance, counter-productive sponsor-lobbying, shirking, and budget-maximization behavior. Furthermore, the budgeting principle and funding source may influence NTOs' stability of budget size and control thereof. In turn, that will impact its ability to plan and operate with a Long-Term Perspective, which is necessary to achieve sustainable market performance. Finally, we believe that the *budgeting principle, funding source* and *ownership/control* constellation can influence NTOs' Operational Freedom. For instance,

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<sup>4</sup> From this point on we will use *italics* to denote the independent variables and Capitalization to denote the dependent variables when these are mentioned in the text.

performance-based budgeting may lessen the need for sponsors and/or owners to intervene in NTO activities and plans. We believe the NTO needs to have some degree of autonomy to make professionally sound decisions, and to motivate the NTO toward optimal participation and initiative, and entice the NTO to assume responsibility for its own actions. Consequently, we believe these factors have an impact on the motivation and ability of the organization to solve its marketing tasks efficiently and effectively.

**Figure 1.1**  
**Factors believed to drive market performance**



Following the discussion above we arrive at the first research problem of this thesis:

*The first research problem of this study is to evaluate how different principles for setting up and governing National Tourism Organizations can affect the market performance-enhancing incentives and working conditions of NTOs, and thereby the NTOs' ability to influence their countries' tourism market performance positively.*

This leads us to the first of three research questions:

1. *Which governing principles can be considered “best” for NTO operation?*

As Figure 1.1 depicts, our focus is on the three *factors* on the left and how they may influence NTOs’ working conditions and incentives; so that NTOs will be enticed and allowed to have a Market Focus, adapt a Long-Term Perspective, and enjoy Operational Freedom (shaded boxes right/center) under certain restrictions. We believe this will be positive for NTOs’ market performance, as depicted on the rightmost box in the figure. The budgeting principle may or may not feed back incentives through market performance (dotted arrow). Other factors and characteristics of NTOs (white box on the left/center) may also influence NTOs’ abilities, focus and behavior; as well as external factors somewhat beyond NTOs’ control (white box on the right/center) that probably will also have an impact on NTOs’ market performance. The latter will *not* be discussed in this study, but may be relevant for further research on NTO governance and administration, as we outline in the final chapter of this thesis.

To summarize the discussion of the first research problem we can then state the “discovery” of the following prepositions:

1. We believe the *budgeting principle* will have an impact on NTOs’
  - Market Focus
  - Long-Term Perspective
  - Operational Freedom
2. We believe the *funding source* will have an impact on NTOs’
  - Market Focus
  - Long-Term Perspective
  - Operational Freedom
3. We believe the *ownership/control* arrangement will have an impact on NTOs’
  - Market Focus
  - Long-Term Perspective
  - Operational Freedom
4. We believe that
  - Market Focus
  - Long-Term Perspective
  - Operational Freedomin turn will have a positive impact on NTOs’ market performance (NOTE: although measuring market performance is beyond the scope of this thesis).

Out of the three dependent variables we study in this thesis we have chosen to emphasize the importance of Market Focus of the NTO, because we believe this aspect will contribute the most to safeguard the interests of all stakeholders to the extent it is practically possible. (We will explain this in more detail in Section 3.1 and 3.2 later). We



admit, however, that market performance may not be the only goal for some NTOs. Market Focus, and thereby a strong market performance, may in some instances be in conflict with the pursuit of other societal goals such as e.g., sustainable tourism, regional development, cultural values, etc. However, an important premise of this thesis is that market performance, which we define to be the ability to generate incoming tourism traffic, will be a very important criterion for judging the overall performance of the majority of NTOs.

For clarity and better understanding, we should already at this point bring to the reader's attention the particular nature of this thesis. The abductive research approach we have chosen is based on the discovery of theoretical prepositions through review of relevant theory and any theory recommendations derived thereof, as well as discovery of decision-makers' *espoused theories* and *theories-in-use*<sup>5</sup>.

The chosen research approach entails to look into different areas of theory to find out what existing theory and empirical research described in academic literature can recommend in terms of the issues at hand, as well as consult theory experts. We will then try to find out how the decision-makers think and reason about the issues mentioned (espoused theories), and to compare this with what they and their colleagues actually end up doing in terms of NTO governance (theories-in-use). The recommendations from theory, and the evaluations by theory experts, will be compared with the decision-makers' espoused theories and theories-in-use to find out to which degree all these are congruent. We compare all this in two separate gap-analyses, as explained in detail in Sections 1.4-1.5. If congruence exists, that is a good argument to preserve *status quo*. If not, that may call for revisions in pre-existing theory and/or current NTO governance practice.

We are then looking to establish the following in our second research problem:

*The second research problem of this study is to investigate whether current NTO governing practice is consistent with practitioners' espoused theories and with recommendations from theory.*

Thus, the second and third research questions of this thesis are as follows.

2. *Are the ways the governing stakeholders of NTOs think and reason consistent with current theoretical knowledge and empirical evidence?*
3. *Do these stakeholders actually practice according to their own "theories"?*  
(*In other words: does the "terrain match the map"*)

If we through this study can answer positively to both questions, this may indicate that current academic theory is "true" and applicable in the context of NTOs - or simply that the stakeholders are in fact "doing it right". However, if there is a *mismatch* between: a) the theoretical recommendations and the respondents espoused theories, b) and/or a

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<sup>5</sup> We will define and discuss the concepts of *espoused theories* and *theories-in-use* in more detail later in this chapter in Section 1.4.

mismatch between the respondents espoused theories and their theories-in-use in current practice, there will be a need to

- a. try to explain why this is the case
- b. either *develop new theory* or *readjust current theory*, or try to *change the theory-in-use* by offering recommendations to the stakeholders more in line with current theoretical knowledge and empirical evidence (See also the research design as outlined in Figure 1.2 later in this chapter).

A more detailed explanation of why we address these specific issues and why we have chosen this particular research approach will be provided in Section 1.5 below and in Chapters 2, 3 and 4 later in this text.

## 1.4 Theories-in-use: Practitioner's theories

An important point in this study is to find out how stakeholders influencing NTOs think and reason in terms of the governing principles we have stated earlier. We want to investigate whether what NTOs' governing stakeholders *actually end up doing*, with respect to choosing the governing principles for NTOs, is congruent with what a sample of the same stakeholders *think* should be done. Another research issue is the degree to which current practice is consistent with recommendations that can be derived from written theory and theory experts. We therefore look into the concepts of *espoused theory* (i.e., what the stakeholders express ideally should be done with respect to NTO governance) and *theories-in-use* (i.e., what is done in practice) developed by Argyris and Schön (1974). We will discuss how these theories evolve to learn more about this kind of decision process.

### 1.4.1 Practitioner's theories and how they evolve<sup>6</sup>

Theories are predictive statements of what causes what, and why. Many managers and other decision-makers view themselves as practical men and women and do not view their actions as being guided by theory. But every plan that a decision-maker produces and every action that a decision-maker takes are, in fact, based on some theory in his or her mind - a belief that certain events or actions will result in particular outcomes. "If we cut price, more people will buy more" is an action predicated on a theory. "If I give her a performance-based financial incentive, she will work harder and more productively" is another. "If I outsource this subsystem to a supplier that does the job more cost-effectively than we can do it in-house, we'll be more competitive" is a third example. These theories serve as mental maps guiding the everyday actions decision-makers take.

Too often, though, decision-makers are not even aware of these powerful mental maps - beliefs about cause and effect - that they employ when making plans and taking actions. Still, the maps are there, somewhere in the decision-makers' minds. Every decision-maker is, therefore, in fact a theory-driven decision-maker to some extent.

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<sup>6</sup> Adapted from Clayton M. Christensen's foreword in the book "Leading Strategic Change: Breaking Through the Brain Barrier" by Black, J. Stewart and Hal B. Gregersen (2002)

Most theories that decision-makers use were formulated through experience - and because members of decision-maker teams experience many things in common, they end up employing similar theories, consciously or unconsciously, as they make decisions. Edgar Schein, a noted Massachusetts Institute of Technology scholar of organizations, has shown how these shared theories develop and come to comprise an organization's culture (Schein, 1992). He notes that, in the earliest days of every organization's history, there came a point when a group of people had to get something done. Confronted with that task, they put their heads together and figured out how they would approach the challenge. If their efforts failed, then the next time that task arose, they would be inclined to devise another way to get the job done. If that method proved successful, then the next time the task arose, the group would be inclined to use the same method to get the job done. If that method proved successful again when the same task arose, they would be even more likely to address the task with the same approach when it arose again, and so on.

Ultimately, if a group of people have successfully worked together in particular ways to address recurrent tasks again and again, they come simply to assume that this is the way they should do things. When this happens - when people begin adopting ways of working by assumption, rather than by explicit debate and decision - that process becomes part of the organization's culture. This is what an organization's culture is: ways of getting things done that a group of people have used so successfully for so long that they simply come to assume that doing things the same way is the only way to get the needed result. As a consequence, the more successful the organization is, the stronger will this unconscious consensus about cause and effect become. Another way to put it is that, because theories are statements of what causes what and why, an organization's culture is actually a collection of theories-in-use. These theories provide valuable guidance to decision-makers as they make plans and take actions, because they build on what individuals in the organization have learned from their collective experience. In fact, organizations with strong cultures or theories-in-use become in many ways self-managing, because decision-makers in disparate parts of the organization can be trusted to make decisions autonomously that are consistent with what the organization has learned will work. [This could also be true in an inter-organizational context, where governing stakeholders make decisions that will affect the relationship between entities or organizations or between organizations and the public and society in general.]

All of this is good, of course, except when things change, e.g., when market competition increases drastically or resources become increasingly scarce. Then the widely shared maps that decision-makers have unconsciously used to predict what events and actions will produce the needed results may no longer hold true. The theories-in-use can then change from being effective heuristics to becoming dysfunctional obstacles to needed organizational change.

### 1.4.2 Theories of action: espoused theory vs. theory-in-use<sup>7</sup>

Argyris and Schön (1974) argue that people have mental maps with regard to how to act in situations. This involves the way they plan, implement, and review their actions. Furthermore, Argyris and Schön assert that it is these maps that guide people's actions rather than the theories they explicitly espouse. What is more, fewer people are aware of the maps or theories they do use (Argyris, 1980). One way of making sense of this is to say that there is split between theory and action. Argyris and Schön suggest that two *theories of action* are involved. The distinction made between the two contrasting theories of action is between those theories that are implicit in what we do as practitioners and managers, and those on which we call to speak of our actions to others. The former can be described as *theories-in-use*. They govern actual behavior and tend to be tacit structures (Argyris & Schön 1974: 30). The words we use to convey what we, do or what we would like others to think we do, can then be called *espoused theory*.

*When someone is asked how he would behave under certain circumstances, the answer he usually gives is his espoused theory of action for that situation. This is the theory of action to which he gives allegiance, and which, upon request, he communicates to others. However, the theory that actually governs his actions is this theory-in-use. (Argyris and Schön 1974: 6-7)*

Making this distinction allows us to ask questions about the extent to which behavior fits espoused theory; and whether inner feelings become expressed in actions. In other words, is there congruence between the two? Argyris (1980) makes the case that effectiveness results from developing congruence between theory-in-use and espoused theory. A key role of reflection, we could argue, is to reveal the theory-in-use and to explore the nature of the "fit". Much of the business of supervision, where it is focused on the practitioner's thoughts, feelings and actions, is concerned with the gulf between espoused theory and theory-in-use, or in bringing the later to the surface. This gulf is no bad thing. If it gets too wide then there is clearly a difficulty. But provided the two remain connected then the gap creates a dynamic for reflection and for dialogue.

Where the consequences of the strategy used are what the person wanted, then the theory-in-use is confirmed. This is because there is a match between intention and outcome. There may be a mismatch between intention and outcome. In other words, the consequences may be unintended. They may also not match, or work against, the person's governing values. Argyris and Schön suggest two responses to this mismatch, and these can be seen in the notion of single- and double loop learning.

Learning to change underlying values and assumptions is the mantra in *double loop learning theory* developed by Chris Argyris (1976). The focus of the theory is on solving problems that are complex and ill structured, and which change as problem-solving advances. An important aspect of the theory is the distinction between an individual's espoused theory and their "theory-in-use" (what they actually do); bringing these two into

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<sup>7</sup> Adapted from M. K. Smith's (2001) internet-published article "Chris Argyris: theories of action, double-loop learning and organizational learning", *The encyclopedia of informal education*, [www.infed.org/thinkers/argyris.htm](http://www.infed.org/thinkers/argyris.htm). A more detailed discussion of the concepts *theories-in-use*, *espoused theories*, and *single- and double loop learning* can be found on this web site.

congruence is a primary concern of double loop learning. Typically, interaction with others is necessary to identify the conflict. Double loop learning involves applying each of these steps to itself. In double loop learning, assumptions underlying current views are questioned and hypotheses about behavior [or cause-and-effect relationships] tested publicly. The end result of double loop learning should be increased effectiveness in decision-making and better acceptance of failures and mistakes (Smith, 2001).

### 1.4.3 Theories-in-use in the NTO context

The set-up of an NTO can be considered as a kind of "intervention" (Calder, Phillips and Tybout, 1981) in which the governing stakeholders of NTOs apply their "theories" or insight into how organizations work to make decisions. We thus believe that the principles that govern the establishment and operation of NTOs are not arbitrary, but reflect the theories-in-use of the stakeholders, whether these theories are explicit or not, or whether or not they are consistent with scientific theoretical frameworks.

An important purpose of this study is to elicit how the stakeholders think and reason when they make decisions about NTO matters, and if this reasoning is actually congruent with what ends up as implemented principles in current practices. In fact, this research process can be described in terms of Argyris and Schon's (1974) notion of *discovery of espoused* and *theory-in-use*.

From his research Argyris has developed two important principles:

1. Effective problem solving about interpersonal [and inter-organizational] or technical issues requires frequent public testing of theories-in-use.
2. Double loop learning requires learning situations in which participants can examine and experiment with their theories of action.

Double loop learning is a theory of personal change that is oriented towards professional education, especially leadership in organizations. It has been applied in the context of management development, but can be applied in an inter-organizational context as well.

Following the discussion earlier in this section, it is also likely that stakeholders with influence on governing NTOs are guided by their theories-in-use. There is also reason to believe that these theories-in-use have evolved through the years of collective decision-making by the governing stakeholder-actors in the NTO context. For the sake of this discussion, it is interesting to compare the often non-commercial context of NTOs with a competitive commercial environment. First, there is the issue of executive choice. A manager in a commercial organization is assumed to have a certain degree of decision autonomy granted him by the board of directors or shareholders. The decisions he makes will be guided by his theories-in-use as described earlier. In the NTO context, however, the situation may not be the same in terms of the governing stakeholders' decision-making. The stakeholders may not only have to make governing decisions based on what is rational from a business perspective, but also have to consider e.g., political concerns budgeting regulations, public agency/bureau laws, and bureaucratic procedures. So the decisions they make about NTO governance may not reflect their own theories-in-use

solely based on their professional judgments, whereas their practices are the executive outcome of their professional judgments under the restrictions put on them in the NTO context. Furthermore, it should be noted that in the empirical part of this study we use only a sample of potential decision makers and influencers of NTO governance. Thus, the existing practices in NTO governance of the countries we sample are probably not solely decided on and influenced by the people we have included in our practitioners' sample, but also their colleagues in the respective countries who are not included in our sample of practitioners. In the following we ask the reader to keep this in mind when we refer to the practitioners' theories-in-use.

Secondly, there is the issue of the virtual absence of market-disciplining mechanisms in the NTO context. The survival-of-the-fittest-condition of a competitive commercial context will in many cases discipline managements' decision-making. Companies (and their managers), which do not adapt their decision-making when their business environment changes, will probably go bankrupt or otherwise subdue. In many cases, the market forces will then act as a corrective mechanism enticing managers to change their theories-in-use when they prove to no longer produce the needed results. The ones that do not will probably succumb. However, in most cases NTOs are not subject to the same kind of market competition as commercial companies are. Decision-makers involved with the creation and governance of NTOs will not be punished in the same way by the market forces if they continuously make sub-optimal decisions in NTO-matters. Theories-in-use successfully applied in the past, will in many cases be able to stand unchallenged, and could perpetuate in the NTO contexts' inter-organizational culture. NTOs' stakeholders may have only weak incentives to change existing practices. The administrative systems, and the principles applied therein, are then probably able to remain unchanged through time. We therefore believe that it is particularly important to elicit and investigate both the espoused theories and the theories-in-use of the decision-makers with real influence on how NTOs are set up and governed.

In this thesis we will then seek to present and implement a new method for discovering both the espoused theories and the implicit theories in-use of NTOs' stakeholders. These underlying theories are the ones NTOs' governing stakeholders have learned to trust in the course of creating and governing NTOs, as well as influences due to political concerns, procedures, and tradition in the NTO context. We believe these theories must be understood explicitly before new ones can be adopted in times of change.

In line with Argyris and Schon's research, we want to contribute through this study so that the theories-in-use of NTOs' governing stakeholders and their underlying assumptions are discovered, made explicit and put under public scrutiny. We believe that in this way NTO governing matters could be made subject to healthy public debate, and eventually, that any inefficient or obsolete practices are abandoned.

## 1.5 Research approach

In order to assess how the governance decisions should be made, it could be fruitful to investigate whether established theory can provide any recommendations as to how

NTOs should be set up and governed. Through the application of theory one can learn more about whether, and to what extent, any of the suggested decision alternatives or *principles* are expected to lead to the desired consequences or not. These decisions call for a somewhat pragmatic *application of established theory*, rather than the more common approach in academic research, which is applying and *testing theories* through rigorous falsification procedures. We will explain the choice of research method in more detail in Chapter 4.

### 1.5.1 Abductive versus inductive or deductive research approach<sup>8</sup>

To the American philosopher Charles Peirce abduction is a logic reasoning-form along with deduction and induction. He argued that one would use abduction when one experiences something peculiar about which one lacks knowledge of. One would then use a hypothesis to explain that peculiarity which follows deductively from the hypothesis. Peirce holds that it is only abduction that can generate new ideas. Induction can never generate an idea, just confirm hypothesis. What separates induction and abduction fundamentally, is whether those constructs one is working with, and which then becomes the essence of what one finds, is given immediately from the data itself.

Induction as a process goes from empirical observations to theory, while deduction goes from theory to empirical data. Both inductive and deductive research approaches have testing of a theory's degree of truthfulness as the overarching goal (Troye, 1994). However, both induction and deduction create a dilemma: Induction can not give knowledge that is qualitatively new. It cannot give a type of knowledge that one has not had in advance. Induction requires that one has to know the constructs one utilizes as measures in the induction process. Deduction can, on the other hand, give us sure knowledge, but also here the constructs are assumed known. An important question is whether there exists a method for collection of data that can provide new knowledge, which one can later refine, affirm, and develop through induction and deduction. Abduction can be seen as a reaction on the limitations of induction and deduction, and as an interactive process between the inductive and deductive approach (Hanson, 1959).

Through abduction, the thought process is enriched with new material in the form of ideas that are included as new possible ways of understanding whatever is studied (Kirkeby, 1994). These ideas can be stated as an assumption which later on can be tested against reality. Thus, Peirce holds that the research process entails the three logic forms: abduction, deduction and induction. Abduction is therefore perceived as the first step in a universal scientific procedure comprised of three steps (Fann, 1970):

1. Abduction; the first step where the hypothesis is *discovered*
2. Deduction; the next step where *facts are deduced* from the hypothesis
3. Induction; the final step where the *empirical validity* of these predictions are *falsified* through testing of the theory.

Abduction and induction can be termed each other's adversary. Abduction is the first step in scientific thought, while induction is the final step. Abduction seeks theory, while

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<sup>8</sup> Adopted from "Essay i Teori og forskningsevaluering" av Hans Jørgen Lund (2002).

induction seeks facts (Fann, 1970). Hence, the abductive approach does not serve the same purpose as induction and deduction when it comes to testing theories. The theories could rather be perceived as tools to extract information from observations of reality. The focus is directed at discovering aspects, traits, and qualities in the empirical reality, which is studied with theories as idea-generating tools, and then in turn suggests theories that can explain such discoveries. Guiding constructs are in this regard more open to the empirical reality than pre-defined constructs. Such guiding constructs have the ability to add new dimensions. They can be utilized to guide the research process towards certain aspects in reality, but they are not so precisely defined that they narrow the perspective so much that nothing but pre-defined constructs can be discovered (Patton, 1990). Theoretical models or constructs from one research area can in this manner work as “heuristic tools” for theory development in another area (Troye, 1994).

In terms of our research approach we have used an abductive process. As explained earlier in Section 1.1.2 we have observed a behavioral pattern of some NTOs that were not expected according to our own reasoning of how they ought to behave. We have thus “experienced something peculiar of which one lacks knowledge about”, and we use theory to discover (although *not* test) new hypothesis or *propositions* as we phrase it. For the most part, the theoretical constructs (i.e., possibly apart from the market-orientation construct) we use to explain NTOs’ behavior are not pre-defined in theory, and serve to add new dimensions that can be tested empirically in future research.

### 1.5.2 Research design

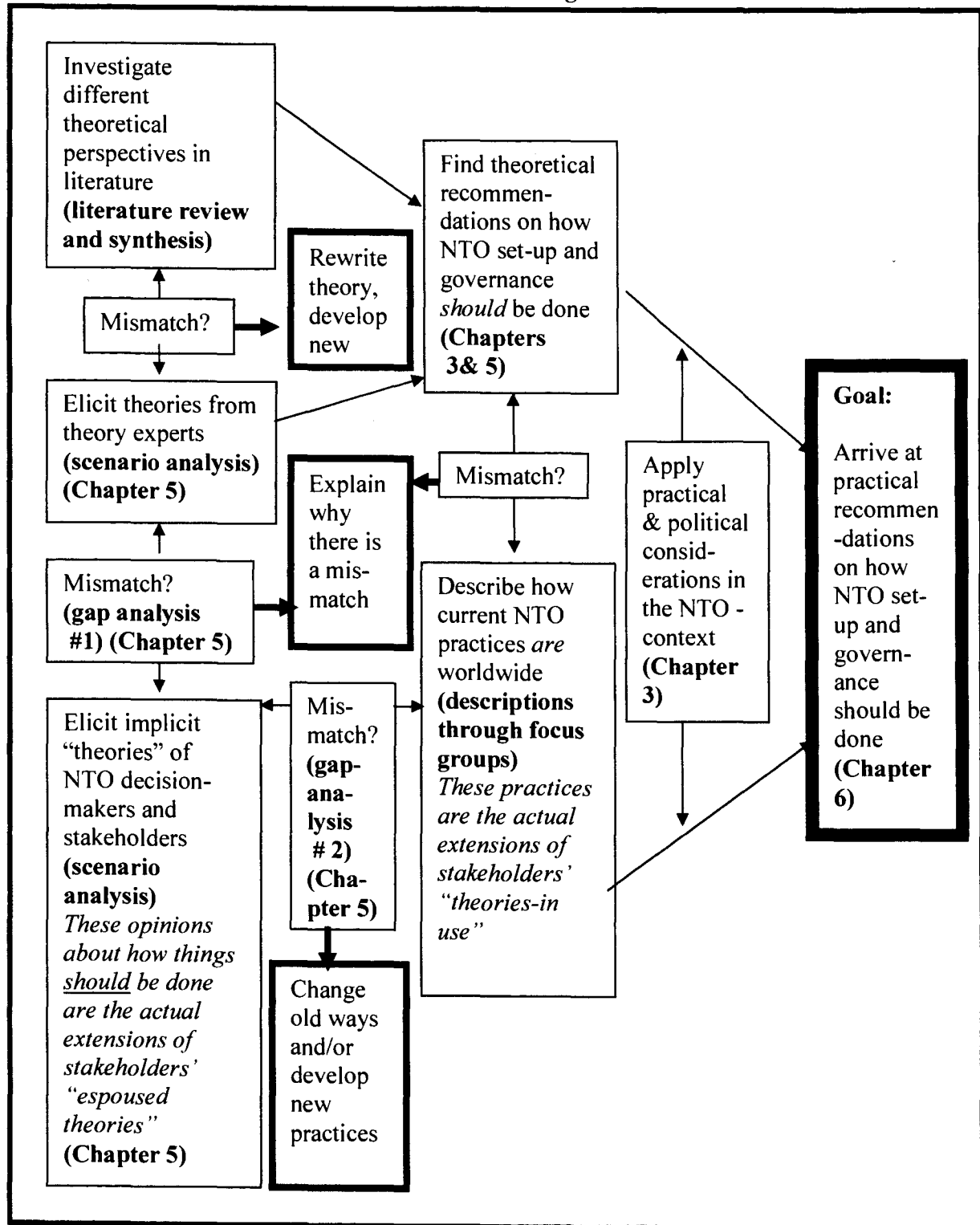
We have approached our first research problem stated earlier in four ways, as shown in Figure 1.2: First, we analyzed the issues at hand by applying a number of alternative, and partly overlapping, bodies of theory to build a **theoretical framework**. The purpose was to examine each of the theories’ relevance and implications for the research question stated earlier. We therefore asked ourselves: From given theoretical perspectives, how should we expect NTOs’ decision-making, in terms of its Market focus, Long Term-Perspective and Operational Freedom, to be affected by *how budgets are determined*, by *whom it is funded*, and by *whom it is controlled or owned*? Do alternative theories suggest that the various aspects of organizational control and funding we have named will have any bearing whatsoever on the way it operates and approaches its markets? If so - *how* should we expect its behavior be affected by such factors?

Second, we complemented our theoretical basis by addressing this research question from the **perspective of experts on theory** representing different branches of theory (e.g., marketing, organizational sciences, and public economy). We then attempted to elicit and describe their theoretical reasoning as to how principles for funding and controlling NTOs may affect the behavior and performance of such organizations. For this purpose we used a scenario technique, as explained in more detail in Chapter 4.

Third, we had respondents describe **how things are done in practice**, which is an extension of the practitioners’ and their respective colleagues’ theories-in-use. We asked our practitioner respondents to rate the degree of use each of the principles we have named, and thus establish to what degree each principle is actually implemented in current or existing practices.



Figure 1.2  
Research design



Fourth, we addressed the research question from the NTO **stakeholders' perspective**, using the same scenario technique. We thus attempted to elicit and describe our practitioner respondents' "theories" as to how the said principles may affect NTOs and their performance. It is reason to believe that these "espoused theories" will to some degree influence the decisions made when NTOs are set up, organized, and governed.

However, these espoused theories may not be congruent with the actual existing practices, i.e., the practitioners' and their respective colleagues' theories-in-use.

Therefore, we addressed the second research problem of this thesis: We contrasted the recommendations derived from the theoretical frameworks and from theory experts on one side, with the espoused theories of the practitioners on the other side to answer our second research question in gap analysis # 1. Finally, we contrasted the espoused theories of the practitioners on one side with and the corresponding theories-in-use of our practitioner respondents and their colleagues on the other side to answer our third research problem in gap analysis # 2.

### 1.5.3 The application of theory to address practical issues vs. testing of theory

An important methodical note regarding the application of theory is due here. In this study we will *not* apply the theoretical frameworks by using some kind of falsification procedure (ref. Calder, Tybout and Phillips, 1981) to assess their predictive power. We will rather investigate whether academic theories can be used to derive recommendations as to how NTOs should be set up to be well-functioning as marketing organizations.

Our research approach brings about some challenges: In order to discuss these practical issues in a theoretical context, one will have to discuss some theoretical considerations (e.g., agent and stakeholder risk-sharing, programmability of tasks, budget-maximizing behavior, the common goods-problem, etc.) somewhat beyond the core, practical issues of this thesis. This is because theory is in itself richer than the specific practical issues we are interested in, and "deserves" to be discussed somewhat comprehensively and not only conveniently as it relates to practical matters. On the other hand, there are clearly some practical and political considerations in the NTO context that are not fully discussed in pre-existing theory. Furthermore, the issues at hand also call for solutions that are not only theoretically sound, but also practically possible, implementable, and politically acceptable on an international arena as well.

Some readers may feel that the thesis has some amount of redundancy and thus seemingly unnecessary repetitions of certain aspects in the text. First of all, this may be the case in e.g., the theory chapter: Several bodies of theory, when applied to the NTO context, reach the same or similar conclusions; then there are repetitions of what is earlier found in one area in the conclusions from another area, etc. However, this is a consequence of using an abductive research approach (explained earlier in Section 1.5.1), where the idea *is not to test* any given theory, rather than find theoretical evidence (e.g., based on several theories) to build a case - that there is in fact a likely connection between the variables in question. Viewed from this perspective, *repetition is not redundancy* or necessarily something bad; *repetition can be good* because it strengthens

the theoretical evidence that the proposed model is correct, or has at least some degree of scientific merit.

It is also important to note that the purpose of the theory review is to arrive at well-founded theory-based recommendations on the issues at hand, rather than to deductively develop hypothesis that can be used to test the theory. Thus, this thesis will not contain any explicit hypothesis in the theoretical/conceptual part of the study that will be tested through a rigorous falsification procedure in the empirical part of the study. Therefore, we will not resort to the traditional testing-of-theory type of research method.

## 1.6 Overview of the thesis

The thesis is divided into seven chapters plus seven appendices: Apart from this introductory chapter, Chapter 2 deals with the general theoretical framework. Within this framework we will discuss several areas of theory, each of which offering different perspectives on issues related to our research problem. From the review of pre-existing theory and empirical research we build a theoretical foundation for the constructs and variables we develop and use in the empirical part of the study. We will then investigate how this synthesis of theory can offer recommendations on which principles are best suited for NTO governance.

Chapter 3 incorporates the conclusions made from the theoretical framework into the particular NTO context. In this chapter we go more into detail about the NTO context. We then discuss the theory recommendations related to this context, and how they can be made practically and politically acceptable in terms of NTO governance worldwide. The discussion in Chapter 3 eventually arrives at our standpoint in terms of which governing principles should be chosen and applied - considering both the theoretical, practical, and political implications. This chapter also describes the general research model for the empirical part of the study, the variables studied, and the rationale for the choice of those.

Chapter 4 explains the choice of research method, and discusses some problems related to the traditional testing-of-theory-approach in the NTO context. The data collection procedure and data analysis method is also presented in Chapter 4.

Chapter 5 contains the presentation and discussion of the empirical data. Chapter 5 has two empirical parts: The first part is descriptive, and identifies the governance principles in use for our sample NTOs today. In the second part, we describe and analyze how both the existing and alternative principles for NTO governance were evaluated by a group of theory experts and 14 the groups of practitioner respondents from our OECD sample. We then arrive at some conclusions about the suitability of the various principles based on the evaluations, the theoretical framework, and the special considerations of the NTO context. This chapter also contains the two gap analyses we outlined in Figure 1.2.

Chapter 6 provides an overview of the main findings and our conclusions based on these findings. We also offer some practical recommendations for NTO set-up and governance.

Finally, in Chapter 7 we list some management implications for practitioners and what we think this thesis represents in terms of contributions to academic research. We also discuss some limitations of this thesis and provide some suggestions for further research in this area.

In the appendices (A1-A7) we have included: a summary of the empirical results from research on market orientation, an overview of control principles for NTOs derived from application of theory, the material used for data collection, as well as the data from the factor and cluster analysis. We have also included the results of a separate study on the effect of the funding source on NTOs' organizational focus and market orientation, as well as some illustrative simulations of the effects of performance-based principles on NTOs' budgets.

## **2.0 Literature review and theoretical framework**

The purpose of this section is to provide a theoretical framework for the discussion of the applicability of various alternative governance principles for NTOs, as well as to provide a basis for the empirical part of this study. Six bodies of theory will be discussed in this chapter:

1. *Market orientation theory*, which deals with how use of market information can enhance the effectiveness and efficiency of organizations in competitive markets;
2. *Agency theory*, which deals with the control of contract relationships between a principal and agent under uncertainty, and how control devices can be designed and implemented;
3. *Transaction cost theory*, which deals with contract-related costs. Transaction cost theory will be discussed only briefly as it relates to agency theory in terms of the costs incurred through stakeholders' monitoring structures for the NTOs;
4. *Public choice theory*, which deals with the design of political organizational control for political institutions;
5. *Public economy theory*, which deals with issues like market failure and control of monopolies, regulation of government-owned organizations, the effects of private vs. public ownership of organizations, the common goods problem etc.;
6. *Corporate governance/finance theory*, which deals with management incentives and corporate control, which can be usable in a non-commercial NTO context as well.

In practice, the set-up of an governance system for NTOs deals with the process of identifying and implementing a system that will give the organizations freedom and incentives to work on the tasks they are supposed to, which is a matter of effectiveness. An equally important concern is to assure that scarce resources are not wasted, which is a matter of efficiency. The six bodies of theory we have listed appear to be particularly applicable for the NTO context. Figure 2.1 on the following page gives an overview of the theory discussed and applied in the NTO context and how it relates to the research problem and the theoretical variables of this thesis.

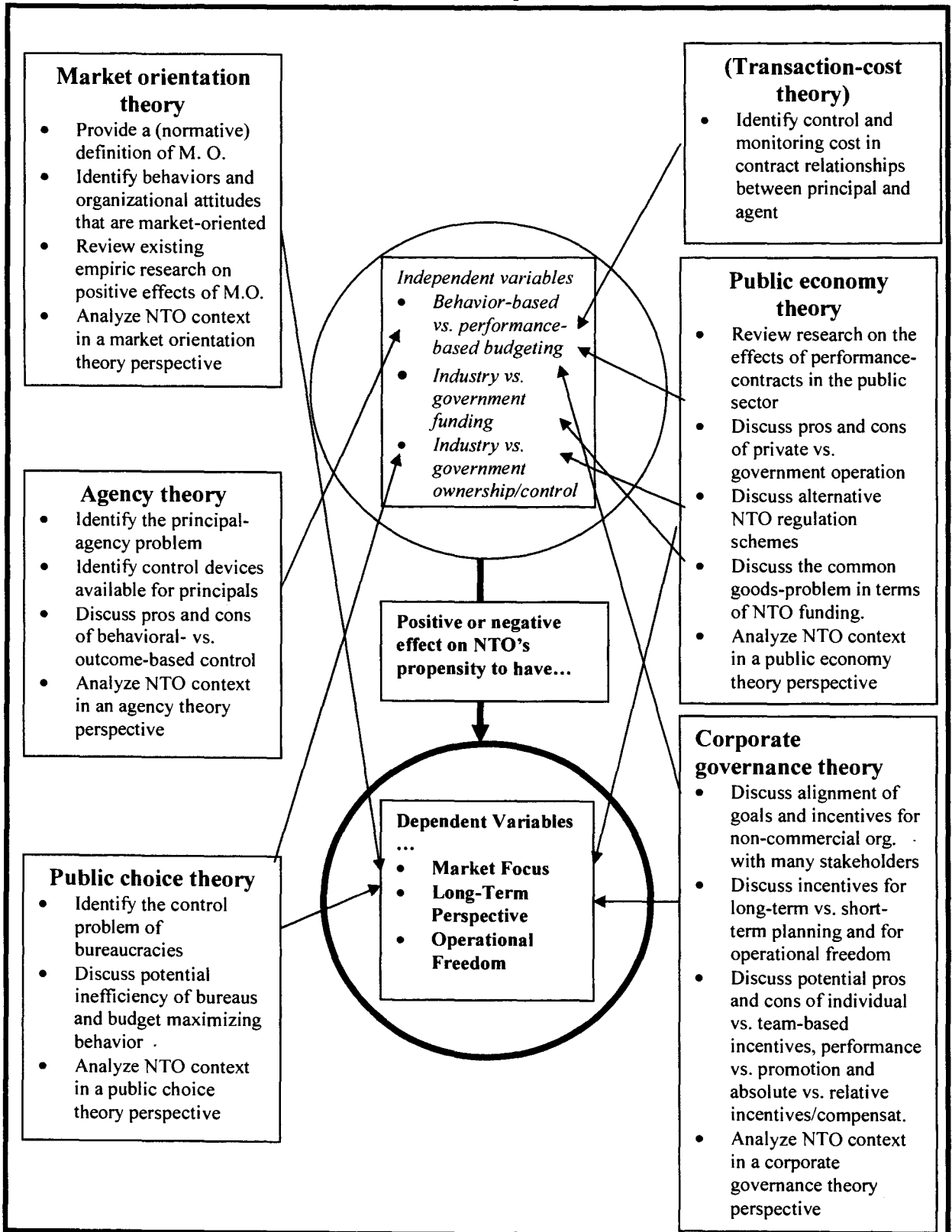
### **2.1 Market orientation theory**

Several studies provide evidence of the positive effect of market orientation on the market performance of organizations. A partial summary of existing research on the effects of market orientation is included in Appendix 1. Market orientation theory, as a theory of the firm and a part of marketing management theory, has a more microeconomic perspective compared to some of the organizational theory we will discuss later. There are two main contributions from the 1990s to the definition of the market orientation concept: Kohli and Jaworski (1990) and Narver and Slater (1990)<sup>9</sup>.

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<sup>9</sup> A number of other researchers have also contributed to the market orientation literature, but we will in this thesis limit our discussion to the main contributions of Kohli and Jaworski (1990) and Narver and Slater (1990).

**Figure 2.1**  
**An overview of the application of different areas of theory**  
**on the main research problem**



**Table 2.1**  
**Market orientation theory's relevance for independent and dependent variables**

<i>Independent variables' relevance for study</i>		<i>Reference to text</i>	<i>Dependent Variables' relevance for study</i>		<i>Reference to text</i>
<i>Budgeting principle</i>	Unlike commercial organizations NTOs have few incentives for a Market Focus. A performance-based type of budgeting principle can provide such an incentive	2.1.3 & Fig. 2.2	Market Focus	Defines what M.O. is and which activities and attitudes it entails. Provides theoretical and empirical evidence that M.O. is beneficial for organizational performance	2.1.1-2.1.2.
<i>Funding source</i>	If NTO is not made dependent on market performance, the NTO could have undesirable incentives for a funding source/sponsor focus rather than market focus	Fig. 2.3	Long-Term Perspective	For survival, a business cannot avoid a L.T.P. in the presence of competition. An NTO needs extra incentives for L.T.P., since it can survive without it, if not made somehow dependent on market performance	2.1.2 & 2.1.3
<i>Ownership/org. control</i>	If NTO is not made dependent on market performance, the NTO could have undesirable incentives for a owner focus rather than market focus	2.1.3 (end)	Operational Freedom	NTO needs some degree of O.F. in order to undertake professionally sound market-focused activities. Without O.F. the NTO can be forced into e.g., a product orientation rather than M. O.	2.1.3 (end)

### 2.1.1 Market orientation as conceptualized by Kohli and Jaworski

Kohli and Jaworski developed the following definition of market orientation:

*“Market orientation is the organizationwide generation of market intelligence pertaining to current and future customer needs, dissemination of the intelligence across departments, and organizationwide responsiveness to it”* (Kohli and Jaworski, 1990).

The first dimension of market orientation is *information generation*, which can be obtained through systematic gathering of unbiased and rich information from multiple sources. Market information is the essence of the organization's marketing activities. “Without such information the organization will not be able to adapt its strategy and behavior to the various stakeholders in the market. Consequently, information should capture the current situation and the future anticipated situation of (current and potential) customers” (Sandvik, 1998)<sup>10</sup>.

The second dimension of market orientation is *intelligence dissemination*. Kohli and Jaworski argue that

“...it is clear that responding efficiently to a market need requires the participation of virtually all departments in the organization – R & D to design

<sup>10</sup> We also subscribe to Sandvik's (1998) construct of Market Orientation Domainwidth (e.g., information generation regarding *new* markets and *new* competitors).

and develop a new product, manufacturing to gear up and produce it, purchasing to develop vendors for new parts and materials, finance to fund activities, and so on". Kohli and Jaworski (1990)

This dimension deals with the spreading of information from the information-generating entities in the organization to other parts of the organization that can utilize this information to adapt the organization's products and services to the customers' needs and preferences. We will discuss in more detail how *intelligence dissemination* can be understood in the NTO context in Section 2.1.3 later.

We then go on to the third dimension of market orientation, namely *responsiveness*: "...which is the action and behavior taken in response to generated and disseminated market intelligence." (Sandvik, 1998) More specifically, this entails the use of market information when:

..selecting target markets, designing and offering products/services that cater to the customer's current and anticipated needs, and producing, distributing, and promoting the products in a way that elicits favorable end-customer response. Virtually all departments – not just marketing – participate in responding to market trends in a market-oriented company. (Kohli and Jaworski, 1990)

According to Kohli and Jaworski "...virtually all of the organization's activities, including planning and strategy development, should take market information into account in advance." Thus, a market-oriented organization would base its strategic plans and actions on the collection and use of market information.

## 2.1.2 Market orientation as conceptualized by Narver and Slater

Narver and Slater (1990) provide the second main contribution to the market orientation concept. They focus on the ability to create superior business performance through SCA [Sustainable Competitive Advantage]:

*"...a market oriented business continuously examines these alternative sources of SCA to see how it can be most efficient in creating sustainable competitive superior value for its present and future target buyers" (Narver and Slater, 1990)*

Narver and Slater's (1990) definition of market orientation entails five dimensions. (We will discuss only three of them as they pertain to NTOs in the next section<sup>11</sup>) The first relevant dimension is *customer orientation*, which is argued to be "sufficient understanding of the firms target buyers to create superior value for them continuously – not only today but also as it will change over time". In order to understand the customer, the organization needs a constant acquisition of information about the buyer. This notion is really the core of the marketing concept, according to Houston (1986) (Sandvik, 1998).

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<sup>11</sup> The two other dimensions not discussed here are *Interfunctional coordination* and *Profitability*, which are both somewhat less relevant in this particular discussion of the NTO context.



According to Narver and Slater (1990) "...competitor orientation is the seller's understanding of the strengths and weaknesses of both the current and the potential key competitors". Furthermore, they argue that "...the analysis of principal and potential competitors must include the entire set of technologies capable of satisfying the expected needs of the sellers' target buyers". This analysis should include both close and more remote competitors. However, Narver and Slater clearly emphasize that it is necessary for a market-oriented organization to balance the market- and competitor orientation, and avoid selective attention on either dimension. This is also consistent with Day and Wensley (1988) (Sandvik, 1998).

Finally, Narver and Slater include *long-term perspective* as related to market orientation. To overcome the problem that market activities can be costly, a market-oriented firm should consider the impact of market activities on profitability, or market performance - in the NTO context, in the long run as well as in the short run.

"For long-term survival in the presence of competition, a business *cannot avoid a long-run perspective*. To prevent its competitors from overcoming whatever buyer-value superiority it has created, a business must constantly discover and implement additional value to its customers, which necessitates a range of appropriate tactics and investments." (Narver and Slater, 1990)

According to Sandvik (1998), Narver and Slater have in recent studies treated Long-Term Perspective as a *consequence* of market orientation, rather than a part of the market orientation concept. One can argue that the opposite is the case as well, that a long-term perspective is a *prerequisite* for market orientation. We will not get into a further discussion on that issue here. In this thesis we choose to treat Long-Term Perspective as a separate factor<sup>12</sup>.

### 2.1.3 Market orientation in the NTO context

The term "superior customer value" in Narver and Slater's (1990) first dimension of market orientation is interconnected with the second dimension, *competitor orientation*. In order to create "superior value", this "value" must be superior *relative* to some "other value". Assuming a situation other than perpetual monopoly - and that the customers will choose the products and services [or resources; - man-made<sup>13</sup> or natural] best suited to their needs and preferences, this "other value" is the value of the products and services offered by competitors in the target market. This competition may consist of other NTOs promoting products/services of other countries, foreign private tourism businesses, or any

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<sup>12</sup> *Long-Term Perspective* is treated as a separate variable because of the following: In our research model the factors theorized to influence the construct are exogenously given by stakeholders external to the organization (e.g., budgeting principle, funding source etc), and are not solely a matter of NTO management discretion, which is a more common situation in a commercial context.

<sup>13</sup> This also includes any current or potential travel and tourism infrastructure such as transport vehicles and facilities; accommodation facilities; food and beverage service, public services; and other man-developed natural based resources e.g., ski lifts, scenic roads, beach facilities, camping grounds, etc.

substitute tourism products and services available in the international tourism market. NTOs should then contribute to create superior customer value relative to competing destinations. For instance, selecting target markets, developing its country's destination image, providing advice to the industry with regards to capacity increases/decreases and on product and services development, etc. requires input of market information and competitors' offerings and actions. Likewise, use of market and competitor information is crucial when coordinating destination promotions, e.g., securing message consistency across target markets, choosing differentiating strategy, and selecting media channel and media magnitude appropriate for each target market.

A contextual challenge with respect to the market orientation literature in general is that it assumes that the unit of analysis, the organization or firm, both produces, owns, and markets its own products or services. Often the organization is assumed to possess and control all functional departments e.g., as is common in a manufacturing company. Usually, NTOs neither produce nor own the products and services they market. Of course, NTOs rarely have manufacturing departments, physical R&D laboratories, or purchasing departments etc., typical in a manufacturing company either. The NTOs have in fact only direct control of the Promotion-parameter out of the four P's (Promotion, Product, Price and Place/distribution) commonly referred to in marketing strategy literature. However, the NTO can influence the application of the other parameters through advice to the industry, which controls these other parameters. Therefore, for NTOs, which are not themselves in direct control of the tourism industry's products and services, *intelligence dissemination* then deals with passing the gathered information on to the producing tourism industry as a part of the organization's advisory role. We will discuss the NTOs' activities and roles in more detail later in Section 3.1.

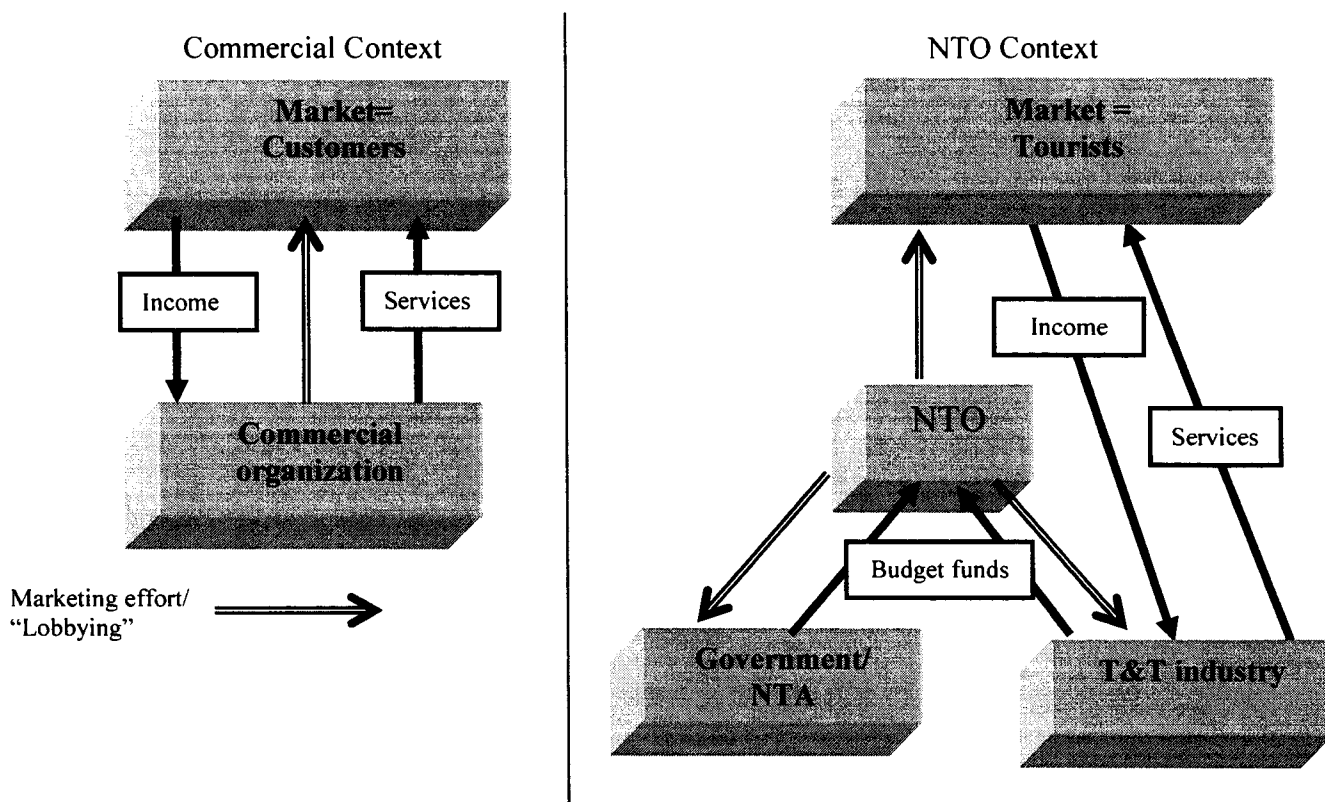
NTOs are, first of all, international tourism *marketing* organizations. Furthermore, they are usually closer to the international markets than most of their national tourism industry constituents. Ideally, NTOs should then continuously gather international market information and disseminate it both internally in the organization itself and externally to the domestic tourism industry. It is important that the information about the target market's needs and preferences is passed along to the tourism industry, because the industry is the entity that controls the tourism products and services. In that way the industry can use this information as an input to new product and service development or improvement. For instance the NTO could do so by advising the industry so that any expansions and investments in new travel and tourism capacity (supply) will be matched with the actual needs and preferences of the market (demand). This is also the case in the process of modifying or repositioning of existing travel and tourism products and services. Systematic *market research* and other kinds of information generation are needed to uncover these needs and preferences. *Communication* and information dissemination to its tourism industry constituents is necessary to make the market information available to the industry, so the industry can adapt its tourism products and services to the customers' current and future needs and preferences.

A problem with the work on market orientation by Kholi and Jaworski and Narver and Slater is that they for the most part provide normative definitions of market orientation only. Moreover, market orientation is viewed in an intra-organizational perspective,

rather than in an inter-organizational perspective, which is the focus in this thesis. Little is said about what processes or incentives are involved to foster market orientation, or how to intervene or otherwise facilitate so that organizations become (more) market oriented. For our purposes, application of market orientation theory deals with where NTO has its main focus, whether it is on the market - or its sponsors or owners. Thus, we are not particularly concerned with which market-oriented activities the NTO should undertake; we will leave that to the NTOs' management. The focus will be on finding ways to provide the NTO with organizational incentives for pursuing a market focus, first of all.

Another problem is that most of the previous research of the effects of market orientation has been conducted on commercial organizations. Although important knowledge can be gained from the study of for-profit organizations, the results of these studies may not be fully generalizable to NTOs. Whereas most commercial organizations have one market arena, NTOs have several, as illustrated in Figure 2.2. This is one reason why previous findings with respect to market orientation may not be completely valid for NTOs. Unlike commercial organizations, non-profit NTOs are not dependent on the direct income from the tourism market. Therefore, one cannot take for granted that the market will be the most important focal point for an NTO, since other arenas may be more important for its organizational survival and growth.

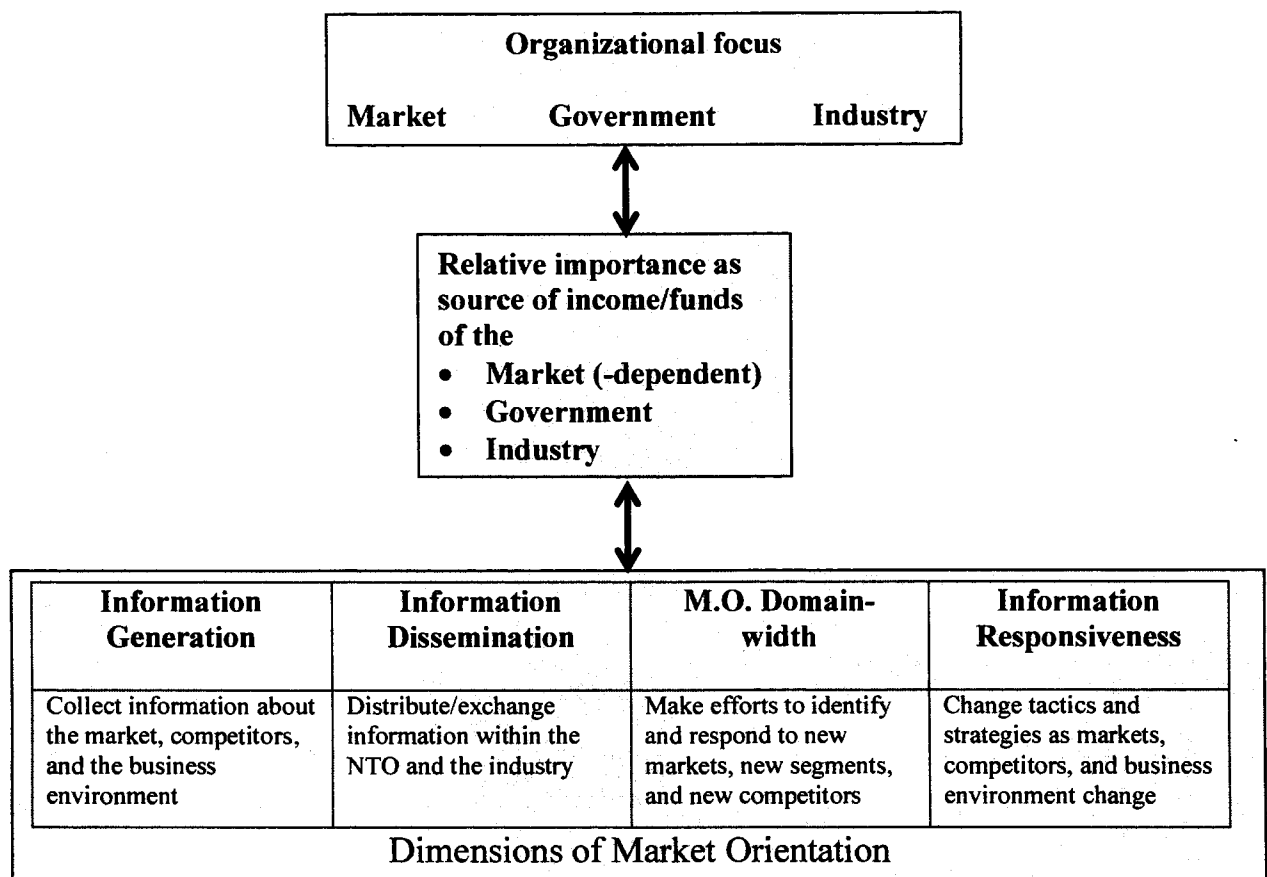
**Figure 2.2**  
**A comparison of NTOs and commercial organizations**



Market orientation and proper focusing of NTOs should be a long-term, continuous process. True NTO market focus requires investment of considerable resources, planning, and industry coordination efforts over time. When an organization like an NTO is not made dependent on the market for its income, it has few real incentives to spend or invest the majority of its resources on activities directed at the market. It stands to reason that the more a rational organization is dependent on a given source of revenue, the more attention will be devoted to the source. Its organizational focus and its orientation toward its market should thus reflect the degree to which the NTO is dependent on e.g., the government for its economic resources.

The double-pointed arrows in the Figure 2.3 illustrate that the relationships between source of income/funds on one hand, and organizational focus and market orientation on the other, may be two-way. An NTO that deliberately pays attention to a given stakeholder may also as a consequence receive more resources from the same stakeholder. On the other hand, a given stakeholder that provides an important part of the NTO's resources will also *require* more attention and influence on the organization.

**Figure 2.3**  
**The relationship between organizational focus and market orientation and the importance of different sources of revenue**



By *focus* we refer to *market-*, *industry*<sup>14</sup>-, or *government*-orientation as the dominating strategic focus of the NTO in question. In Figure 2.3 *organizational focus* and *market orientation* are treated as separate factors. This illustrates that although *organizational focus* and *market orientation* probably are related; a focus on e.g., government or industry does not preclude a strong market orientation. It is not impossible that e.g., government or industry *requires* a strong market orientation of the NTO as a condition for financial support. We use the term *market focus* in this study to encompass an organizational focus on the market, including market-oriented activities. So by the term market focus we mean that the organization's main focus is first and foremost on the market as opposed to the financial sponsors or owners. Such a focus also includes the organizational activities and attitudes described in the market orientation literature.

However, if the NTO has few or weak incentives to focus on the market through a performance-based principle that rewards market results, it could instead have stronger incentives to focus on gaining support from its owners. Aside from financial support as discussed earlier, such support can be of more political character to retain legitimacy or goodwill, or support for NTO management or employees' career aspirations or personal agendas. So without a market incentive, the NTO could be more susceptible to spend resources to cater to its owners rather than investing resources on market-oriented activities.

The market orientation theory has been centered on commercial organizations. The discussion in this body of theory also assumes that the management of the organization has the discretion to set its own goals and decide on its strategies and activities. It may very well be so that the owners would not be market-oriented themselves, and try to influence the organization to perform activities that run counter to a market-oriented strategy. For instance, the owners may have a strong product focus rather than market focus, and would try to force or influence the NTO to promote certain products or special interest. In order for an organization like an NTO to be able to be market-oriented, the organization will need at least some degree of autonomy and discretion without undue interference from owners. In other words, an organization like an NTO needs some amount of Operational Freedom in order to be capable of deciding on strategies and activities that are in line with a true market focus.

#### 2.1.4 Conclusions from market orientation theory

Market orientation research generally suggests that organizations should assign more resources to market-oriented activities and adapt the organization to facilitate market orientation. This will lead to better performance for the organization, and thus should be implemented (Sandvik, 1998). Narver and Slater (1990) also emphasize the importance of a long-term focus as related to market orientation, and that long-term focus will be beneficial for the organization's performance. The majority of empirical studies conducted on the effects of market orientation support the notion that market orientation has positive effect on organizational performance.

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<sup>14</sup> By the term *industry* we refer to non-government business stakeholders with interests in the tourism sector (i.e., tourism, as a demand-based phenomenon, cuts across many traditional industries).

Unlike commercial companies NTOs have no direct financial incentive to invest resources in market oriented activities, because it is not directly dependent on market performance for survival and prosperity of the organization. From a governance perspective, it may be necessary to introduce an incentive for market focus by making the organization somewhat dependent on the country's market performance. This may encourage NTOs to reduce their focus on the sponsors and/or owners of the organization, and turn more of its attention towards the market. It may also encourage NTOs to try to influence the industry to become more market-oriented, and induce NTOs to provide the industry with market-oriented advice on e.g., the application of the four P's of marketing. NTOs would then benefit from a market-oriented industry as well, because NTOs' budget would depend on the industry's market performance. All of these aspects call for the use of outcome-based budgeting principles i.e., budget resource-rewards based on market performance. As shown in Table 2.2, a behavior-based budgeting principle e.g., budgets based on plans and activities, may not alone provide the desired incentives for market focus of NTOs.

**Table 2.2**  
**Conclusions from application of market orientation theory**

<b>Theory</b>	<b>Consideration</b>	<b>Relevance in the NTO context</b>	<b>Attractive to use behavior-based control</b>	<b>Attractive to use outcome-based control</b>	<b>Recommendation about governing principle to use</b>	<b>Comments/ references to theory area</b>
Market orientation	Market orientation is beneficial for a company	Little natural incentive for market orientation	NO	YES	Outcome-based budgeting	Market orientation theory assumes a commercial context, while NTOs are not subject the same impact of market forces
	Market orientation entails information generation, dissemination, and responsiveness	NTOs must be motivated to use market information	NO	YES	Outcome-based budgeting	Since NTOs are not normally dependent on the market, incentives are to collect information about sponsors/owners
	Market orientation also entails customer orientation to achieve SCA, and appropriate competitor orientation	NTOs must be motivated to focus on the market and on market competitors	NO	YES	Outcome-based budgeting	Market competitors are not NTOs' real "competitors", competitors may be other bureaus/agencies or marketing organizations competing for funds
	Long-term operation is considered vital for a market-oriented focus	NTOs must be motivated to adopt a long-term perspective	YES	YES	Both outcome- and behavior-based budgeting & joint funding (ref. Section 2.5.5 later)	It is a short-term focus under most current budgeting regimes; budgets are determined from one year to another. Lobbying and negotiation incentives for NTO.

Market orientation theory is important in terms of the efficiency and effectiveness issue of organizations involved in marketing activities. Market orientation theory provides substantial theoretical grounds and empirical evidence that market oriented organizations

are, in general, higher-than-average performers in terms of business profitability or other measures of market success. Market orientation theory then is useful to identify what market oriented behavior is, and what organizational activities it entails, which can be applied when pointing out the activities an NTO should enact in order to perform well in a competitive market. So this has value as normative theory. However, market orientation theory does not really explain *what makes organizations become market orientated*, e.g., what factors foster market orientation. This question is one of the key aspects in this study. Furthermore, market orientation theory typically assumes a commercial context, where market control will provide an “automatic” incentive for market focus (at least from a Darwinist or evolutionary point of view). In other words, organizations that are not market-oriented are probably assumed to perish sooner or later faced with market competition. However, most NTOs are not commercial organizations, and do not face the threat of bankruptcy present in a commercial-competitive context. Thus, NTOs may very well survive and grow without being market-oriented at all. Considering this, we draw the conclusion that existing market orientation theory is quite useful, but far from sufficient, to address all the important issues of this study.

## 2.2 Agency theory

We will now leave the somewhat microeconomic perspective of market orientation theory, and attempt to add some inter-organizational perspectives derived from parts of organizational theory. The parts of organizational theory we will discuss, namely *agency theory* and *public choice theory*, deal with the hierarchical control of organizations. Two sub-parts of agency theory will be discussed here as it relates to the NTO context. Those are *common agency* and “*traditional*” *agency theory*.

### 2.2.1 Common agency

A special form of agency is analyzed in this thesis, namely *common agency*, which is the case where one agent relates to several principals, or what Meyer (1979) denoted as a situation when public officials [or organizations] serve dual masters. NTOs responsible for international marketing on behalf of a country’s tourism industry can be classified as an agent subject to multiple stakeholders<sup>15</sup>. Stakeholders in the NTO context range from national to local level government, public and private national and local trade organizations, and public and private businesses within or with interests in the tourism industry. This is a different situation than what is often assumed in traditional agency theory (e.g., Conlon and Parks, 1988; Anderson, 1985; Eccles, 1985; Eisenhart, 1985, 1988, 1989; Kosnik, 1987), where the typical unit of analysis is the hierarchical relationship between one principal and one agent. The principal-agent relationship is also usually implicitly assumed formalized in some sort of explicit contract between the parties.

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<sup>15</sup> In this context we have chosen to use the term *stakeholders* instead of *principals*, since not all parties with interest in the organization actually compensate the organization for its services, and thus are not *principals* in the exact meaning of the term as used in traditional principal-agent theory. (See Figure 3.3 and 3.5 for an overview of NTO stakeholders).

The inter-organizational relationship in the NTO context between several stakeholders, who may consist of both sponsors and non-paying beneficiaries/clients/constituents, and a national generic marketing organization, can be considered a common agency. NTOs can be organized as a public agency/bureau, a private industry-led organization, or some combination or hybrid of the two. Not all relationships between the organization and its various stakeholders are governed by formalized contracts, not all stakeholders compensate the organization directly for the benefit of its services, and not all of the stakeholders are readily identifiable. Neither do all important stakeholders necessarily possess the formal and legitimate control of the agent, such as in a hierarchical relation typically assumed in traditional agency theory.

**Table 2.3**  
**Agency (and transaction cost) theory's relevance for independent and dependent variables**

<i>Independent variables' relevance for study</i>		<i>Reference to text</i>	<i>Dependent Variables' relevance for study</i>		<i>Reference to text</i>
<i>Budgeting principle</i>	1) Information asymmetry could result in moral hazard and adverse selection. Goal conflict between agent and stakeholders can occur, and NTO can "get away with" less than optimal effort due to unobservable behavior. 2) Stakeholders can either monitor the NTO through behavior-based budgeting (Monitoring structure # 1) or seek alignment of goals via transfer risk through performance-based budgeting. Risk-transfer also has some costs and benefits. 3) Both Stakeholders and NTO incur transaction costs as control and monitor cost and maladaptation cost when behavior-based control is used.	2.2.2  2.2.3.1  2.2.4  2.2.5  2.2.3.4	Market Orientation	Market-oriented activities cost organizational resources. Due to unobservable behavior, an NTO could be able to avoid being market-oriented, and use too many resources on shirking and non-marketing activities, unless the NTO is controlled by its stakeholders. Probably the best thing to do is to introduce performance-based budgeting principles to motivate the NTO for increased M. O. In this way marked results are tied to rewards and punishments for the NTO, which gives incentives to focus on the market.	2.2.2 & 2.2.2.2
<i>Funding source</i>	The stakeholders can influence the NTO and "purchase" information about NTOs' behavior through a role as financier. (Monitoring structure # 3)	2.2.3.3	Long-Term Perspective	The long-term nature of contract relationships between NTO and its governing stakeholders should reduce the need for outcome-based contract (i.e., performance-based budgeting)..	2.2.5.5
<i>Ownership/control</i>	1) The common agency-situation with one agent (NTO) and multiple stakeholders could create problems in terms of vague authority and goal establishment. 2) The stakeholders can monitor the behavior of the NTO through ownership/control (Monitoring structure # 2).	2.2.1 (ref. also 3.1 and Fig 3.2 in Ch. 3)  2.2.3.2	Operational Freedom	Active use of monitoring structures such as behavior-based budgeting (Monitoring structure # 1), ownership control (Monitoring structure # 2), and funding influence (Monitoring structure # 3) limit NTOs' Operational Freedom. (This is not necessarily a bad thing, as long as intervention by stakeholders is professional and market-oriented in nature.)	2.2.3



For instance, the tourism industry or taxpayers may not have such formal control when the NTO is government owned and funded (see also Figure 3.3 and 3.5 for an overview of stakeholders). Thus, some of these stakeholder-agent relationships can be quite blurred. The NTO may not be fully aware of who its real “masters” are. This makes comparisons with the typical common agency situation somewhat difficult.

Furthermore, the agent (NTO) may not know exactly who the ruling coalition of stakeholders is, its preferences or resources, or the “true” price of the NTO’s operation and existence (cf. Jensen and Meckling, 1976). In addition, there might even be conflict of interests *among stakeholders*. This can make both the NTOs and their stakeholders question whom NTOs should relate to in terms of authority, what this “authority” really wants, and how many resources NTOs really need. All of these particular NTO-related circumstances make the situation far more complicated than in single dyad contract relationships between one agent and one principal as often assumed in traditional agency theory. These special agent–stakeholder relationships in the NTO context will be discussed in more detail later in this chapter and again in Chapter 3.

### 2.2.2 “Traditional” agency theory

Despite these challenges, agency theory raises a few issues useful for our discussion and has some traits and that can be applicable, at least to some extent, in the NTO context. *Agency theory* (ref. Baiman 1982, 1990; Eisenhart 1985, 1988, 1989; Levinthal, 1988; Moore 1981; Scapens 1985, for reviews) is about organizational control under uncertainty in general, and deals with the efficient organization of information and risk bearing cost in contract relationship between the agent and principal. Common problems addressed in agency theory, are the existence of asymmetric information, adverse selection and opportunism. *Asymmetric information* is the situation where some actors in the transaction process have access to more information than others. *Opportunism* may be defined as self-interested behavior unconstrained by morality (Milgrom and Roberts, 1992). Agency theory directs attention to the possibility that some agents could behave opportunistically and utilize asymmetric information, but not that every agent will do so.

Even though not all relationships between the stakeholders and the NTO are formally controlled by explicit contracts, (at least some of) the stakeholders have licensed activities to the organization in return for funds allocated/contributed to finance these activities and the operation of the organization. These contributions may exist in the form of direct contributions, or indirectly through public funds from taxpayers ‘money. The agreement, that the organization will perform marketing activities in return for budget allocations/contributions from the stakeholders, can then be considered an *agency relationship*, regardless of whether this agreement is formally stated or implicitly made. Formally, an *agency relationship* is defined as a contract under which one or more persons/entities (the principal(s)), engage another person/entity (the agent), to perform some service on their behalf, which involves leaving some decision-making authority to the agent (Jensen and Meckling, 1976). The discussion of these agency relationships between the principals (stakeholders) and agent (NTO) may be applicable both in terms of profit organizations, government/public agencies, and non–profit organizations, since

important decision agents do not necessarily bear a close share of the outcome of their decisions (Farma and Jensen, 1983).

Agency theory can be quite useful to understand how the relationships between the NTO and its stakeholders best can be governed. The “contract”-relationships within the NTO-context are all subject to the same problems as outlined in traditional agency theory: 1) the potential goal conflict between stakeholders and agent; 2) the difficulty and expenses on the part of stakeholders associated with monitoring the activities of the agent; and 3) the problems with risk-sharing and differences in attitudes toward risk between principal and agent (e.g., in terms of compensation, regulation, leadership, impression management, etc.) as outlined by Eisenhart (1989).

As we will discuss later in Section 2.2.3.4, *transaction cost theory* (Williamson 1985, *et al*) can be useful to identify some of the various organizational costs related to the different alternative administrative systems that are set up to govern these contract relationships.

### 2.2.2.1 Goal conflict

Most organizations exist for a purpose - and inherently have some goals for their existence. In general terms these goals are mainly of two kinds: *external* and internal. *External* goals reflect the needs and interest of the organization’s external constituency and are tied to the achievements of the organization that result from interaction with its business environment. Such goals may be in terms of profitability, welfare of the various stakeholders, or the promotion or advocacy of some cause or interest of groups of people or organizations. External goals are often explicitly expressed in mission statements of organizations.

The *internal* goals on their side may be quite different from the external goals, and sometimes even be in *conflict* with the latter. Internal goals may e.g., be to ascertain the survival, prosperity and growth of the organization; to ascertain job security (and career paths) of employees; to secure the welfare of the employees (including management) or even to take advantage of resource slack for consumption in leisurely activities (shirking). In agency theory, these goals are subsumed in the term *self-interest* of the agent.

A problem arises when these internal and external goals are not aligned, i.e., that there is an implicit incentive for the agent to maximize self-interest on the expense of the stakeholders’ interests. Given the problem of self-interest of the agent and differences in goals, the stakeholders are faced with a monitoring problem if the stakeholders cannot determine if the agent has behaved according to the interest of the stakeholders. In other words, the information problem is that the stakeholders do not know the activities, efforts, output or slack in the agent organization.

In the context of the NTO, the NTO may not have overlapping interests with the NTA and other stakeholders. For instance, it may be so that the NTO would want a high budget or payment for a low effort. In a situation where the principals could easily evaluate the

NTOs effort, this would only be a minor problem. The principal-agent-problem arises from at least three information difficulties:

1. *Effort*: The stakeholders, e.g., NTAs and/or industry/public, cannot directly observe and monitor NTOs' actions, or it would be very costly to obtain such information.
2. *Outcomes*: It is difficult, or at least very costly, for the stakeholders to measure the quality and the quantity of NTOs' production of marketing services.
3. *The relationship between effort and outcomes*: The outcomes, e.g., level of incoming tourism traffic, do not solely depend on NTOs' effort, but also on other aspects more or less beyond NTOs' control, such as international market conditions, political situation, currency exchange rates and so on. It can be hard to determine to what degree the outcome is a result of NTOs' behavior or other external aspects.

These information problems will be discussed in the following sections.

### 2.2.2.2 Unobservable behavior

Organizations responsible for international generic tourism marketing face a complex marketing task. First of all, the NTOs do not have the direct control of the products themselves nor the sales closure process related to the exchange of these products, which increases the uncertainty of NTOs' market-performance outcome. Even if the organization "does everything right", the industry could deliver low quality products or put in insufficient effort, which then could influence NTOs' market-performance negatively. Furthermore, the organization will have to identify, gain consensus on internally, and get endorsement from various stakeholders with regards to a few common, communicable tourism product characteristics. This can be difficult, considering the many heterogeneous tourism products and services made available from a number of domestic suppliers, who all would like to have their particular products and services promoted. We have also mentioned before the problems associated with conflicting goals among the various types of stakeholders. Furthermore, the market communication of the various product characteristics will have to be made somehow differentiable in relation to competitors' products. Multi-market international tourism marketing is a demanding task because of the distance both geographically and culturally between the businesses in the industry, the NTO, and the various customer markets. It may not be readily identifiable what the customers' preferred bundles of product characteristics are - preferences that may be different from one key market to the other. Therefore, it can be very difficult for the various stakeholders to determine exactly what organizational actions would be most effective to generate increase in the demand for the various types of tourism products/services in question. This should in fact be the very reason why one has an NTO in the first place, since the agent (NTO) is supposed to have more special competence than the stakeholders related to this particular marketing task. The marketing task can be so complex that it is not easily assessable for the stakeholders what would be the best courses of action. The task-assessment problem can make it hard for the stakeholders to detect whether the agent puts forth the assumed/agreed upon effort or not. This control problem is referred to as *moral hazard* in agency theory (Eisenhart 1989, p.61).

Considering this task complexity, it can also be difficult for the stakeholders to judge the competence of the NTO and its human resources, and thus whether any alternative marketing channels would be more effective or efficient. Such alternative channels can for instance be local or international tourism marketing organizations or private marketing companies. In the NTO context, the stakeholders have licensed marketing and other operational activities to the agent organization, which is itself in a superior position to evaluate the activities delegated to it. This situation can cause *adverse selection* of the marketing agent (ref. Eisenhart 1989, p.61) in favor of alternative marketing activities or organizations, or the industry stakeholders' own marketing efforts. In a situation, where the behavior of the agent is uncertain or unobservable, agency theory predicts that an outcome-based contract could be attractive to the stakeholders. It will make the agent more likely to behave in the interest of the stakeholders i.e., limit its expenses and increase effort, since rewards for all parties depend on the same outcomes.

Ouchi (1979) asserted that the principal monitors behavior if outcome is uncertain, or monitors output if behavior is uncertain. In an agency relationship under uncertainty and asymmetric information, it could be rational both for the stakeholders to monitor the agent, and for the agent to bond its expenditures, in order to minimize the residual welfare loss (Jensen and Meckling, 1976). The NTOs' stakeholders are faced with the problem of unobservable behavior on the part of the NTO due to possible moral hazard and adverse selection, and have in general two different options:

- 1) *Investment in information systems* that reveals agent behavior (behavior monitoring), such as behavior-based budgeting systems, boards of directors, reporting procedures, and additional layers of management.
- 2) *Transfer of risk* (outcome monitoring) through outcome-based contracts (i.e., performance-based budgets).

### 2.2.3 Stakeholder control through investment in information systems (Behavioral monitoring structures)

Information systems in the NTO context can be categorized in three types of *monitoring structures* available for the stakeholder coalition. These are monitoring through *behavior-based budgeting-principles*, through direct *organizational control*, or through indirect influence by way of being the *funding source*.

#### 2.2.3.1 Monitoring structure #1: Behavior-based budgeting principles

The stakeholders can monitor the actions of the organization by investing in several forms of information systems. For instance, this is possible by using behavior-based NTO budgeting principles. One way is to use a procedure where the stakeholders participate<sup>16</sup> in the decision process for the organization's marketing plans and activities for a given time period, and then determine the organization's budget on the basis of the expected

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<sup>16</sup> By the term "participate" is meant that the stakeholders will have an active role in determining the organization's plans and activities, or goals and operational objectives. The more control/discretion in this procedure the stakeholders possess, the more the budgeting principle will take on the characteristics of a behavior-based contract.

cost related to the activities to be performed. Another way can be to base the budgets of the organization on contract-specific projects, where sponsoring stakeholders specify the content and activities to be performed in the project. A third way can be for the stakeholders to outline some broad and general goals and activities through negotiations with the NTO and allocate a fixed sum to the organization's budget each period based on these goals and activities. This is analogous to salary-pay on the individual person level. Common for these three behavior-based principles mentioned above is that the stakeholders can *after the fact* evaluate whether the NTO has carried out the actions as agreed upon and reward/"punish" the NTO accordingly. All these three budgeting principles i.e., plan and activity-based, project-based or negotiated fixed sum, are in principle *behavior-based*. They are all designed to gain some control of the behavior of the organization through information systems that reveal agent behavior.

These three principles represent a kind of *input control* through traditional budgeting negotiation processes. Wildavsky (1986) argued that this form of budgeting continued as the dominant form despite the availability of more "advanced" management controls such as planning, programming and budgeting systems (PPBS), and performance measurement. According to Wildavsky, as the traditional budgeting process does not score the highest judged by the criteria a manager could put forward for a management control model, for instance simplicity and information about output, the traditional process still matches these criteria best in total. A large budget in a large and complex organization may therefore call for the use of the traditional (input control) processes rather than control through performance measurement (Johnsen, 2000). NTOs can sometimes be large, complex organizations including domestic and foreign branch units with numerous tasks, sizable budgets with many line items; several outputs; and many stakeholders (see also section 3.1). This may partially explain why so few NTOs are subject to performance-based budgeting principles, despite the merits of such principles.

### 2.2.3.2 Monitoring structure #2: Organizational control

A second form of investment in information systems is to assure that the coalition of stakeholders maintain the organizational control of the organization. *Organizational control* is defined as the theory which specifies the difference between executive choice in an organization and the decisions actually implemented (Cyert and March, 1963/1992). Control has also been defined as any process in which a person, a group of persons, or organizations determine or intentionally affect the behavior of another person, or group, or organization (Tannenbaum, 1968). Organizational control comes from the knowledge that someone who matters to somebody in an organization pays close attention to what is going on and tells the latter if the behavior is appropriate or inappropriate (Pfeffer, 1997). This kind of control allows stakeholders to closely monitor the actions of the NTO, and functions as an information system that reveals agent behavior. Organizational control processes encompass recruitment and selection, training and socialization, organizational design as decentralization, leadership, planning and implementation, accounting and auditing, use of incentives, and monitoring and evaluations. The ruling coalition of stakeholders can gain representation on the organization's board, so that the stakeholders can influence the actions and decisions of the organization. According to Eisenhart (1998) "the richness of information can be measured in terms of board characteristics

such as frequency of board meetings, number of board subcommittees, number of board members with industry experience, and number of board members representing specific (interest- or) ownership groups". Thus, the access to this kind of information system through organizational control is likely to reduce stakeholders' need for outcome-based contracts.

### 2.2.3.3 Monitoring structure #3: Influence through funding

The World Health Organization (WHO) has many features similar to an NTO (as we will discuss in more detail later in Section 2.5.1). In a critical study of the WHO (Peabody, 1995) it was reported that Member States demanded, in exchange for political support and financial contributions, a countryman or woman in a particular position. Not surprisingly, Member States who pay a large percentage of the regular budget, or donate to special programs, secure many of the senior positions in the WHO (Peabody, 1995). Thus, the WHO case exemplifies that influence on a supposedly neutral, non-profit and ideal organization can be "bought" through organizational funding. (Please note that this is not to be confused with outright corruption, which is not to be discussed here.) It is also likely that a financial sponsor of the NTO could demand influence or positions in the organizations Board of Directors. We can call this means of organizational influence *financial authority*.

If we revert back to the discussion on agency theory, this theory views information systems as a *purchasable commodity* (Eisenhart, 1989 p.59). Information systems often represent limitations on the organization's decision autonomy. The agent organization would probably require some form of compensation in exchange for giving up this potential autonomy. In the NTO context the stakeholders can to some extent "purchase" information systems by contributing funds or financing the organization, in exchange for influence on planning of activities or goal establishment. Furthermore, the sponsoring stakeholders can control the organization's behavior by introducing reporting procedures so that the organization will have to report on its activities and related expenses to the stakeholders on a frequent basis. Such investment systems also reveal the agent's behavior to the stakeholders, and the organization is more likely to behave in the interest of the stakeholders. Even if provision of funds does not necessarily give the sponsor access to formal control e.g., through board representation it is still likely that the organization would either be required or feel obligated to inform the sponsor on its activities and its operation. Thus, the sponsor will have some legitimate influence on the organization's behavior. The sponsor or financier will probably require the agent to keep him informed on the actions and resource-expenditure of the organization, unless the organization will keep the sponsor informed voluntarily. Roles as sponsor and organizational-controlling entity often overlap, but it is not necessarily always so. The role of a funding sponsor may therefore allow influence over the organization without formally controlling it through organizational ownership.

### 2.2.3.4 The cost of information systems

*Transaction cost theory* (Williamson, 1975, 1985) identifies the cost associated with this kind of behavioral control through alignment-of-interests-processes. In the process of determining the next period's budgets for the organization based on any of the behavior-

based budgeting principles, bargaining is necessary to safeguard the interests of both stakeholders and the agent. The amount of goal conflict among stakeholders, between stakeholders and agent and the frequency of bargaining are all factors likely to increase the transaction cost of behavior-based budgeting control.

In transaction cost theory the investments in information systems are termed *control and monitor cost*. These are the resources spent to monitor whether transactions are consistent with the principal-agent contract. In the NTO context, these are the costs incurred by the stakeholders to monitor that the organization performs activities and behaves in the interest of the stakeholders, as well as the costs associated with budget negotiations. On the part of the agent NTO, costs are incurred by the organization itself to promote its interests to its stakeholders. This includes both justifiable transaction-efficient bargaining activities, as well as more resource inefficient behavior related to lobbying, justification-for-existence and impression-management efforts directed at the controlling and/or funding stakeholders.

Even if the stakeholders may invest considerable resources in information systems, these systems will still produce some information that is invalid and imperfect as input in the decision process. In transaction cost theory this is referred to as *maladaptation cost*, which represents the communication and coordination failures between the stakeholders and the organization. These costs reflect resources used to produce information that is not absorbed by the other part of the transaction (Williamson, 1985).

## 2.2.4 Stakeholder control of the agent through transfer of risk

An alternative to behavioral control of the agent through information systems is *the transfer of risk from stakeholders to the agent*. In the NTO context, this could be achieved through introduction of performance-based budgeting systems. In agency theory this is referred to as outcome-based contracts.

### 2.2.4.1 Benefits of risk transfer to the agent

*Risk* can be understood here as the way possible losses and gains can be derived from an action (Clark and Montgomery, 1986). Agency theory suggests that an outcome-based contract motivates alignment of preferences, because rewards for both stakeholder and agent depend on the same actions, which will curb agent opportunism. This will shift the risk of outcome from the stakeholders to the agent. It means to “reward or punish” the organization on the basis of the outcome of its actions, and not on its behavior. The purpose of risk transfer through performance-based budgeting is to align stakeholder and agent goals through common dependence on the same outcome. A major advantage is that it reduces the stakeholders’ need to monitor the agent. Thus, it reduces the stakeholders need to control the organization through information systems, including the stakeholder and agent transaction cost of such systems. For instance, it reduces the importance of maintaining monitoring structures number 1, 2 (and 3).

By the same token, acceptance of higher risk by the NTO may also be traded for increased operational freedom, which means a relaxation of the stakeholders’ control through any of the information systems we discussed earlier. It gives the agent increased decision autonomy, which in turn will increase the organization’s control of its own

operation, and thereby decrease its perceived uncertainty of outcome. This may reduce propensity for the NTO to demand a risk premium in the form of higher budgets. Furthermore, it may reduce the potential efficiency losses due to constraints imposed on the NTO by the ruling coalition of stakeholders.

#### 2.2.4.2 Risk-transfer devices

In practice, risk-transfer can be done by basing the budget of the organization on what the country achieves in terms of incoming tourism. A desired increase in tourism is a beneficial outcome for the stakeholders. Such budget principles assume that the increase or decrease in tourism traffic can be somewhat attributed to NTOs' actions. For instance, the sponsor coalitions could base the "reward" (i.e., an increase in NTOs' budget amount) of NTOs on the absolute increase in number of incoming tourists or tourism receipts, or as a portion of tourism-related tax revenue (See Appendix 7 for an illustration). This is analogous to sales-commission payment at the individual person level. Another alternative, which also serves the purpose of reducing the perceived risk of the NTO agent, is stakeholders to base the agent's compensation relative to the performance of other NTO agents. In the NTO context this would be to base the compensation on a measure relative to the performance of other "comparable" NTOs or countries. The performance-measurement determining the reward as the budget amount can be made relative to the market performance of other comparable countries that are subject to similar market conditions and have similar tourism products (see Table 5.1 for a more detailed explanation).

In this way the role of chance events can be reduced, since both the agent in question and other agents are all exposed to roughly the same chance events. This is a performance scheme sometimes referred to as *tournaments* (Nilakant and Rao, 1994). A similar procedure is known as *benchmarking* through the DEA-model for public sector efficiency measurement (see Johnsen, 2001:14 for details).

A hybrid solution between behavior-based and performance-based principles is also possible. This can be done by allowing stakeholders to participate in the establishment of specific goals and operational objectives (behavioral component), and then base the budget of the organization on the achievement of these goals and objectives (outcome component). This procedure is similar to the human resource management technique known as Management By Objectives (MBO).

#### 2.2.4.3 Potential negative consequences of transfer of risk

Transfer of risk through performance-based budgeting may be valuable as an incentive for the NTO to be more market-oriented and a catalyst for resource efficiency. But this transfer of risk may also create some problems: An NTO is faced with a number of business environment conditions that are likely to influence the outcome of the organization's actions. Factors such as: sudden change in government policies or other stakeholders' actions, economic climate, competitor actions, and tourism product characteristics could generate more or less uncontrollable variations in outcome for the NTO as an agent. In addition, NTOs have only limited or no direct control of the



product/service, price, and distribution parameters of the marketing mix. Furthermore, since most NTOs are not actually handling the sales transaction of the tourism product or service to the end-user, it is difficult for the NTOs to ensure appropriate sale closure, e.g., so that the tourist actually purchases a flight ticket or hotel room that will assure their arrival. This responsibility is left to the businesses or service providers in the tourism industry. Since the commercial or industry operator is left with the direct control of the product and sales, it decreases the controllability of the NTOs' business environment. In other words, it is hard for NTOs to control that the industry actors are doing their part of the job in getting tourists to visit their country. Therefore, it may be hard to determine if the outcome in terms of market performance can be attributed to the actions of NTOs or by any of these uncontrollable conditions, because cause-and-effect relationships are ambiguous (see also section 3.1 later for further details). Thus, neither the organization nor the stakeholders will not know for sure that a given activity or behavior will lead to the desired effects. This has at least two consequences 1) Developing valid measurements and measuring the direct effects of NTOs' behaviors may be difficult or costly. 2) It introduces outcome uncertainty, and consequently limits the organization's ability to pre-plan.

Kahneman and Tversky (1979) refer to what they term "the certainty effect" (prospect theory). This theory states that individuals tend to want to avoid risk in choices involving sure gains. This knowledge can be applied to organizational behavior as well, since management teams of organizations are made up by individuals who are faced with decisions under uncertainty. Transposed to the stakeholder-agent context, this should predict that the agent would favor behavior-based contracts in the form of behavior-based budget principles when uncertainty is high, because these contracts will yield "sure gains". Such sure gains can be in the form of predetermined income, such as budgets based on a fixed sum each period or any other behavior-based budgeting-principles. It will also predict that organizations will resist acceptance of risk as uncertainty increases, and it will become increasingly expensive to shift risk to the agent despite the motivational benefits to behave in the interest of the stakeholders. In other words, the agent would probably demand some kind of compensation in order to accept higher risk, for instance in the form of higher budgets. Agency theory predicts a risk premium to the agent, because the principal will have to increase the agent's overall total compensation in order to protect the agent from risk (Stroh, Brett, Baumann and Reilly 1996).

Another consequence of shifting the risk of outcomes to the agent is that it is likely to decrease the agent's willingness to take on additional *operational risk*. Operational risk means that in this case a risk-averse agent will seek to minimize activities that are perceived to increase risk, while attempting to engage in activities that are less risk-laden. Within models of business competitiveness (Day, 1994), there is a recognition that constructive risk-taking is an important factor in stimulating entrepreneurship (Miller, 1987) implicit in market opportunity-seeking behavior (Baird and Thomas, 1990). As risk-aversion increases, the organization is likely to resort to activities known to have been beneficial in the past, while restricting activities associated with greater uncertainty of outcome, such as new product development, entrance into new markets, investments in brand building etc. The danger of shifting risk to the agent is that the agent will restrict its marketing attention to existing customers and competitors and become subject to the

“tyranny of the served market” (Hamel and Prahalad, 1991, p.83). Focusing on existing markets and competitors can be perceived by the agent to be more “safe”, at least in the short run. For the agent, market-oriented behavior represents investments of resources in activities with an uncertain outcome, and thus has an element of risk attached. “Despite the fact that businesses’ [NTOs] gains and losses may be high from new product introductions serving both new and existing customers, market orientation requires that firms [NTOs] are tolerant to risk and accept possible failures (Jaworski and Kohli, 1993). Consequently, transfer of risk to the agent may reduce the agent’s willingness to engage in entrepreneurial activities and the more risk-laden activities of market-oriented behavior.

## 2.2.5 Disadvantages of outcome-based contracts

Thus, for the stakeholders there is clearly a trade-off between a) the cost/benefits of measuring behavior through investment in information systems and b) the cost/benefits of measuring outcomes and transferring risk to the agent NTO.

### 2.2.5.1 Risk aversion of stakeholders and agent

To get a better understanding of different situational contexts it may be fruitful to relax the assumption of a risk-averse agent (e.g., Harris and Raviv, 1979). For instance in the case where the agent is wealthy enough to easily absorb any negative consequences of an undesirable outcome, the agent is likely to become less risk-averse. Likewise, the agent may become less risk-averse if he perceives to be able to control the business environment and possess resources, e.g., human capital, organizational experience, networks, technology, etc., which enables the agent to better control the outcome of activities. Thus, outcome uncertainty will be reduced, and so will the perceived risk by the agent.

As the agent becomes increasingly less risk-averse, it becomes more attractive to pass on the risk to the agent using outcome-based contracts. Conversely, as the agent becomes more risk-averse, it is increasingly expensive to pass risk to the agent (Eisenhart, 1989: 62). Thus, behavior-based contracts become more attractive. Similarly, it becomes increasingly attractive to pass on the risk to the agent if the stakeholders are risk-averse.

NTOs are, with a few exceptions, not particularly wealthy organizations with large *discretionary* budgets and savings to buffer NTOs in hard financial times. Likewise, they face a business environment that is highly uncontrollable, while cause-and-effect relationships are ambiguous, and uncertainty of the outcome from their actions is fairly high. Generally, this would cause these organizations to become quite risk-averse. Furthermore, the collective risk of the stakeholders is distributed across a large number of individual stakeholders, so that no single stakeholder or group will alone have to bear the negative consequences of a potential negative outcome. Such a negative outcome could be the result of e.g., a poorly performed major marketing campaign by NTOs or any other strategic or operational mistake. In addition, industry stakeholders often invest resources in other marketing channels such as: own marketing activities, local-level tourist organizations, trade associations, private marketing firms, etc. Under these circumstances

NTOs will only constitute one agent in a portfolio of several agents or risk-objects. This will reduce the stakeholders' perceived risk attached to the single agent NTOs represent among all agents or risk-objects. Furthermore, in cases where the government is a major stakeholder, e.g., being a major funding source, which is often the case, government funds spent on NTO budgets will not have the same strict requirements for return on investment as private funds do. This could in sum suggest that we are dealing with a stakeholder coalition with a fairly *moderate* collective risk perception. However, the degree of risk-aversion of this group is unknown, since risk aversion is a personality trait or "organizational" trait.

Therefore, one can probably argue that stakeholders in the NTO context are only moderately exposed to risk in the agency relationship with the NTO. Assuming then, a high agent risk-perception and moderate-to-neutral stakeholder collective risk perception; behavior based-type contracts become attractive as opposed to outcome-based contracts in the relationship between the stakeholders and the NTOs.

### 2.2.5.2 Relaxation of the assumption of goal conflict

It can also be fruitful to relax the assumption of goal conflict between the stakeholders and the agent. Agency theory has been criticized for exaggerating the degree to which individuals (and organizations) are work-averse (Perrow, 1986). This might occur in situations where self-interest gives way to selfless behavior. For instance, when the agent employs highly professional human resources genuinely interested in their work; or when these employees are strongly motivated by non-monetary rewards such as recognition from stakeholders groups - the agent might act according to the interests of the stakeholders. This could happen even though the agent could have "gotten away with" less than the assumed or agreed upon marketing effort. In other words, even if there is a potential *moral hazard* in the relationship between the marketing agent and the stakeholders, the agent may very well refrain from adversely exploiting its position to evaluate the activities delegated to it. Management and employees' professional "pride" and motivation from rewards other than benefits through shirking can reduce the moral hazard problem. It seems safe to assume that such underlying motivations may have a positive impact on the more "selfless" actions of the agent, particularly since most of the NTOs are non-profit organizations - and therefore are not necessarily dependent on maximizing own monetary utility. According to Eisenhart (1998: 62), as goal conflict decreases, there is a decreasing motivational imperative for outcome-based contracts. Under such circumstances behavior-based contracts become more attractive, and there is a lesser need to transfer risk to the NTO by imposing performance based budgets. However, it is sometimes hard to *ex ante* assess the NTOs employees'/management's degree of motivation and "professional pride" ensuring that they will act in the interest of stakeholders and give up self-interest.

### 2.2.5.3 Goal conflict among principals

In agency relationships where there are several principals or stakeholders, goal conflict among principals can result in outcome uncertainty. Complex organizations such as government agencies (e.g., NTOs), hospitals and educational institutions are

characterized by multiple demands from both inside and outside the organization (Tusi, 1990). In such settings, variations in outcome may reflect multiple goals rather than effort-aversion. Only under high levels of agreement about efforts and outcomes among principals and/or between principals and agent is it possible to define precise standards for performance evaluation (Nilakant and Rao, 1994). In the NTO context, such agreements are less likely, which is reducing the attractiveness of performance-based contracts. On the other hand, potential disagreement among principals and/or between principals and agent on prescribed optimal agent behavior makes precise behavior-based contracts difficult to design as well, as explained later in section 3.1.

#### 2.2.5.4 Measurability of outcome

Another task characteristic is the measurability of outcome (Anderson, 1985; Eisenhart, 1985). Some tasks require: a long time to complete, involve stakeholder and agent joint effort, or produce soft outcomes - outcomes that may be difficult to measure within a practical amount of time. For NTOs such task may involve: brand or product/service image building, repositioning of products/services, new market venture, new distribution channel development, and new product/service development, etc. When outcomes are measured by difficulty, behavior-based contracts are more attractive (Eisenhart, 1989:62). Because of the lack of direct measurability of NTOs' behavior - supported by the fact that NTOs often face a number of uncontrollable factors that will influence the outcome of their activities, measurability difficulty will make behavior-based contracts attractive in the NTO context.

#### 2.2.5.5 Length of contract relationship

The length of the relationship between the stakeholders and the agent should also have an impact on the contract form chosen, according to Eisenhart (1989: 63). In long-term relations the stakeholders will learn about the agent (e.g., Lambert, 1983) and will be able to assess the behavior of the agent more readily. Conversely, the information asymmetry is likely to be greater in short-term relationships, making outcome-based contracts more attractive. In the NTO context, these relationships are often of a long-term character. The relationship with the government, which often is a dominant stakeholder, is usually long-term, and may last for decades. Thus, the long-term nature of relationships will tend to make behavior-based contracts attractive in relationships between the government and the NTO. The same can be true with dominant, wealthy industry stakeholders involved in long-term relations with the NTO. Conversely, relationships with other, less dominant industry partners are often of a more short-term character, such as in the case of specific time-definite projects.

#### 2.2.5.6 Programmability of tasks

Another consideration made by Eisenhart (1989) is the programmability of tasks to be performed by the agent. As defined by Eisenhart, *programmability* is the degree to which appropriate behavior by the agent can be specified in advance. According to agency theory, task-programmability will be positively related to the use of behavior-based

contracts (e.g., fixed-sum budgeting) and negatively related to the use of outcome-based contracts (i.e., variable compensation). In the NTO context, some of the operational tasks are highly programmable, while others are not. Some administrative and non-marketing tasks are to a large extent programmable. Programmable tasks can be e.g., public information and PR, distribution of promotional material, information services, representation/seminars/presentations, education services, and simple marketing research tasks such as travel statistics collection, and collection of other trade information. Other tasks are substantially less programmable, for instance acquisition and use of new technology, new product development, development of new markets, tactical and technical innovation, advanced market- and competitor research, strategic planning etc. According to Eisenhart (1989) the more programmed the task; the more attractive are behavior-based contracts. Very programmable tasks reveal agent behavior, and the situation reverts to the complete information case. In cases where NTOs are assigned typically programmable tasks only, one can expect presence of behavior-based contracts. Many NTOs are in fact not typically formally assigned the non-programmable tasks mentioned, which is in many cases considered to be the responsibility of the industry the NTO is promoting products/services for<sup>17</sup>. To the extent it occurs, the less programmable tasks are often undertaken on NTOs' own initiatives, and thus not formally tied to a behavior-based contract. In some cases, NTOs may assume those tasks in connection with specific projects. Such projects often have a stronger than usual outcome focus and agent-stakeholder shared risk.

### 2.2.6 Conclusions to be drawn from agency theory and transaction cost theory

The main aspect of this study is to find ways to give the NTO working conditions and incentives to behave in a way that will increase the chances for better market-performance. In other words, this is a matter of identifying the best combination of control and incentive mechanisms for the NTO. The principals may use those in order to induce the NTO to behave in a desirable way, as described above. The context of organizational control and incentive mechanisms as means to control behavior - lends itself to agent-principal theory. Agent-principal theory is very useful (for the principal) to understand when to use performance-based contracts and when to use behavior-based contracts as means to control the behavior (of the agent). Concepts such as *asymmetric information*, *unobservable behavior*, *moral hazard*, *risk-sharing*, etc. are useful to enlighten agency problem in the NTO context. The concepts of *common agency* (Meyer, 1979) and *transaction cost* (Williamson, 1985; i.e., agent behavior *monitoring cost*) are also useful concepts in this discussion.

From a simple agency theory perspective the NTO context would call for an outcome-based type of contract due to the potential problems associated with goal conflict between principals and agent or the stakeholder and the NTO in our case. The probable inability of the stakeholders to observe the behavior of the NTO could lead to problems with moral hazard and adverse selection. Under a behavior-based contract regime, the NTO would

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<sup>17</sup> We found some evidence for this in the empirical part of this thesis e. g., in the focus group sessions including both stakeholders and NTO, as well as in written documentation on NTOs activities.

also be more susceptible to lobbying efforts from different stakeholders who would want different outcomes. The goal-alignment benefits of an outcome-based contract would favor a performance-based budgeting-principle. Under such an arrangement, both the stakeholders and the NTO depend on the same outcome, e.g., increased tourism influx. The choice of an outcome-based type of contract is also supported by transaction cost theory, since outcome-based contracts would reduce monitoring and controlling cost, bargaining cost, and maladaptation cost.

However, several factors particularly important in the NTO context could reduce the attractiveness of outcome based-contracts, namely stakeholders' accessibility to information systems, high agent and low stakeholder risk perception, the relatively high cost of risk-transfer, low outcome measurability, and the long-term nature of relationships, etc. The latter may also partially explain the strong presence of behavior-based type of principles in the existing NTO-stakeholder relationships, as shown in the empirical part of the thesis in Chapter 5, Table 5.1.

When viewing the problem from the perspective of agency theory, and taking the above considerations into account in the NTO context, theory implications of what controlling device to use, e.g., behavior-based budgeting and other monitoring structures as opposed to outcome-based contracts, appear to be somewhat inconclusive.

Agency theory in general assumes the principal's perspective, and thus the principals' legitimate right to achieve its ambitions through the behavior and achievements of the agent. It also assumes rational principals with common clear, undisputed, and legitimate goals, and that corresponding clear goals and undisputed compensations can be specified for the agent. In the NTO context, however, one may have a ruling coalition of stakeholders i.e., government and/or industry that are not exactly sure what they want the organization to do (ref. Figure 3.4 in Chapter 3). In addition, some important stakeholders e.g., *society* and *the market* (ref. Figure 3.3 in Chapter 3) may not have the type of legitimate influence on the organization as the principal is assumed to have in agency theory.

Contract forms or principles taking only the interests of principals with legitimate powers (i.e., funding/controlling principals) into account are probably not sufficient to safeguard the interests of all the important stakeholders in the NTO context. For instance, it is probably possible to construct control devices that favor the principals with legitimate powers, without taking other important concerns such as *market focus* and *long-term planning and operation* into account.

A second problem with agency theory is that, as a theory of performance, it attributes variations in outcome or performance solely to variations in the agent's effort. Less than optimal output is solely attributed to "shirking" by the agent, i.e., lack of appropriate effort by the agent (Nilakant and Rao 1994). We have pointed out that the NTO faces some factors more or less beyond its control that may influence the outcome in terms of

**Table 2.4**  
**Conclusions from application of agency theory & transaction cost theory**

<b>Theory</b>	<b>Consideration</b>	<b>Present in the NTO context</b>	<b>Attractive to use behavior-based control</b>	<b>Attractive to use outcome-based control</b>	<b>Recommendation about governing principle to use</b>	<b>Comments/ references to theory area</b>
Agency theory	Unobservable behavior	YES	NO	YES	Outcome-based	Moral hazard, adverse selection
	Accessibility to information systems (monitoring structures)	YES	YES	NO	Behavior-based	Behavior-based budgeting, purchasable information/control
	High cost of risk transfer to agent	YES	YES	NO	Behavior-based	Risk premium, reduced M.O. and innovative kinds of behavior
	Outcome uncertainty	YES	YES	NO	Behavior-based	Many uncontrollable factors, difficult to preplan long-term activities
	Resistance to take on high risk on the part of the agent	YES	YES	NO	Behavior-based	Outcome uncertainty, cause-effect relation ambiguity
	Risk neutral stakeholders	YES	YES	NO	Behavior-based	Risk dispersed, government funded, non-profit organization
	Goal conflict between stakeholders and agent	Depends on both the NTO and its principals	YES and NO	YES and NO	Both types of principles	Professionalism, non-monetary rewards, exaggerated work-aversion assumption
	Goals and means conflict among stakeholders	Likely conflict	YES and NO	YES and NO	Both types of principles	Hard to agree on performance measures, but also on appropriate behaviors
	Task programmability	Both programmable tasks and non-programmable tasks	YES	NO	Both types of principles	Traditional tasks are programmable, innovative and venture type of efforts are not
	Outcome measurability	NO (Yes, indirectly)	YES (and NO)	NO (and YES)	Both types of principles (hybrid)	Hard outcomes can be easily measured, but not soft, cooperative, or long-term outcomes
	Long-lasting relationships	YES	YES	NO	Behavior-based	Predominately long-term relationships
Transaction cost	High monitoring /transaction cost for both principal and agent	YES	NO	YES	Outcome-based	Negotiation, monitoring, and maladaptation cost

market performance. (We will also revert to the issue of shirking by the agent in the next section.)

For our purposes, agent-principal theory/transaction cost theory is not sufficiently developed in terms of dealing with cases when:

- a) there are many principals with potentially conflicting goals

- b) (some) principals and the agent are not necessarily profit-maximizing entities, which often is a common assumption in agency theory
- c) it may not be clear to the agent whom the ruling coalition of stakeholders is; that is, who the principals/stakeholders/clients really are and whom to report to
- d) the demands from stakeholders are conflicting, and thus the goals of the agent (NTO) are made ambiguous
- e) cause-and-effect relationships are unclear or subject to discussion
- f) feasible (direct) performance-measures are difficult to attain, costly and/or subject of discussion
- g) market competition exposure of the agent is weak to non-existent as a control device
- h) financial bonuses or other types of rewards for good performance/punishment for the agent cannot easily be paid out or invoked like in a commercial situation
- i) there are no alternative agents, i.e., only one NTO in a given country that has a virtual monopoly, thus the agent cannot easily be dismissed

Although important considerations can be derived from application of agency theory, it is not in isolation a body of theory sufficient to comprehensively address all the issues we are interested in. A somewhat more applicable body of theory can be found in *public choice theory*, which is to be discussed next.

## 2.3 Public choice theory

Public choice theory is strictly speaking a “subspecies” of agency theory, which focuses on political institutions in particular. However, for the sake of this thesis we have chosen to discuss Public choice theory apart from traditional agency theory. Public choice theory adds an important non-commercial and societal perspective when considering the NTO as a public agency (which it often is) created to also serve the interests of the public rather than only the interests of profit-maximizing owners or any other sponsoring commercial principals. This is opposed to traditional agency theory’s somewhat implicit assumption of a commercial principal and agent. Public choice theory is defined as “the economic study of non-market decision-making”, or simply the application of economics to political science, and also as the economic analysis of political institutions (Mueller, 1989).

### 2.3.1 NTO as a public institution

NTOs are typically non-profit and (semi-) political institutions, at least partially funded, controlled by, and responsible toward the government. The usual government connection and public institution character are revealed through the commonly used names of these organizations. Along with the nation’s name, “Tourism” or “Tourist” is followed by “Board”, “Council”, and “Committee”, “Commission” etc. The control problem posed by such political institutions, *where market competition does not constitute an additional organizational control*, is that the agent can make more effort than necessary, which costs resources, or does other tasks than desired from a societal viewpoint. Effectiveness and equity are then reduced, and agents can shirk on resources such that inefficiency emerges



and hence effectiveness and [overall stakeholder] equity are also reduced (Johnsen, 2000).

**Table 2.5**  
**Public choice theory's relevance for independent and dependent variables**

<i>Independent variables' relevance for study</i>		<b>Ref-erence to text</b>	<b>Dependent Variables' relevance for study</b>		<b>Ref-erence to text</b>
<i>Bud-geting prin-ciple</i>	1) Due to information asymmetry the NTO can engage in budget-maximizing behavior. Both the NTO-management, politicians and some industry beneficiaries can benefit from a larger budget than socially desirable.	2.3.2 & 2.2.4	Market Ori-entaion	With no performance measurement tied to market results, the NTO will have weak incentives to focus on the market. There are probably stronger incentives for a budget-maximizing focus rather than a market performance-focus.	2.3.5
<i>Fund-ing source</i>	1) Under government operation, the residual control and rights are separated. Then NTO stakeholders have no financial residual rights, thus this additional control device is not in effect. Shirking and diversion of resources can occur. 2) Costs of the NTOs' operation are spread out among many taxpayers, while relatively small groups benefit from higher NTO budgets. The expected gains from forming pressure groups are greater for the gainers than for the losers, and these groups can put politicians under pressure to increase budgets.	2.3.3  2.3.4	Long-Term Pers-pective	Privatization of the NTO, or commercialization through a Limited corporation, might reduce the budget-maximizing problem and inefficiency problems linked to the bureaucracy. On the other hand the NTO might then be enticed or forced to focus on short-term demands from profit-seeking short-term oriented commercial shareholders.	2.3.3
<i>Owner-ship/ org. control</i>	Most NTOs are public agencies/entities. Market competition does therefore not constitute additional organizational control. This creates both an efficiency and effectiveness control-problem.	2.3.1	Oper-ational Free-dom	Under public operation as a government bureau/agency the NTO has incentives to lobby the government in the budget-negotiation process in order to maximize budgets. This takes focus away from marketing activities.	2.3.5

In agency theory organizational hierarchical control is dealt with through two issues simultaneously. The first is the issue of effectiveness, which is to let the agency work on the tasks it is supposed to do (Johnsen, 2000). In the NTO context this is to allow the NTO to turn its attention toward working with the market, and at the same time to give the agent some degree of operational freedom and decision autonomy to do so on a professionally sound basis. The second issue is to ensure that the agency is doing the tasks as efficiently as possible (Johnsen, 2000). In practice, this means to assure that the organization has an incentive to perform only the activities required to solve its marketing tasks, and de-emphasize efforts on non-marketing tasks.

### 2.3.2 Budget-maximizing behavior

In public choice theory the terms *bureau* and *sponsor* are often used instead of *agent* and *principal* respectively. Niskanen (1971) proposed the hypothesis that bureaucrats or employees in political institutions were budget-maximizers, and Migué and Bélanger (1974) amended this to the assertion that bureaucrats were maximizers of *discretionary* budgets. Due to the bureaucrats' asymmetric information on production, the bureaucrats (the NTO bureau) could profit from their information advantage relative to the representatives (NTA in our case) and demand a larger budget and a bigger output than what is socially desirable. Niskanen modeled bureaus as expense centers where the budget was negotiated between the bureau and the sponsors. The bureau provides most of its output to clients such as the tourism industry, society and tourists, many of who do not have to pay for the services directly. The clients then may have no incentive to compare the cost of services with the value provided. Furthermore, the bureau may obtain support from the clients if the sponsor were to cut down on the budget. The bureau may also threaten to cut down on the most valued services rather than reducing services of more marginal value during budget negotiations (Johnsen, 2000). Actually, this can put the government sponsors under pressure from *two sides* in the budget negotiating process: One from the NTO itself, often being the sole agent officially designated to perform the international tourism marketing task and in a virtual monopoly situation; another from the tourism industry and other stakeholders, which would benefit from a larger budget without actually having to pay for it directly. Even if the industry contributes parts of the budget, such as in a matching principle, the industry would benefit from increased budgets available for matching purposes because their marketing effort would be subsidized by a matched part from the government. This can swell budgets beyond what is socially desirable.

Not only may the bureaus shirk in the budget negotiations due to asymmetric information, but also the sponsors could shirk through cooperation with the budget-maximizing bureaus. The representatives in the sponsoring committee i.e., NTA or other stakeholders may get increased support from their voters and constituents by an increased or constant bureau output; that is, more than what would be desirable from the society's point of view. We will discuss this in detail later in Section 2.3.4.

### 2.3.3 Lack of a financial residual

Private ownership of a resource entails that the owner has all residual rights, *both residual control* and *residual rights* (Milgrom and Roberts, 1992). Residual control means that one has decision authority over any use of the resource that is not illegal or transferred by contract to other parties. Residual right means that if the government or any contract partners have been compensated, one has the right to keep the profit from the use of the resources. The problem is when the residual control and residual rights are separated. If the decision authority of a resource is transferred to an agent that does not own it, the agent has no incentive to maximize the residual profit (Johnsen, 2000). This is the main reason why bureaus can be inefficient, namely the lack of a financial residual. Agency theory usually employs the term *residual* when organizational control in firms is analyzed. Residual is the difference between the stochastic inflow of resources (income)

to the principal as the result of the agents' activity and the compensation promised to the agents (Farma and Jensen, 1993). Organizational control can be enhanced by letting the agents share some of the residual (profit), which means that the agent will also have a stake in the same outcome as the principals pursue. Political institutions, on the other hand, usually have no financial residual. The budget is to be balanced against the expenses. The residual, the net benefit, is often directed to constituents who do not pay marginal prices.

Bringing this consideration into the NTO context, the NTO may feel tempted to direct its residual resources towards gaining increased support from the government, special interest groups or other powerful stakeholders such as a large airline company or hotel chain. This kind of misallocation of funds can occur instead of NTOs investing the residual resources in additional marketing effort, which NTOs are supposed to do from a socially desirable standpoint. The consequence may be that NTOs will over-prioritize promotion of products or interests of sponsors who have contributed significant funds to NTOs' budget. The NTOs could also spend too many resources on lobbying activities directed at special powerful interest groups in the industry; or spend too many resources on lobbying government sponsors, as shown in Table 2.6 on the next page.

“The presence of slack is similar both in firms and in public institutions, but firms have financial claims as additional organizational control, while political institutions have not. Performance measurement may on this reason be relatively more important in political institutions than in firms, because interest groups [e.g., powerful stakeholders] may compete for the residual claims on the net benefits” (Lapsley and Mitchell, 1996).

The absence of financial residual claims may increase *slack* in political institutions. Slack can be explained as the difference between the minimum costs for providing some amount of service and the amount the agents/bureaus actually use in providing the service. Slack consists of payments to coalition members in excess of what is required to maintain the organization (Cyert and March, 1962/1992). This may be used to compensate stakeholders for policy support, subordinates for compliance, extended quality and new equipment, or as personal consumption or “on the job consumption”. “Slack is only possible where inefficiency exists” (Niskanen, 1971). NTOs may use slack to take on tasks that are not really their responsibility, hire or maintain more staff than necessary, employing consultants in excess of what is required to solve its marketing tasks etc. The NTO may i.e., use consultants when in-house personnel could have done the job sufficiently, spend resources on extensive “business” travel, or participate in fairs or trade shows with only marginal value in solving the supposed tasks of the organization. In addition, slack may be used to finance activities used, symbolically rather than instrumentally, as proof of quantifiable activity and to show visibility, e.g., through distribution of vast amounts of printed promotional material/brochures, holding seminars directed at gaining support from stakeholders etc., and thus to sustain legitimacy and resources.

**Table 2.6**  
Some examples on how NTOs *can* spend excess resources

<b>Condition</b>	<b>NTO-incentives (if unchecked)</b>	<b>What to do with excess resources?</b>	<b>Possible consequences</b>
1A) <i>Non-profit NTO</i> : Market performance is <b>not</b> generating income for the NTO. Unused portions of budgets will be reclaimed, or budgets will be cut accordingly the following period.	Make as little marketing effort as possible and/or as inexpensively as possible to maximize level of residual resources.	Use it to compensate coalition members (powerful stakeholders) for budget support. Overspend resources within the NTO.	Low market effort, <i>overall</i> industry will suffer in competition with other countries. Powerful industry stakeholders may be over-prioritized.
	Do as much “visible” market effort as possible to spend the entire budget (i.e., minimize residual).	Spend excess resources on highly visible (potentially expensive and expense-inefficient) activities to display visibility and achieve justification.	Inefficient market effort, <i>overall</i> industry will suffer in competition with other countries. Powerful industry stakeholders may be over-prioritized and less powerful ignored.
2) <i>Non-profit NTO</i> : Market performance is <b>not</b> generating income for the NTO. Unused portions of budgets can be transferred for use in the future.	Do as little as possible and/or as inexpensively as possible to maximize “savings” for the future.	Save resources for the future regardless of current need.	Low current market effort, <i>overall</i> industry may suffer in competition with other countries.
3) <i>Non-profit NTO</i> : Market performance is generating income for the NTO. Unused portions of budgets can be transferred for use in the future.	Use resources as efficiently and effectively as possible to achieve current <i>and</i> future market performance. (Given that they believe in what they are doing)	Balance resource usage between current and future needs. Curb spending on non-market activities and compensations.	Efficient market effort, <i>overall</i> industry will benefit in competition with other countries both short-term and long-term.
4) <i>Commercial NTO</i> : Market performance is generating income for the NTO. Unused portions of budgets are either paid to stockholders as compensation or transferred for use in the future.	Use resources as efficiently and effectively as possible to achieve current and future market performance.	Pay dividends to stakeholders, or possibly reinvest resources for use in the future.	Efficient market effort. In some cases the stockholders’ interests may be over-prioritized on the expense of overall stakeholders’ interest. NTOs’ Long-Term Perspective depends on stockholders and their representatives’ willingness to reinvest profits in the NTO.
	Use resources to maximize short-term gain directly from market performance or to try to maximize short-term stock price.	Pay dividends to stakeholders. Compensate NTO management for (short-term) performance	Short-term activities may be over-prioritized on the expense of a long-term perspective. Shareholders may pressure NTO to maximize short-term gain. (Ref. Section 2.5.5 later.)

**Note:** These are only a few examples on NTOs’ potential distribution of excess resources. Other conditions and combinations are conceivable and may occur.

One possible solution to the problem, associated with lack of financial residual claims as an organizational control-mechanism in the NTO context, is to privatize the NTO and its services. Stakeholders could do so by organizing the NTO as a commercial organization/limited corporation with shareholders. The NTO could then be held more accountable for its actions by its shareholders. The shareholders would then have such financial claims on the residual, which may reduce the potential for shirking in NTOs. A problem with this solution is that the stakeholders may force the NTOs to resort to over-focus on short-term activities and/or activities benefiting the shareholders disproportionately more than the overall industry or any important societal concerns. We will revert to this issue later in Section 2.5.5.

### 2.3.4 Inefficiency of bureaucracy<sup>18</sup>

Patrick Gunning (1998) explained why budget maximizing behavior is likely to occur. We have used some of his argumentation to explain why NTO's budgets might get higher than socially desirable, and thus how NTOs can be inefficient from a societal viewpoint. According to Gunning, Niskanen's model of demand and supply is what economists call a bilateral monopoly. The bureau [NTO] is said to be a monopolist seller of government services. The combination of the executive and legislature, as expressed through the budgeting process, is said to be a monopolist buyer. Gunning's model is widely used in public choice theory, and it helps express the general pressure to maximize the budget, as discussed below:

Gunning considered many reasons why one would not expect bureau budgets to be optimal from the consumers' point of view. For instance, Gunning pointed out that there are several reasons to believe that the budgets demanded by the politicians will be *higher* than the one that is optimal from the consumers' standpoints. First, incumbent politicians ordinarily favor higher budgets because the higher budgets can be partly used to help them or their parties in their election campaigns. Second, because national taxes are used to supply local public goods [e.g., demand for local tourism products, and employment and local infrastructure stemming from increased local tourism traffic etc.], the benefits of large budgets that are used to supply such goods, are concentrated in relatively small groups, while the costs are spread about among all of the nation's taxpayers. Other things being equal, the expected gains from forming pressure groups [e.g., tourism industry lobbyists and trade organizations] are greater for the gainers than for the losers. As a result there is asymmetric pressure on politicians to favor a higher than optimal budget. Third, members of the collective can be easily fooled about the burden they must bear in financing bureaus. Fourth, there is a bias among voters who supply resources [both to the NTO itself such as: consultants, marketing firms, transportation etc., and suppliers to the tourism industry such as: labor-force, support services, and other supplies]. Those who supply resources to bureaus [and to the tourism industry] are more likely to know how they will gain from a higher bureau budget than those who supply resources to private firms are likely to know how they lose from higher taxes.

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<sup>18</sup> Adapted from Patrick Gunning's book: "Understanding Democracy - An Introduction to Public Choice".

According to Niskanen, the *bureau management* also wants a budget that is as high as it can get. Given this desire, the question is: How high a budget can the management persuade the legislature to give it?

To answer this question Gunning points to Niskanen, who focused on *information asymmetry* between politicians and bureaucrats. There are two types of relevant information in a bargaining situation: information about costs of supply and information about demand. Consider a situation that is somewhat like the relationship between the bureau management and politicians in the budget negotiation. The bureau management who wants to maximize its budget does not want the politicians to know its true costs; and the politicians do not want the bureau management to know their true demands. But the bureau management has an advantage. Consider first the information about a bureau's costs. The bureau management and other bureaucrats know better than anyone whether a particular style of desk, vehicle, office location, working environment, employee, foreign office etc. is worth buying in relation to the alternatives. Politicians are at a distinct disadvantage. Their ability to find out whether a bureau is wasting money is limited. Even the "experts" who advise the politicians seldom know as much about the technology and costs of resources as the bureau chief and other bureaucrats.

According to Gunning, Niskanen also recognized the propensity for the heads of bureaus and other bureaucrats to be *secretive*. These people deliberately attempt to increase the information asymmetry beyond what it would otherwise be in order to make monitoring more difficult. Secrecy has long been recognized as a characteristic of bureaucracy.

The next issue is information about demand. A bureau management can easily learn about the politicians' demands for bureau services since the legislature's meetings and the chief executive's policies are typically open to the public. The bureau management has access to the newspapers, television, etc. In a typical constitutional democracy, the politicians cannot keep their demands a secret.

Considering these factors, there appears to be information asymmetry. The bureau management has information about politicians' demands but the politicians lack information about the bureau's costs. Suppose that the bureau management is able to exploit its position to the fullest because of information asymmetry. This can happen when there is so much information asymmetry between politicians and bureaucrats that the bureau management can persuade politicians to approve the highest possible budget. Moreover, because the method of financing conceals the costs of the budget expansion, consumers would not realize their losses.

One can readily imagine what would happen if all bureaus could succeed in this way. Bureau managements, competing for status, prestige, promotions, or whatever would expand their bureaus to the max. Voters and taxpayers would probably be worse off than if the bureaus did not exist. And massive amounts of resources would be diverted from the private sector into a bloated public sector. There would be plenty of government services, of course, but this would not be good from the standpoint of consumers and society as a whole.

Applied in the NTO context one can assume that a similar pattern could be present for NTOs as well. The NTA (department dealing with tourism) could benefit from a higher NTO budget because it could bring prestige and power, as well as increase chances that supporting politicians would be re-elected, and department bureaucrats keep their jobs and secure their carriers. This is especially the case for representatives from regions where the tourism industry has great local importance.

Furthermore, the NTO-management would want as high a budget as possible, because this would give the NTO more prestige and excess resources. We have pointed out earlier that it is very difficult for stakeholders to estimate what the cost of the NTO services should be, because of information asymmetry. The NTO management could then be able to persuade the politicians in the NTA to approve the highest possible budget. In a worst case a manager, unrestricted by morality, could spend a disproportionate part of these resources pursuing pet projects, engaging in personal on-the-job consumption, allowing the NTO to grow in size beyond what is desirable, and on lobbying politicians for even more resources.

### **2.3.5 Resistance against performance measurement**

Apart from the fact that performance-measurement will deter the possibilities for budget maximization, there is another reason why the NTO and some principal stakeholders may want to avoid performance-measurement. According to Markus and Pfeffer (1983) and Argyris (1990), it is likely that actively involved stakeholders in political organizations will resist implementation and use of performance measurement that may cause embarrassment, unless such systems are used for external legitimization only, or there is so much ambiguity that embarrassing information from the performance measurement does not affect the ruling coalition (Baier, March and Sætren, 1986). In fact, this potential embarrassment can cause implementation and use of performance measurement to be resisted both by the political institution/bureau itself and the sponsor e.g., the government through the NTA. It may reveal inefficiency, which obviously can be embarrassing for the institution itself, but also for the public sponsor who is supposed to be at least partially responsible towards its constituents for the agency's (mis)behavior. Thus, when performance-based principles of organizational control are evaluated by stakeholders, who may be subject to embarrassment from such performance-measurement, one could speculate that these principles are evaluated less positive than from an objective standpoint.

Due to asymmetric use of information, politicians may want to monitor a bureau in order to avoid strategic behavior. Even imperfect monitoring [e.g., imperfect performance measures such as tourism market performance] may reduce the bureau's ability to deceive the legislature (Bendor, Taylor and Gaalen, 1985). However, monitoring of the agent/bureau could be costly, as explained earlier. Another means in organizational control is to let constituency groups, such as interest groups, monitor the agencies. The interest groups can then communicate the results directly to the politicians rather than through a formal organizational control system (Banks and Weingast, 1992). This can be in the form of access to board representation for interest groups or formalized reporting procedures accessible to such groups. For NTOs this could be e.g., periodic mandatory presentation of the bureau's activities and achievements. (This seems to be a quite

common form of indirect control in the NTO context, as reported by our respondents in the focus groups). The interest groups then bear some of the monitoring cost but they also have more information and industry expertise necessary to evaluate the information than the politicians do. Furthermore, they receive benefits from NTOs' output directly. This means that performance measurement may have substitutes and compliments in interest group monitoring behavior and in the news media and trade press.

### 2.3.6 Conclusions to be drawn from public choice theory

Public choice is very useful in the NTO context because it adds an important non-commercial and societal perspective, which traditional agency theory usually lacks. Concepts such as *budget maximizing behavior*, lack of shareholder financial *residual claims* and public agency *resource shirking*, are important considerations in a situation where market competition is unavailable as additional organizational control. It also applies when the agent/bureau (NTO) has some non-sponsoring/funding societal stakeholders, such as tax-payers, some tourism businesses and other beneficiaries.

In conclusion, public choice theory suggests that political institutions are more susceptible to slack than profit-maximizing firms are because both the agent and the principals may have an incentive to shirk due to absence of financial residual claims. Furthermore, budget maximizing-behavior and selective attention to special interest groups or other powerful stakeholders is more likely. This makes performance measurement relatively more important in political institutions than in firms. However, due to the potential embarrassment as a result of unfavorable information from performance-measurement, one can expect resistance to the use of such measurement both from sponsors and the NTO itself. This could explain in part why performance measurement is rarely used as a disciplinary mechanism to control NTOs. Our empirical data (see Table 5.1 in Chapter 5) show that performance-measurement through performance-based budgeting principles is uncommon for NTOs worldwide. Furthermore, stakeholders such as the government, private sponsors and industry clients, may perceive that they can control the organization and reveal the agent's behavior through interest group and media monitoring, which reduces the perceived stakeholder need for direct performance-measurement.

The theory of public choice tries to explain inefficiency and growth in the public sector by assuming that bureaucrats would want a larger discretionary budget than they would need, and that they to a large extent are able to do so (Blais and Dion, 1991). It is not unreasonable to believe that any public or private agency would like to have slack in the organization, and that this can be achieved through the budget negotiations. There are, however, some weaknesses in Niskanen's theory and similar explanations on public overspending: First, the effect of any disciplinary mechanisms in the public sector is overlooked, while the trust in disciplinary mechanisms in the private sector is very strong (Boyne, 1998: 698). For instance, according to classical bureaucracy theory, the promotion opportunities discipline bureaucrats in a way that it would make it attractive to assure cost effective operation rather than to pursue short-term selfish interests (Weber, 2000). Bureaus can also be under pressure from interest groups that can form a disciplinary mechanism. Second, considering the private sector, the problem with Niskanen's theory is that he implicitly assumes that profit-motivated owners and



competition between suppliers will deter the possibilities for the employees to pursue self-interest contrary to the owners' interests in cost-efficiency. This may not be an entirely safe assumption. A third weakness is the assumption that politicians have weaker incentives than private owners to assure that public services are brought about to the public (Johansen, 2001).

**Table 2.7**  
**Conclusions from application of public choice theory**

<b>Theory</b>	<b>Consideration</b>	<b>Present in the NTO context</b>	<b>Attractive to use behavior-based control</b>	<b>Attractive to use outcome-based control</b>	<b>Recommendation about governing principle to use</b>	<b>Comments/ references to theory area</b>
Public choice theory	Lack of market competition, non-commercial operation, no profit-maximizing owners	YES	NO	YES	Outcome-based	No financial residual claim =lack of efficiency -incentive
	Agent incentive for budget maximization	YES	NO	YES	Outcome-based	Bureau's asymmetric information advantage
	Stakeholder joint incentive for budget-maximization	Moderately YES	NO	YES	Outcome-based	Non-paying clients, public funds, pressure on political representatives from constituents and interest groups.
	Favoring of special interest/lobbying efforts	Likely	NO	YES	Outcome-based	No budget residual, slack could be distributed towards powerful stakeholders to win support
	Resistance to performance measurement	YES	YES	NO (risk premium must be paid)	Behavior-based	Potential embarrassment for both bureau and legislature/sponsors
	Media and interest-group monitoring	YES	YES	NO	Behavior-based	Media and interest groups will reveal behavior and bear some monitoring costs

Overall, this body of theory supports the notion that market-related performance-measurement may be necessary to avoid inefficiency and budget-maximization and to create incentives for a market focus of the organization. This is probably particularly important in countries where the NTO is funded and responsible toward the government alone and the NTO is a purely government –owned/controlled and government-funded bureau.

However, there are some potential weaknesses in public choice theory which one should keep in mind when this body of theory is applied. These weaknesses are due to Niskanen's assumptions about the lack of disciplinary mechanisms in the public sector and probable over-confidence of the corresponding mechanisms in the private sector. Moreover, while very useful for our study, public choice theory as well has a few shortfalls in light of covering all issues of this study comprehensively. The rather complex NTO context does often have some elements of a commercial market, and may

very well have important commercial principals/stakeholders who depend on the NTOs' market-performance. Nor does public choice theory address the issues of a) the effect of public vs. private ownership/control, and b) the issue of funding source - sufficiently for our purposes. So public choice theory fits the NTO context quite well, but is far from a comprehensive theory for all facets in this study.

## 2.4 Public economy theory

Public economy theory or social economics theory deal among other aspects, with the issues of market failure, which may call for the government to intervene. In this section we will also discuss: the consequences of public versus private ownership of the NTO, the impact of performance-based contracts on state owned firms' performance, and the need for regulations to avoid monopolistic behavior by the NTO. Finally, we have included a discussion about the problem of common/collective goods and how this relates to the question of public versus private funding.

### 2.4.1 Ownership of the NTO – Does it matter?

First we will address the issue of ownership, or more specific - governance control of the organization. In this section we will look at what expectations one can find from economic theory about cost-efficiency and other societal concerns in terms of public and private operation of an organization like an NTO.

From empirical research on private versus public ownership there is strong empirical support that private owners operate companies or organizations in competitive environments more efficiently than the government. In several countries there have been made comparative studies of public versus private operation (e.g., Borchering, 1992). It seems to be a consistent finding in the results from those studies that in areas where there are private alternatives parallel to public operation, the unit costs are higher under public operation. However, the cost-differences are clearly lower in areas where public entities are faced with active market competition. It therefore seems to be empirical evidence that the competitive situation has a major importance for the cost discipline both in public and private operation (Hagen, 1992).

The argument that *ownership* does matter, is that in the case of for-profit commercial operation in e.g., a limited corporation, the production will be more effective. This is because the profit from the organization's operation will be granted individual owners. Because shares can be sold, the owners would want to maximize current and future income, by assuring cost-efficient operation. In the NTO context this consideration is most applicable when the NTO is organized as a commercial company, which is unusual, yet conceivable. The owners of the NTO would favor cost-efficient operation because it could pay dividends or profit from sales of shares. Furthermore, the owners are likely to be at least partially made up of people representing firms that have a commercial interest in the tourism industry. Private owners would benefit from a cost-efficient NTO, which at the same time is effective in generating tourism traffic, since these firms would benefit from more incoming tourist customers and thus higher sales.

**Table 2.8**  
**Public economy theory's relevance for the independent**  
**and dependent variables**

<i>Independent variables' relevance for study</i>	Ref-erence to text	Dependent Variables' relevance for study	Ref-erence to text
<p><i>Bud- geting prin- ciple</i></p> <p>1) Performance contracts should include rewards and penalties that could motivate staff to exert more effort, particularly in entities under public ownership. Budget increases should be linked to better performance.</p> <p>2) Soft performance measures should be avoided, and relative performance measures in the form of benchmarking can help reveal the true cost of NTOs' operation.</p> <p>3) A performance-based budgeting system will motivate the NTO to tailor its production to the organization's true cost.</p> <p>4) Behavior-based budgeting can in some instances motivate the NTO to under-produce on quantity and quality.</p> <p>5) Performance-based budgeting gives incentives for higher production, stronger incentives for undesirable selection, as well as it does not provide incentives to reduce the production to meet the balancing (non-profit) restriction.</p> <p>6) A "take-care-responsibility" may be needed, and a combination of per-unit and fixed-sum principles can thus give better incentives for optimal production. A combined alternative will distribute risk between the producer NTO and the sponsor, which is beneficial as well.</p>	<p>2.4.2</p> <p>2.4.2</p> <p>2.4.3</p> <p>2.4.4</p> <p>2.4.5.1</p> <p>2.4.5.2</p> <p>2.4.5.3</p> <p>2.4.5.4</p> <p>2.4.5.5</p>	<p>Market Ori- en- taion</p> <p>1) Private operation would probably entice the NTO to be more marked-oriented and effective, since the owners from the industry are more dependent on market performance than the government, and would put stronger pressure on NTO to show market results than the government would do.</p> <p>2) Without a "take-care-responsibility", the NTO could resort to focus on existing markets only and ignore important markets that require more efforts.</p>	<p>2.4.1</p> <p>2.4.5</p>
<p><i>Fund- ing source</i></p> <p>1) Government as a funding source can provide a stable source of income over time, and thus beneficial in terms of long-term planning, unless budget cuts are done arbitrarily.</p> <p>2) Private funding might be more unstable over time, and depends on sponsors own budget situation and willingness and ability to commit to funding of NTOs' long-term activities.</p> <p>3) The <i>common goods</i>-problem makes it difficult to obtain funds from the private sector for generic marketing and NTO activities. Performance-based budgeting may increase the private sector's willingness to sponsor the NTO, since it transfers some of the risk of the outcome from the sponsors to the NTO.</p>	<p>2.4.1</p> <p>2.4.6</p>	<p>Long- Term Pers- pective</p> <p>1) Large private firms with large investors might pressure the NTO to under-provide quality and ignore Long-Term Perspective or otherwise shortchange the NTOs' other stakeholders because of their likely single-minded focus on short-term profits.</p> <p>2) Pure-per unit budgeting can give undesirable incentives to focus on short-term gains.</p>	<p>2.4.1</p> <p>2.4.5.2</p>

**Table 2.8 (continued)**

Independent Variables Relevance for study		Referen ce to text	Dependent Variables Relevance for study		Referen ce to text
<i>Owner -ship/ org. control</i>	1) Some researchers argue that the production would be more efficient under a commercial limited corporation operation than non-profit public operation.	2.4.1	Operat- ional Free- dom	1) Performance-based budgeting should allow the stockholders to give the NTO more autonomy, because it reduces the need to monitor and control the activities of the NTO.	2.3.5
	Politicians would not have as strong incentives as private owners to assure cost-efficient operation.				
	2) Others argue that concentrated private ownership/control can be used to redistribute wealth (or benefits), or force the NTO to focus on special private interests, on the expense of weaker stakeholders (e.g., society, smaller industry actors etc.).	2.4.1			
	3) Again some scholars argue that the inefficiency often associated with public operation does not serve the public the best, whereas private operation would improve efficiency and thus benefit all stakeholders.				
	4) World Bank study found that the greater the participation of private agents in ownership and management, the better performance of the organization.	2.4.2			
5) A non-profit NTO asked by its owner to balance budgets will have other production incentives than a profit-maximizing owner (Limited corporation).	2.4.5				

Section 2.1 earlier in this chapter provides some theoretical and empirical evidence that market-oriented firms are more successful and profitable than others are (ref. Sandvik, 1998). Private ownership could entice the NTO to become more market-oriented, because effectiveness through market focus could help increase incoming traffic, which would be in the private owners' interest. One could then argue that a commercial NTO organization would have a stronger market-orientation incentive than a non-commercial NTO organization. For instance, this can be due to pressure from profit-oriented owners motivated by profit from either higher sales in own business or by income from NTO dividends or share sales.

We have discussed earlier in Section 2.1.2 that a Long-Term Perspective is desirable. A commercial NTO organization could, however, have speculative owners that would want to boost short-term gains from current NTO dividend payments or sales of shares on the expense of longer-term operation (see also Section 2.5.5 later). A privately owned *non-commercial* NTO would probably provide somewhat weaker incentives for this kind of undesirable owner behavior, where maximization of short-term profits from shares sales or dividends is unlikely, while the cost-efficiency incentive would probably be stronger in a commercial type of NTO organization.

With public ownership, however, the benefits from cost-efficient operation would not be granted individual owners in the same manner as in the private-ownership case (Johansen, 2001). Politicians and the bureaucrats in the NTA would not have as strong incentives as private owners to make sure that the operation is cost-efficient, or purpose-effective for that matter.

There is little doubt that the leading scholars in this field, particularly in the US, have emphasized the arguments for privatization the heaviest (Johansen, 2001). There are, however, some counter-arguments to this notion. This body of research seldom focuses on the societal interests public ownership is supposed to safeguard (Johansen, 2001). A plausible one is that an important purpose of public operation is that one should consider other concerns beyond maximizing profits. We have discussed earlier the danger of the NTO becoming overly industry-oriented or in other ways subject to undesirable pressure to over-prioritize powerful owner-stakeholder groups, which may not be socially desirable. For instance, the needs and interests of small businesses in rural areas or small sub-sectors of the industry may be overlooked. This could happen, if the private NTO-owner-coalition was dominated by, for instance, several large city hotel chains or large international airlines.

Shleifer and Vishny (1997) argue that large investors [e.g., large private sponsors/owners of the NTO] and thereby concentrated ownership will have some obvious benefits, at least theoretically. The large investors have both the interest in getting their money back and value for their investment, and the consensus and power to demand it. Again, the problem with concentrated private ownership is that the large investors/sponsors represent their own interests, who may not coincide with the interest of other smaller sponsors, NTO employees or management, the government, society, or other stakeholders. In the process of using his control right to maximize his own welfare, the large investor/sponsor can redistribute wealth –in both efficient an inefficient ways- from others.

Thus in some situations, according to Shleifer and Vishny, concentrated private ownership e.g., by one or a few firms may not be optimal. This is because non-shareholder constituents such as: managers, employees, small stakeholders, and consumers are left with too few *rents* (or net benefits), and thus too little incentive to make relation-specific investments. Relation specific investments can be e.g., financing of a long-term co-project between a small and large stakeholder, or a long-term destination brand-building campaign by the NTO. For instance, large private firms with large investors might pressure the NTO to under-provide quality and ignore a long-term perspective or otherwise short-change the NTOs' other stakeholders because of their single-minded focus on short-term profits. This logic has been used to explain why health care, child care, and even retailing are sometimes provided by cooperatives, even consumer cooperatives. (It is for example conceivable that one could organize the NTO as a cooperative or some kind of other non-profit organization). A similar argument has been used to justify government ownership of firms or organizations (Shleifer and Vishny, 1997). Where monopoly power, externalities, societal or other distributional issues raise concerns, privately owned profit-maximizing firms, which a commercial version of an NTO *could* be, may fail to address these concerns. A publicly spirited

politician or NTA bureaucrat can then improve efficiency by controlling the decisions of such firms. Social welfare arguments underlie the traditional ownership of railroads, electricity, prisons, schools, health care, and many other activities (Laffont and Triole, 1993; Sappington and Stiglitz 1987). In addition there is the issue of the common/collective good problem, which creates a free-riding incentive, and consequentially, problems with under-funding. This may explain why we encounter so many government-owned NTOs (see Table 5.1 later). With a few exceptions of activities where the argument for state ownership is feasible, such as police and prisons (Hart, Shleifer and Vishny, 1997) the reality of government ownership is broadly inconsistent with this efficiency argument. First, state firms do not appear to serve the public interest better than private firms do. For example, in many countries state enterprises are much worse polluters than private firms are. Indeed the pollution problems are worst in the former communist countries that were dominated by state firms (Grossman and Krueger, 1993). Second, contrary to theory, state firms are typically extremely inefficient, and their losses result in huge drains on their countries' treasuries. Some government owned NTOs possess budgets in excess of US \$100 million annually, much of this financed by taxpayers' contributions. One can only imagine what the potential inefficiency-losses of such large government-owned NTOs can do to taxpayer's money in a given country. As Shleifer and Vishny put it: "In their frequent disregard of social objectives, as well as their extreme inefficiency, the behavior of state firms (or organizations) is inconsistent with the efficiency justification of their existence" (Shleifer and Vishny, 1997).

The recognition of enormous inefficiency of state firms, and the pressures on public budgets have created a common response around the world in the last few years, namely privatization (Shleifer and Vishny, 1997). In the case of NTOs we can see a corresponding tendency of increased government pressure for private sector NTO funding and control (World Tourism Organization, 1996). In most cases privatization replaces political control with private control by outside investors. At the same time, privatization in most countries creates concentrated private cash flow ownership to go along with control. The result of this switch to these relatively more efficient ownership structures is typically a significant improvement in performance of privatized firms (Megginson *et al*, 1994; Lopez -de-Sialnes 1994).

In terms of Long-Term Perspective as it relates to *funding source*, one could argue both ways. A change in the national budget situation or a change in political power, which in turn may change priorities, could make the governments cut NTOs' budget arbitrarily from one year to another. "Arbitrarily" is defined here as regardless of NTOs' performance. As a consequence, the NTOs may have to cancel long-term programs such as destination image building or work with new markets. Such sponsor behavior would make the long-term budget situation uncertain and impede long-term planning and operation for NTOs. Obviously, for government ownership to be beneficial for the organization, such behavior must be avoided. On the other hand, private sponsors may also decide to pull or reduce their sponsorship arbitrarily due to political or tactical reasons or simply the businesses' own budget situation. Such behavior could also reduce the predictability of NTOs' budget situation and reduce the ability for long-term planning and operation. From the empiric results of this study presented later in Chapter 5 it appears that our practitioner respondents seem to believe that government funding

provides a more stable source than private funding. As we will point out later in the recommendations chapter, performance-based budgeting principles will probably reduce the impact of funding source, since it limits the sponsors' ability to cut budgets arbitrarily. This is of course given that sponsors are fully committed to the liabilities vested in the principle.

In sum there are some strong arguments that NTOs would be more cost-efficient, effective, and more apt to be market-focused under private ownership. On the other hand, some will argue that government NTO ownership could help safeguard societal interests beyond cost efficiency and owner profit maximization, but this has not yet been proven empirically. On the contrary, some evidence suggests that government ownership does not guarantee that societal interests are best served. In terms of desired Long-Term Perspective of NTOs, government funding/and or control could be beneficial for the organizations' long-term operational perspective. However, this notion will only be valid under a steady NTO budget policy and no or few arbitrary budget cuts, which may not be the case in all countries. In countries where budget policies are unstable, governments change often, and frequent budget cuts occur, private funding/and or control may be better for the Long-Term Perspective and operational ability of the NTO.

#### **2.4.2 Performance-based budgeting for the NTO – What makes it work and what doesn't?**

In a World Bank study of state-owned enterprises (SOEs) in developing countries (World Bank, 1995) one found that the greater the participation of private agents in ownership and management, the better performance of the organization, which is in line with Shleifer and Vishny's arguments in the preceding section. The study also found that performance-based contracts had little impact on performance. This is explained by the fact that these contracts did not improve the incentive structures facing government SOE managers. They did not reduce the managers' information advantage; instead the managers were able to use their knowledge of the firm to negotiate multiple soft targets that were easy for them to reach.

The World Bank also pointed out that the performance contracts encountered in the study rarely included rewards and penalties that could motivate staff to exert more effort. Where cash bonuses were offered they had little effect because they were not linked to better performance. Other promised incentives such as greater managerial autonomy, were often not delivered, and penalties, such as firing and demotion, were seldom applied.

For the purpose of this thesis, we have thus not included performance-based principles based on soft measures in our independent variables. Soft measures could be, for instance, indirect measures such as: knowledge of the country in target markets, number of activities initiated, service satisfaction among clients/users etc. Instead we have used hard targets such as increase in number of tourists/receipts (absolute performance) and increase number/receipts of tourists relative to comparable countries (relative performance). (See also Table 5.1 in Chapter 5 for an overview of the principles/independent variables). We have included the relative performance principle

(P2), for another reason as well. This kind of benchmarking principle can act as substitute for market competition, since the NTO will be awarded or punished relative to the performance in terms of tourism traffic of other comparable countries. By comparing a given NTO with its neighboring NTOs on “hard” performance, one can find out what is reasonable to expect from that NTO in terms of resource efficiency and effectiveness. It can help reveal the “true” cost of effective and efficient NTO operation. This can help reduce the NTO’s information advantage over its stakeholders. This may prevent that NTO management is able to negotiate unreasonably high budgets, which often produces socially undesirable resource slack in the organization and resource-inefficiency through shirking or other types of resource misallocation or waste.

The internal organization, operation, and incentive structures of NTOs are somewhat beyond the scope of this thesis. However, it should be clear that performance-based budgets ought to have consequences for how management and employees are rewarded and penalized as well as for the NTO itself as an organization (see also section 2.5.2 for details). Performance-based budgets should be linked to management and employees’ bonuses; a greater budget as a result of good performance should give room for such bonuses. Weak performance over time should be linked penalties, such as firing and demotion. This should be a part of the NTOs’ internal incentive structures in order for performance budgeting to have any effect on the NTOs’ behavior whatsoever.

Most important for our purposes here is the issue of managerial autonomy. Performance-based budgets should in theory give the stakeholders less of a need to monitor NTOs, and should give NTOs more Operational Freedom. (See also section 2.2.3.2, 2.2.3.3 and 2.5.2 for more detailed explanations.

A final problem why performance contracts had little effect pointed out by the World Bank study is that governments demonstrated little commitment to the terms of the contracts, frequently renege on key promises. This increased managers’ incentive to use their information advantage to negotiate soft targets. For performance-based budgeting to have an incentive effect on NTOs, it is crucial that promised budget rewards are awarded as promised. This can be challenging for some governments or other funding stakeholders, because it makes the governments liable to come up with extra budget funds if NTOs achieve increases in tourism traffic. The governments will not know for sure how much they will have to pay out in NTO budgets the following year, which may be problematic in the public budgeting process. The governments will also lose their discretion to cut NTO budgets arbitrarily. The public budgeting problem can be mitigated by linking the performance budgeting process to tax revenue from tourism (Principle 7 and 8, see Table 5.1). The governments’ increased NTO budget liabilities as a result of increases in tourism traffic can be offset by higher hypotecrated tax revenue from the same increases in tourism traffic.

Furthermore, the increased risk for NTOs associated with implementation of performance based-budgets should be compensated by greater Operational Freedom, e.g., in a more “hands off” approach by the governments or other controlling stakeholders. In practice, this means to relax some of the control devices mentioned under monitoring structure # 2, (see Section 2.2.3.2) in order to give NTO managements greater autonomy. This can



make performance budgeting more acceptable to the NTO, and at the same time reduce stakeholder transaction cost associated with monitoring and negotiating with the NTO.

### 2.4.3 Market failure – governing stakeholders' alternatives

A lot of the academic discussion in public economy theory regarding privatization is under the assumption that private operation, probably subject of some kind of regulation, in most cases is more efficient than public operation (Olsen, 1992). Assuming a normative view, and thus assuming a government that is interested in furthering the interests of the public and society, it will under perfect information (no information asymmetry) be so that the three forms of public intervention - public operation, regulation, and taxation - are all equivalent. (Taxation of the organization itself as means of organizational control is a more indirect form of intervention and not relevant for our purposes.) We have discussed earlier (e.g., in Section 2.2.2.2 and 2.4.2) that it probably is some degree of information asymmetry between the NTOs and the NTAs or other principal stakeholders in our case. Along with information asymmetry, we have a situation of market failure. In general, market failure occurs when there is:

- a) *lack of competition*, in a commercial context most often caused by economics of scale or irreversible investments. (In the NTO context there is usually only one NTO in a given country which has been designated to do international tourism marketing on behalf of the country<sup>19</sup>, and NTO has a “monopoly” on official country representation).
- b) *external effects*, such as employment, infrastructure development, and tax revenue
- c) *common goods*, for instance knowledge gained through research and development, or generated county image (brand name).
- d) *information asymmetry* in transactions between private actors

That leaves the government with two realistic alternatives in order to respond to a situation with market failure, as is common in the NTO context: Either public operation of NTO as a government entity or private sector NTO operation subject to regulation. The latter is also known as *contracting out*.

In fact, NTOs have in most cases been licensed a “monopoly” position in the national supplier market for international generic tourism marketing. A government may give so large subsidies to an NTO bureau, or may subject private competitors to such stringent regulations that other organizations or companies find it unprofitable to compete. Thus, the task for the government is somewhat similar to that of regulating the production and pricing of monopolistic businesses in the private sector. As we have discussed earlier, a common problem for the government is that it does not fully know the organization's technology, assets and costs, and that these are better known to the organization than the government. Such information asymmetries make it possible for the organization to

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<sup>19</sup>In theory, it is conceivable to have more than one NTO so that several organizations offering international marketing are able to compete on a contract basis. Competition could then reduce NTOs' information advantage. But economies of scale and other political considerations (e.g. hierarchy of organization, official country representation, one entity only for clients to respond to etc) make this a less likely scenario.

strategically better its own position (Olsen, 1992). Without any kind of regulation, this organization could use its monopoly position to gain unreasonable profit (in the contracting out case) or consume slack on the expense of taxpayers and society (in the public operation case).

If the governments followed a principle of determining the organizations' budget based on the estimated cost of NTOs' operation (e.g., principle # 4 and partially P3 and P5 in Table 5.1) NTOs would have had incentives to exaggerate their cost estimate. When the true cost is hidden for the governments and is kept hidden [by the NTOs], the production will not be adapted to these costs; and the resource usage will normally be inefficient (Olsen, 1992). This means that, if an organization with private information should be motivated to tailor its production efficiently to the true cost, it will have to get some kind of reward, also a *pure profit*. In a commercial NTO context this would be equivalent to increased operational profits; in a non-commercial scenario this could take the form of or slack or bonuses/perks. From the government side there is then a trade-off between motivating for efficient production and letting the organization have some level of profit or slack. This potential profit or slack is a *basic rent*, and thus a reward that is not a compensation for productive effort. When the government values the organization's pure profit less than consumer (society) surplus, the regulation problem becomes to extract this basic rent (at least to some extent) (Olsen, 1992). The optimal regulatory system grants the organization *operational freedom*, and has a design that gives the organization incentives to *tailor the production* [here: marketing effort] *to its true production costs* (Olsen, 1992). The produced quantity [level of marketing effort] will, however, not be first-best effective, and the efficiency loss will be greater the higher the organization's true costs are. Due to the fact that the organization has private information and will use this strategically, it will achieve a certain information rent – and this profit will be greater the lower the costs of the organization. We will discuss this in more detail in Sections 2.4.4 and 2.4.5 next.

#### 2.4.4 Incentive-based budgeting principles and asymmetric information<sup>20</sup>

In this section we will discuss how a governing stakeholder can design incentive-based budgeting-principle for a national producer of international tourism marketing. In a recent research report, Bjorvatn, Kjerstad, Sannarnes, and Sunnevåg (2002) discuss how incentive-based financing systems can be designed for public health services. Much of their discussion on financing systems public health services can be applied directly to our study of financing and control of NTOs, as discussed below.

For simplicity we will assume that the government would operate in the role of a regulator or governing stakeholder and the producer operate as the agent for the government. In a situation where the government has complete information of the producer's operating cost, technology, and opportunities for cost-efficiency, the

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<sup>20</sup> Adapted from Bjorvatn, A., E. Kjerstad, J. G. Sannarnes, and K. Sunnevåg's research report "Incentivbaserte finansieringssystemer for helseforetak", SNF, Bergen, Norway.

government would be able to design a budgeting system that would assure efficient and adequate production of marketing services. However, the government does normally not have such complete information. When the producer has more information than the government, there would be information asymmetry. As discussed earlier, asymmetric information can result in problems associated with moral hazard and adverse selection.

Four conditions related to the design of a budgeting principle will be discussed here:

- Incentives for efficiency in the production and investments
- Optimal quality and quantity
- How to avoid undesirable selection of certain markets
- Optimal allocation of risk between the government and the producer of international tourism marketing

A budgeting principle should give incentives for efficiency in production and in investments. Efficiency in production has at least two aspects: One is that the costs of production of international tourism marketing services are minimized by a budgeting principle that gives correct incentives for cost efficiency. To achieve this, the reward must be compared to the cost of the cost-reducing activities. This means that the gain from a cost-reduction should be fully or partially retained by the producer. In this way the producer will have incentives to cut costs and produce the services in an efficient way. The other aspect is that the budgeting principle gives incentives to choose an optimal combination of input resources such as capital and labor. We will not get into discussion of the latter here.

The objective of efficiency has also a dynamic aspect. A well designed budgeting system should give correct incentives so that considerations of whether to invest in marketing production equipment or capacity (e.g., IT equipment, staff training and competence, establishment of new foreign offices, etc.) and other types of investments are done in a social-economic desirable way. At the same time it should assure that the producer considers a new investment versus better utilization of existing production equipment or capacity.

The marketing services should be produced with optimal quality. Examples of higher quality can be a better, yet more expensive, marketing tool such as a new interactive internet site, or a new foreign office. The quality notion can thus mean both better quality of the input factors and that the producer employs more input factors to produce the service. In principle, the degree of quality should depend on cost-benefit analysis where improved quality is measured against the cost.

However, there is a connection between cost efficiency and quality. If the producer will be awarded full coverage of costs, he will not assume the costs of increased quality. Then there will be a risk that the services provided will be of higher quality than what is socially desirable. On the other hand, if the budgeting principle gives strong incentives for cost reductions without special restrictions on minimum quality, there will be a risk that the producer will not assume higher quality in its production. If the benefits of improved quality are only allocated to the tourism industry, the tourists and/or the

government - and not the producer NTO, the services could end up being produced at inferior quality.

The budgeting principle should not give incentives for undesirable selection of certain markets either. For instance, where one has a budgeting principle where the producer would be paid certain amount unit e.g., per foreign tourist that visits the country (tourist arrivals), regardless of the cost of attracting the tourists, the producer would have incentives to try to attract the least costly tourists. For instance, this could be low-spending one-day visitors from a neighboring country, or only tourists from established traditional markets. On the other hand, if a budgeting principle is employed where the producer obtains full cost coverage of the costs associated with attracting each tourist, there would not be any such selection problems. However, in an NTO context it is quite difficult to calculate or estimate the exact cost of attracting each individual tourist, since some visitors may arrive regardless of any influence from NTOs' production, while other may arrive as a result of NTOs' work, or anything in between. Without a large and complicated survey apparatus for measurement of incoming tourists' purchase decision process, it is hard to identify the first from the latter. Therefore it is difficult to allocate a specified cost to each individual or group of tourists, i.e., per-unit cost-pricing is cumbersome in the NTO context.

#### **2.4.5 How to regulate a producer of international tourism marketing<sup>21</sup>**

In the following we will assume a situation where the government is to design a system to regulate a producer of international tourism marketing. The producer can in many instances have a (virtual) national monopoly for production of official international tourism marketing services. In principle the government is faced with the task of regulating a producer through either a budgeting system, or through the instructions, goals, and objectives the government (as the owner of the producer) sets for the producer. In the following we will discuss whether the budget principle should be based on a behavior-based principle (e.g., estimated cost of marketing plans and activities) or a performance-based principle (e.g., per-unit reward) or a combination of the two types of principles.

##### **2.4.5.1 Behavior-based budgeting**

If the producer has a profit-maximizing goal, such as an NTO organized as a limited corporation (ref. Principle 14 in Table 5.1), it will be important to give the producer the right signals for optimal production of marketing services. A profit-maximizing producer faced with a fixed sum funds transfer principle (ref. Principle 5) would want to produce as little as possible, since extra income from increased production would be zero. In such a scenario the government will have to give the producer additional incentives through other mechanisms. Examples for such incentives could be to introduce a "take-care-of-responsibility", where the producer will be instructed to produce marketing services for certain segments of the tourism industry such as: non-central/rural areas, small businesses, eco-tourism, or to promote sustainable tourism, etc. For instance, the

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<sup>21</sup> Section 2.4.5 is adapted from a recent research report (SNF-report no. 34/02) on financing systems for health services.

producer could be given a “take-care-of-responsibility” in the form of certain goals and objectives that will have to be met (ref. Principle 6 in Table 5.1.) If the producer is faced with a “take-care-of-responsibility”, he could still have incentives to produce as little as possible with as low quality as possible, as long as the “take-care-of-responsibility” is satisfied. A similar conceivable budgeting principle could be based on sale and execution of projects with cost coverage of work performed on the part of the producer (ref. Principle 3, Table 5.1). However, as already mentioned, full cost coverage will give weak incentives for cost efficiency.

Two aspects, that could deter such opportunistic and undesirable behavior, could be that the producer would want to maintain a good reputation, or as in most cases, is truly concerned about helping the overall tourism industry.

An alternative to have a profit-maximizing producer is to give him a task to balance his cost against his income, or achieve zero-profit (ref. Principles 12 and 13). For instance, this could take form of a principle where the producer is allocated a budget negotiated on the basis of his plans of the activities and efforts he wants to carry out (ref. Principle 4). In a situation where the “take-care-of-responsibility” is satisfied, the producer would not have special incentives to prioritize any left-over resources. If so, there could be other motives that will determine how the excess resources are spent, for instance where the management or employees have special interests, where there is benefits from lobbying-effort to win political and financial support, or otherwise act in a way that the services are not produced as efficiently as they could. Alternatively, excess resources could be spent for investments in special equipment, technology, or human resources that would strengthen the producer’s standing in a future coordination with other producers or bureaus, or when the services are produced with a higher quality than optimal. It can also come to a situation where the producer faces a conflict between the “take-care-of-responsibility” and the budget balancing restriction. The “take-care-of-responsibility” is not easily measurable for the government because the producer has more information about quality of the services than the government and the efficiency in the production of those. The balancing restriction is directly measurable through the organization’s financial statement.

It can be difficult to design incentive systems when some of the measurement variables are more observable, measurable, or verifiable than others. This is because the producer organizations have a tendency to focus its effort on the observable variables. In this case that would be the balancing restriction of a non-profit organization. The “take-care-of-responsibility” can be specified as a minimum standard. In that case it would be focus on e.g., the number of promotional brochures distributed or number of ads on internet pages that promote the beneficiaries of the “take-care-of-responsibility” restriction, etc. There is thus a risk that there would be a focus on measurable aspects and not on less measurable aspects such as quality and efficiency. It could also be so that the balancing restriction is perceived as a “soft regulation”. If the producer runs with a profit loss, he would turn to the government and ask for more funds to produce marketing services for. In that case there is a risk that different priorities are made strategic and that the producer would choose to run with a profit loss in order to maximize the transfer of funds to the producer over time.

### 2.4.5.2 Performance-based budgeting

An alternative to pure fixed sum budgeting could be a pure per-unit budgeting. For instance, a measurement unit could be per tourist arrival or per dollar of tourism receipts (ref. Principle 1). Contrary to pure fixed-sum budgeting, where the producer receives a certain amount unconditionally of the level of production, a performance-based pure per-unit budgeting principle entails a variable budget income that is to some degree dependent on the production and 100% dependent on market performance. In a short-time perspective a profit-maximizing producer would want to produce marketing effort until the marginal cost of production equals the budget reward per unit. For the producer to have incentives to commit to investments and long-term planning, he will have to be compensated for the fixed cost. In a pure per-unit compensation system this must be incorporated so that the per-unit reward is set somewhat higher than the marginal cost. However, obtaining tourism influx from new markets or segments, or promote important tourism products that are harder to sell (e.g., rural tourism, eco-tourism, etc.), may be more costly than relying on traditional markets that produce tourists at low cost and effort. A better solution would be to base the reward on the economic value of incoming tourism (tourism receipts/expenditure), because this could reward the NTO to focus on higher-spending and longer-stay tourists; that is higher-quality tourists rather than higher quantities of tourists. More affluent tourists are also likely to be better culturally and environmentally educated and fewer in number. Higher quality tourists can reduce the cultural and environmental wear on the host country.

In any case, pure per-unit pricing may give incentives for selection and possibly reinforce the problem with the “tyranny of the served market”. It could also give weak incentives for investments in long-term engagements and “marketing infrastructure”. Even if the per-unit regulated producer is not profit-maximizing, but has a budget-balancing restriction instead, he will still have incentives for undesirable market selection, such as easy-access low-cost markets and short-term operational strategies. To meet the balancing restriction he will, compared to the fixed-sum regulated producer, have stronger incentives for undesirable selection of markets targeted and products promoted, and to reduce quality rather than production.

It is foremost these areas that distinguish performance-based principles from behavior based principles. Performance-based budgeting gives incentives for higher production, stronger incentives for undesirable selection, as well as it does not provide incentives to reduce the production to meet the balancing restriction.

A per-unit budget principle could also be combined with a “take-care-of-responsibility” for certain markets or products. Due to the fact that the per-unit principle inherently stimulates for production, it will not at the same time stimulate to adequate production. However, can such limitations in the form of “take-care-of-responsibility” with minimum standards for quality help to counteract incentives for undesirable selection.

### 2.4.5.3 Combined behavior- and performance-based budgeting

It is also possible to combine a fixed-sum principle with a per-unit performance-based principle. The fixed-sum portion of the budget can then be tailored to represent fixed cost, whereas the per-unit portion of the budget could be designed to give incentives for optimal production on the margin. It will be possible to achieve optimal production in such a system when the per-unit reward is equal to the benefits of the tourism industry's and society's marginal benefits of the marketing service, while the producer will produce until the marginal costs are equal to the per-unit reward. In theory this will be more effective as a budgeting principle because it will on the margin give more correct incentives for production.

If the producer also is restricted to zero profit and at the same time has a "take-care-of-responsibility", he will in theory face the same problems as discussed in a pure per-unit principle as discussed above. To meet the requirement of zero profit the producer will have incentives to reduce quality and use undesirable selection to save cost. The "take-care-of-responsibility" will also reduce the incentives that occur due to the per-unit principle to avoid higher risk markets and products, and possibly take on an undesirable short-term focus. The combination of per-unit and fixed-sum principles can thus give better incentives for optimal production. Compared to a fixed-sum principle it is a risk that, both under the non-profit and profit-maximizing condition, the quality will be prioritized lower.

### 2.4.5.4 Budgeting principles and risk-sharing

The budgeting principles have importance for risk-sharing between the regulator and the producer (i.e., between the NTO and its owner/financer). Risk-assumption has importance for the producer's incentives. The degree of risk on the part of the producer will affect the incentives for efficiency, quality of production, market focus, and long-term planning. Transfer of risk to the producer will help give stronger production incentives, but the risk transfer must be held in relation to the ability to assume risk and in the areas where the producer can influence the cost.

It can be discussed which actor is more capable of assuming increased risk. Normally one will assume that the government is more able than the producer. This is because differences in ability to bear risk, and differences in ability to diversify from risk. The government has the most wealth, and would normally be more able to handle variations in income than a single producer. The government also has a better ability to diversify from the producer-specific and industry-specific risk.

When designing a performance-based budgeting principle or a combined activity- and performance-based one, it is important that there is a connection between risk-bearing and the factors the producer can control or influence. In an NTO context, some factors affecting outcome will be almost completely beyond the NTOs' control, such as currency exchange rates and relative price level. Other factors can be more easily be controlled and influenced. So optimal effort should, in most cases, be strongly related to tourism market performance, but in some cases not.

With a full-coverage-of-expenses-based budgeting principle, through for instance a project sale-based principle, the producer will not bear any risk; all the risk is assumed by the government or any other project financier. Since the producer will be allowed full cost coverage, the producer has no incentives for cost efficiency. It is a danger that this can lead to too high quality and overproduction compared to what is socially desirable. For instance, the producer will have incentives to constantly generate new projects, resulting in a potential “overkill” of the market. Cost coverage principles such as this should give few incentives for undesirable selection, since one will achieve cost coverage for both high risk/expense and low risk/expense markets or products.

If the producer is financed through a fixed-sum principle without a “take-care-of responsibility” the producer will not bear any risk. It would give incentives for cost-efficiency because benefits from any saved costs will be retained by the producer. We have discussed earlier that pure fixed-sum budgeting can give incentives for too low production if it is not combined with a per-unit performance-based principle or “take-care-of-responsibility”. With such a combination, the producer will take over some of the risk-bearing as explained below.

In system with a pure per-unit performance principle, the producer would bear all the risk of both the cost and the income. It is not possible to *ex-ante* estimate exactly how much it will cost to attract a certain number of tourists or achieve a certain level of tourism receipts. Nor can the producer know for sure what the outcome will be in terms of incoming tourism traffic, even if the producer does the right things and puts forward optimal effort and resources. In other words the producer can risk incurring considerable expenses, while his income is dependent on per-unit market performance. So there is a risk associated with both the cost of production and the income stemming from market performance. In a pure per-unit principle the government will have to over-insure the producer for variations in tourism traffic through a risk premium, a premium higher than the marginal cost of attracting more tourists. Otherwise the producer will resist the added risk, and try to insulate itself from financial risk by lowering quality (e.g., avoid work with new, more risky markets, or only focus on short-term engagements and gain).

A benchmark/tournament type of per-unit principle can help reduce some of the external and less controllable industry-specific risk. A relative performance-principle, where the producer’s performance is measured and rewarded against the performance of comparable producers subject to similar industry-specific external risk, can help reduce external risk (ref. Principle 2)

When combining a fixed-sum and per-unit principle, which should be reflecting fixed and variable cost accordingly, the risk is shared between the government and the producer. In such a scenario the producer will be relieved from the risk attached to fixed cost, without weakening his incentive for cost-efficient production through the per-unit production-related variable cost.



#### 2.4.5.5 Budgeting principles and implications for NTOs

If left unregulated under a fixed-sum budgeting principle NTOs could, in extreme cases, do as little marketing effort and produce as low as possible to keep the costs at a minimum and extract the profit or consume the slack i.e., shirk on the residual between allocated budget and real costs. To deceive the stakeholders, NTOs could resort to inexpensive, yet non-productive activities directed at convincing stakeholders that NTOs' existence and operating expenses are justifiable and desirable. The NTOs could do so instead of spending resources on more costly but efficient production in the form of marketing effort (see also Table 2.6 earlier in this chapter). Such behavior can work as a "smokescreen" to detract attention from NTOs' real productivity. To any given stakeholder in government, tourism businesses, or among the public/taxpayers such NTOs may appear to be efficient, while in reality they are not, because they will not be using their resources as efficiently as possible to increase desired tourism traffic. For "clever" NTOs it may be possible to divert attention away from "hard" results e.g., increased tourism traffic, to "soft" measures hard to measure accurately, and focus on displaying high organizational visibility in the media or other high-profile venues. Lack of hard results may be written off as caused by exogenous factors and chance events such as e.g., "too low" budget, the weather, price level, currency rates, the tourism industry's behavior and its quality of products, national and international political conditions, and so on. The NTOs can then still maintain - or even increase - their budgets through lobbying efforts and negotiations. This may again produce more budget slack that can be consumed by the NTOs.

In the other extreme, NTOs' managements could try to create a "crisis" in order to boost budgets and produce marketing effort well beyond what is truly cost-efficient. For instance, the NTOs could point at similar organizations in other countries with huge and bloated budgets, and convince stakeholders that sponsors are under-spending on NTOs' budgets, and then negotiate increases in budgets. This can allow the organizations to grow, employ more staff, and do more activities than necessary to generate a desired level of tourism traffic. This may result in an "overkill" or oversell in the market, and thus resources wasted. The organizations could then be able to show some "hard" results, but through lobbying and visibility- and justification efforts manage to divert stakeholders' attention away from the cost of producing those results. The organizations have weak incentives to really discover and reveal to the stakeholders how much effort is really needed, i.e., their true costs, to be effective in the international tourism market. If left unchecked, NTOs may be able to maintain such budget over-spending for years and years.

The optimal regulation scheme fixes, in a detailed way, the organization's reward based on its observable actions (Olsen, 1992). In this case it could be the absolute or relative amount of traffic NTOs are able to generate. This will entice NTOs to find out through market research what the optimal is effort and produce it, neither too much nor too little. If NTOs put forward too little effort, they will get reduced budgets the next year if the tourism traffic decreases, and will thus be penalized. If NTOs put forward too much effort and "overkills" the market, they will not be able to extract a rent in the form of pure profit or slack because this will cost more than it pays. The increases in budget stemming from increased tourism traffic will not match the excessive cost - and the

organizations will be penalized because their increases in expenses will be greater than their increases in income. This should work as a corrective on NTOs' behavior in terms of resource allocation and level of production of marketing effort.

One possible practical solution for financing stakeholders is to offer NTOs a "budget-menu" comprised of various combinations of a fixed budget component and a performance-based component. We have included some budget simulations in Appendix 7 for illustration of the impact of such budget menus. For instance, NTOs can within reasonable limits be given the choice about how big of a component they would want to have performance-based, e.g., 40% fixed budget and 60% variable performance-based budget. Market conditions change and the market may be stable or turbulent, large or small, difficult or easy. We believe that under fair to good conditions, ambitious, self-confident, and risk-seeking managers acting on the behalf of the organization would then try to maximize the total budget by choosing a relatively high portion of performance-budget and low portion of fixed budget. This would also give the manager an incentive to reduce fixed operational cost e.g., to cut unnecessary staff, non-productive activity, etc. Variable cost could be increased that a larger part of the budget could be made available for tourism traffic generating marketing effort such as e.g., promotional campaigns, country image building, product development, etc. When market conditions are turbulent more and difficult, and risk is thus greater, a higher portion of fixed budget would probably have been chosen.

On the other hand, an obvious practical problem with such sophisticated regulation systems is their complexity. The optimal budget menu and the funds transfer process from the governments or other stakeholders will in a complicated way generally depend on the governments' access to all relevant data needed for the set-up and execution of the regulation system. This means that some resources will be consumed by the governments to design and follow up such systems and for the organizations to understand, familiarize themselves with, and adapt to the regulations (Olsen, 1992).

#### 2.4.6 Common goods and the free-rider problem

The form of international marketing activity NTOs are responsible for can be characterized as a *common good* (sometimes called *collective good*). Common goods have the trait that the use and benefits from it can not be made exclusive only for those who invest in it or pay for it to be made available and maintained (non-exclusivity). Another trait is that consumption of additional units of the good involves zero marginal costs of production (non-rivalry) (ref. e.g., Olson, 1965:14; Nicholson, 1988:729; Elster, 1998). These are a kind of good it is difficult to produce and commercialize in an effective manner through ordinary market mechanisms (Jakobsen, 1998). Benefits derived from the marketing effort and services made available by NTOs can be enjoyed by e.g., tourists, the tourism industry and suppliers to that industry, and the local population, as well as local and national governments (Farstad, Skalpe and Troye, 2001). This is regardless of whether all of these actors that are willing to pay for it or not. The inability to exclude non-paying beneficiaries will make under-investment in this type of common good likely. There are several reasons why the common goods issue (such as NTO tourism marketing effort) is especially important in the travel industry compared to other industries. The demand for typical tourism services such as accommodations,

restaurants, transport, and attractions often depend on international marketing effort to persuade potential tourists to choose a given country as their destination. Moreover, successful marketing effort by NTOs will be beneficial for businesses *outside* the travel industry e.g., suppliers, retail etc., as well as the local population, who benefit from employment, development of tourism infrastructure, and revenue to the local economy due to increased tourism traffic. So (moderate) development of tourism can make it more attractive to live at a given destination. This is because the local population can enjoy the same development of tourist attractions and infrastructure as the tourists enjoy. Local and national governments also benefit from increased direct and indirect tax revenue and legitimate demand for public services. Thus, tourism has many beneficiaries beyond the travel industry itself (see also section 3.1 in Chapter 3).

The problem with this type of common goods is to draw the line between who really benefits from the tourism marketing derived goods and who should be responsible for financing NTOs. This type of financing problem is apt to arise because no single actor has the exclusive control of the benefits derived from the NTOs efforts. Many others can take advantage of NTOs' efforts and act as free riders. This makes it difficult to find one particular private sector actor or group who would be willing to accept the responsibility to fund the NTOs. No single private sector actor or group would normally like to pay single-handedly for services that also benefit a number of stakeholders non-paying stakeholders. This can explain why there are very few NTOs that are funded solely by the tourism industry without any kind of financial support from the government. Without any kind of regulation or legislation, e.g., through a dedicated marketing fee on the industry, a hypotecrated tourist tax, etc. that provides a basis for private sector funding, it is hard to create and operate NTOs that are to be funded by the industry alone on a pure voluntary basis.

We believe that performance-based budgeting systems can mitigate the common goods problem somewhat. However, but it will be naïve to think that such an arrangement will rid us with the common goods problem entirely. There is still an incentive for the private sector actors to behave in an opportunistic way and fee-ride on benefits from the marketing efforts of NTOs. However, the industry actors may have other motives for supporting (or not supporting NTOs) than pure short-term opportunistic agendas. For instance, we could consider the following notion: If the budgets of NTOs were based on market performance, the NTOs would have had stronger incentives to make market-oriented decisions. In turn, this would probably improve NTOs' market performance, since market-oriented organizations usually perform better, as discussed in Section 2.1 and supported by empirical research. Improved market performance, e.g., higher tourism receipts, would then again improve the industry's overall profits. The businesses would then probably realize that well performing NTOs are very beneficial for their own performance. They would also realize that NTOs' market impact could be enhanced by more resources, and could try to affect this market impact by investing more of their own resources in NTOs' budgets. Improved profits due to NTOs' activities would also provide the businesses with more extra resources that can be freed for investments in e.g., international marketing channeled through NTOs. The businesses could then invest their resources in funding of NTOs' budgets under the certainty that these resources probably would be used in a market-oriented and efficient way by NTOs. Under an activity-based

system, they could not have this certainty, and could risk that their invested resources could be wasted through shirking or other types of misallocations, etc. As Peabody (1995) pointed out in the case of the World Health Organization (discussed later in Sections 2.5.1-2.5.3), the problem that seem to deter private sector funding of such organizations can (at least partially) be traced to the gap between promises and accountability. A performance-based budgeting system may help close this gap; then NTOs will be paid budget funds based on real market performance rather than ambitions and promises about results. Thus, we believe performance-based budgeting systems could increase the private sector's willingness to contribute to NTOs' funding. Increased private sector investments could also trigger a greater willingness on the part of the governments to invest more resources in NTOs' budgets.

Local-level tourism marketing organizations organized and funded by the private sector do occur more often than privately funded NTOs. It is arguably an easier task to obtain private financial support for the more specialized type of local tourism marketing organizations than for NTOs, because NTOs would have to engage in a more generic type of international marketing activity. On the local level it is easier to identify precisely who would benefit from tourism marketing efforts and easier to determine who should pay for it. So generic international marketing on the national NTO level is probably perceived more of a common good type of service than more specialized destination marketing on the local level. Therefore, the free-rider problem is more substantial with regards to funding of NTO than with local equivalents. Considering this, the use of performance-based budgeting may increase the willingness among private sector sponsors to participate because it can help reduce the sponsoring stakeholders' perceived risk somewhat. Sponsoring generic international marketing would probably be perceived as more risk-laden for the sponsors in a cost-benefit consideration than sponsoring specialized local marketing efforts of more individual business-directed character. Spending one dollar on generating primary demand for the firm's products or local destination would probably be perceived as more likely to give "probable gains" than spending one dollar on generating secondary demand for the nation's tourism products through NTOs' marketing activity. Thus, performance-based budgeting could be more beneficial in a private NTO funding scenario, when low private sector willingness to contribute financially is a concern. This is because such a system transfers some of the risk for the outcome from the private sponsors (principals) onto NTOs (agents), since the sponsors would not risk having to pay very much if NTOs' performances are weak. We will revert to the issue of the potential benefits of performance-based budgets related to the private sector willingness to engage in NTOs' funding in Section 2.5.3 later in this chapter.

#### **2.4.5 Conclusions to be drawn from public economy theory**

The body of public economy theory we have discussed here is useful for our purposes with regards to: whether NTOs should be private or public entities; how ownership can affect the Long-Term Perspective and Market Focus of NTOs; and whether outcome-based versus behavior-based budgeting is feasible in terms of how it motivates NTOs for efficiency and optimal production. We have also chosen to discuss the *common goods problem* under the public economy section, because of its relevance to the context-related

discussion on public versus private funding of NTOs. Much of the theory developed in the field of privatization points to that the fact that private ownership, in most cases, is more cost efficient than public operation. This notion also has broad empirical support. The differences in cost efficiency are explained by the fact that the profit from the organization's operation under private sector operation will be allocated to the owners, and thus acts as an incentive mechanism for focusing on efficiency, whereas in public operation this is not the case. We also argue here that private ownership can increase the NTOs' propensity to be market-focused.

However, in the NTO context there are other societal considerations than cost efficiency only, which may call for some government intervention through ownership or control and government funding of NTOs. Some researchers disagree with this idea (e.g., Shleifer and Vishny), and argue that government ownership is not a guarantee that public interests will be served in the best possible way. We argue that in some instances, government ownership could help the NTOs retain a Long-Term Perspective in planning and operation, provided that governments do not cut NTOs' budgets arbitrarily from one year to another.

Empirical research by the World Bank on state owned enterprises in developing countries shows that performance contracts often fail to have the expected effect on performance. This is because these contracts often fail to reduce the management's information advantage; seldom provides real performance incentives to managers; and that managers can negotiate soft targets that are easy to reach. Moreover, the government often fails to follow up on commitments in the contracts, which reduces the incentive effect. Lessons can be learned from this study in how performance-based budgets for NTOs should be designed and used, and what *not* to do in such a design and implementation process.

In the NTO context governing stakeholders could often need deal with cases of market failure, e.g., whenever NTOs have something close to a monopolistic position. The NTOs' information advantages can be used to improve their position on the expense of taxpayers beyond what is socially desirable. The governments' task is then to try to motivate NTOs to manage cost efficient production, and at the same time extract some of the pure rent so that the NTO will not be able to (unreasonably) shirk on excess resources. The task is also to try to motivate NTOs to tailor production to its true cost. We believe this can be achieved best through a relative performance-based budgeting principle based on "hard" measures to motivate for cost-efficiency and combined with a fixed-sum principle to insulate the NTO from unreasonable risk.

The outcome of the kind of marketing activities NTOs perform are in many ways a common good, which may explain why NTOs are hard to organize and finance on a voluntary private basis. Tourism activity has many beneficiaries beyond the tourism industry itself, and many actors can therefore act as free riders. This will reduce the tourism industry's willingness to fund NTOs' operation. The government and society enjoy benefits from tourism as well, which justifies public funding of NTOs' tourism generating activity. Introduction of outcome-based budgets can possibly increase private businesses' willingness to contribute with funding. It transfers some of the risk from the private stakeholders to the agent NTOs, and thus reduces risk for the stakeholders. It may

also be easier to “sell” a funding scheme where NTOs “get what they deserves” and are rewarded upon merit to the private industry, which often faces a similar scheme in real business life (see also Section 2.5.3 below).

**Table 2.9**  
**Conclusions from application of public economy theory**

Theory	Consideration	Present in the NTO context	Attractive to use behavior-based control	Attractive to use outcome-based control	Recommendation about governing principle to use	Comments/ references to theory area
Public economy theory	Cost-efficiency, market focus	Probably not	NO	YES	Outcome-based budgeting, private ownership	Private profit claim = incentive for efficiency and market focus
	Societal goals other than cost efficiency and profit	YES	N/A	YES Positive outcome benefits all stakeholders	Public ownership and funding	Where monopoly power, externalities, societal or other distributional issues raise concerns, privately owned profit-maximizing firms, which a commercial version of an NTO <i>could</i> be, may fail to address these concerns
	Performance contracts	Few so far (see Table 5.1)	N/A	YES, but -Hard targets -Real incentives Commitment	Behavior-based budgeting	W.B. Study: Many weak performance contracts in use = no or little effect on performance
	Market failure: Monopoly situation, hidden true cost	YES	NO	YES	Outcome-based budgeting	NTO has information advantage and seeks rent. Motivate NTO to tailor production to true cost.
	Lack of competition	YES	NO	YES	Relative outcome-based budgeting	Benchmarking and relative performance measurement useful to reveal true cost and motivate for increased effort. Chance-event effects reduced.
	Incentives to over- or under-produce on quantity and quality	YES (under various budgeting schemes)	(YES) (fixed sum = pos. for long-term oper. )	YES To motivate for increased production	Combined behavior- and performance - based budgeting	Take-care-of-responsibility along with combined fixed sum and relative per-unit-budgeting seems optimal
	Common good, Non-exclusivity, free-riding problem, low private sector willingness to pay for budgets	YES	NO	YES	Public ownership and funding  Outcome-based budgeting & private funding	Some government funding and operational control may be necessary. Risk transfer through outcome-based system probably increases private willingness to pay (ref. also sct. 2.5.3)

The main conclusions from public economy theory are summarized in Table 2.9. In sum, our application of public economy theory suggests that private ownership has some

cost efficiency benefits. However, pure private ownership may be unrealistic due to the common goods problem and funding difficulties, and could be undesirable due to important societal concerns. At least some degree of government funding and control may be needed. On the other hand, pure government operation and funding can yield inefficiency and budget swelling, so private co-funding and co-control may also be needed to help avoid these problems. Striking a balance between public and private control and funding is a challenge, but should not be a problem impossible to overcome. The exact make-up of private and public influence should of course be adapted to local conditions. The Canadian NTO, which we will look closer at in Appendix 5, is a good example (50%/50% public/private funding).

Several aspects emerging from the application this body of theory call for a performance-based system. Notwithstanding, an outcome-based budgeting system has to be designed carefully for it to have the intended effect on NTOs' performance. If not, it is a waste time of effort (with reference to the World Bank study).

## **2.5 Corporate governance theory**

Unambiguous incentives are necessary to make organizations work efficiently and effectively. We believe that NTOs, often being government controlled, bureaucratic, and inflexible in their form, can be changed into well-functioning marketing organizations when equipped with the right incentives and control structure. This is mainly a matter of aligning the incentives of NTOs' stakeholders, the organizations themselves, their management, and the employees. Corporate governance theory offers some suggestions how to deal with these issues, as shown in Table 2.10 below.

### **2.5.1 Vague goals, many demands, and output difficult to measure**

John W. Peabody (1995) published a critical organizational analysis of the World Health Organization (WHO), which we believe can be applied and adapted to the analysis of NTOs as well. An organization like the WHO has many features in common with NTOs. Apart from the fact that the WHO's output is "world health" and NTOs' outputs are "international tourism marketing", these organizations often face a similar operating environment. The make-up of stakeholders of these organizations are characterized by the fact that: stakeholders are many and diverse; goals are often vague and sometimes conflicting; outputs are difficult to measure; the main output is a common or collective good; the stakeholders actually funding the organizations are not always identical with the beneficiaries of the organizations' services; national governments are often involved in controlling, monitoring and funding the organizations, etc. The following discussion is based on Peabody's analysis of the WHO, and we have applied his findings where appropriate and adapted them to the NTO context.

**Table 2.10**  
**Corporate governance theory's relevance for the independent and dependent variables**

<i>Independent variables' relevance for study</i>		<i>Reference to text</i>	<i>Dependent Variables' relevance for study</i>		<i>Reference to text</i>
<i>Budgeting principle</i>	1) Behavior-based budgeting systems can create procedural organizations. Performance-based budgeting can align goals and reduce cross-incentives.	2.5.1	Market Orientation	Increased decision autonomy and delegation of real authority for NTOs can increase NTOs' motivation for information acquisition related to the tasks they are set to do (e.g., acquire market information), since NTOs need not worry that their decisions will be overruled by governing stakeholders. (See also under O.F. below)	2.5.4
	2) Team based- bonuses (here rewards through NTO budgets) could be more effective as incentives than individual management compensation.	2.5.6.1			
	3) Performance-based incentive systems appear to be more effective than promotion-based incentive systems.	2.5.6.2			
	4) Relative performance-based incentives are more efficient than absolute performance-based incentives.	2.5.6.3			
<i>Funding source</i>	Lack of accountability has probably widened the gap between payments, promises, and performance. Performance-based budgeting principles can help close this gap, and maybe increase private sector NTO-funding.	2.5.3	Long-Term Perspective	Performance based-budgeting could reduce the need for the stakeholders to constantly intervene in NTOs' matters, and thereby avoid frequently changing NTOs' assignments. Long-term contracts (budget periods) can increase NTOs' loyalty to stakeholders' interests. When the NTOs' planning horizon becomes too short, there could be a bias towards quick results on the expense of long-term gain.	2.5.5
<i>Ownership/ org. control</i>	NTOs' many stakeholders have different criteria for measuring NTOs' success. Each stakeholder with e.g., ownership influence could look to the organization to support its own agenda. Stakeholders must often evaluate an unspecified product, and NTOs must respond to shifting criteria that measure their success. This is probably not good for NTOs' productivity.	2.5.1	Operational Freedom	1) Performance-based budgeting could reduce the need to impose procedural constraints on NTOs' activity, and thus increase NTOs' O. F.	2.5.2
				2) Increases in NTOs' real authority and decision autonomy (i.e., O. F.), could foster NTO initiative, participation, and information acquisition (i.e., M.O.)	2.5.4

Peabody's study of the World Health Organization is useful for our purposes. Like the WHO, a typical NTO often has a number of more or less vague goals and multiple tasks. Common for the goals is that they often defy concrete output measure. Consider the following sample of goals and objectives of a few different NTOs:



“Promotion of international tourism through efficient and effective provision of overseas publicity; dissemination of tourist information to foreign tourists; engagement in other activities deemed necessary to increase the number of visits by foreign tourists, etc” (Japan’s NTO). “Enhance the effects of tourism promotion activities and the competitiveness of the tour and travel trade by establishing efficient partnerships with its private sector members.” “Escalate into an organ with the professional responsibility for tourism promotion in the 21<sup>st</sup> century, etc.” (Korea’s NTO) “The NTO shall contribute to stimulate and strengthen the travel industry’s profitability and competitiveness” (Norway’s NTO).

When does one for instance achieve “effective and efficient publicity” or “escalation into an organ with professional responsibility for tourism promotion” or “stimulation and strengthening of the travel industry’s profitability and competitiveness”? Since NTOs’ goals are often not concrete, they are open to a wide range of interpretation by different stakeholders. As we have discussed earlier in section 1.2 (ref. also Section 3.2 and Figure 3.4 and 3.5 in Chapter 3), this legion of NTO stakeholders have different criteria for measuring the NTOs’ success. Each supporter of the organization, whether it provides funding or other influence, looks to the organization to support its own agenda. This creates an almost incomprehensible enigma; stakeholders must evaluate an unspecified product and the organization must respond to shifting criteria that measure its success (Peabody, 1995).

According to Peabody, organizational theories can offer some clarification in such a situation. Like the WHO, NTOs can in general be viewed as procedural organizations, defined here as an organization where it is possible to observe what the organization does but not what it produces. Tasks and behaviors are, therefore, easy to specify but difficult to evaluate. This means that NTOs’ stakeholders can hardly control them unless they set up procedural constraints on its behavior that the organizations must follow. This process can result in an ever-multiplying list of rules, procedures, and demands sometimes found in NTOs’ operational manuals. Procedural agencies like NTOs are vulnerable to politicians and other governing stakeholders who tell them how to do their job but offer little help when it comes to evaluating how the job has been done. External criticism can result in even more elaborate procedural constraints which detract even further from focusing on specific marketing objectives. NTO staffs could find themselves in a situation where they spend a lot of time pursuing internal procedures unrelated to marketing output. The staff supervision by NTOs’ managers can easily end up focused on processes and not on real accomplishments. If criticized, NTOs’ staff can then point to adherence to NTOs’ many rules or procedures generated by NTOs themselves or set by their external stakeholders. This could make NTOs’ staffs, focusing on self-survival in an environment perceived as hostile, e.g., due to external criticism, displace the organizations’ goals with their own self-interests. (For instance, with explanations of under-performance and failures such as: “It is not my responsibility, I just followed the rules”, and so on). Yet rules and procedures can only serve as a justification of processes, not outcomes. In the organizational parlance this makes for looser couplings between the organization’s goals and its daily activities (Peabody, 1995).

## 2.5.2 Alignment of goals

To avoid this situation, organizations like NTOs need to develop incentives that align staffs and managements' individual goals closer to NTOs' real external goals (i.e., tourism marketing). Professional staff must be given specific outcome objectives and thereafter assigned: 1) budget constraints; and 2) policy boundaries. They should be allowed the autonomy to do their work unimpeded by excessive supervision. Evaluation of staff should focus on these outcomes and avoid deleterious effects of excessive procedural evaluation i.e., how well the employees follow the organizations' rules and procedures (Peabody, 1995). This process is critical because it would reorient the incentives for NTO staff. Using a performance-based principle, where both managements and staffs are evaluated, rewarded, and made accountable based on output, as the model for organization - would allow staff to work for their own self-interests and for NTOs' at the same time. This should also eliminate the problem of cross incentives and goal displacement for staffs. Such an explicit policy should also reduce the incentives for the management to over-monitor staff, and reduce the need to constantly generate rules and procedures.

## 2.5.3 Structural reform and funding

Finally, structural reform of NTO governance through performance-based budgeting principles can also offer a way to increase NTO funding. To do so, the NTO must align the demands of the many stakeholders with the resources of the few sponsoring entities. This is a key point and has an important implication: Both the NTOs' managements and the NTAs or other stakeholder coalitions need to openly articulate a set of detailed performance objectives that are acceptable, recognizable, and measurable. Once set, they should be used as the standard to measure and evaluate NTOs and their managements. One of the probable reasons why many NTOs have not garnered more regular private sector budget funding is that a lack of accountability has widened the gap among payments, promises, and performance. Performance-based budgeting principles can help close this gap.

## 2.5.4 Operational freedom – why is it important?

Aghion and Triole (1997) found that in an organization, the delegation of formal authority to a subordinate (agent) will both facilitate the agent's participation in the organization and foster his incentive to acquire information about the corresponding activities. They also showed that centralization (i.e., the non-delegation of formal authority) may jeopardize communication by making the agent concerned about being overruled. Performance measurement (i.e., through performance-based budgeting principles) should reduce the principals' need and incentives to monitor the agent, and reduce the probability that the principal overrules the agent. This increases the agent's real authority and decision autonomy, which in our case is analogous to NTOs' Operational Freedom.

If we apply Aghion and Triole's findings on the organizational level in the NTO context, one could argue the following: Implementation of performance-based budgeting principles reduces the stakeholders' need and incentive to monitor the NTO agents and intervene in NTOs' planning and operational activities. Reduced monitoring and non-

intervention by the stakeholders constitutes delegation of decision authority to NTOs, which also means a reduction of stakeholders' supervisory control of NTOs. This is offset by the potential efficiency gains due to increased NTO initiative and participation, which is also beneficial to the stakeholders. For instance, it could strengthen NTOs' incentives to acquire information about what activities that will be needed to undertake to increase tourism traffic. In other words, it increases NTOs' incentives for market-oriented activities. Giving the NTOs increased Operational Freedom in exchange for performance-measurement and budgeting will most likely foster increased (desirable) information dissemination from NTOs to the stakeholders such as e.g., the NTAs, tourism businesses, or trade organizations, etc. because NTOs will not need to worry that their decisions will be overruled by the governing stakeholders. This means that performance-based budgeting should increase NTOs' Operational Freedom, which in turn could give NTOs incentives for a stronger Market Focus. This is of course a preferable situation for all parties.

### 2.5.5 Long-term perspective as related to performance-based budgets

Narayanan (1985) pointed out that business managers have often been accused for working for short-term profits at the expense of the long-term interests of their firms. The explanations of this short-term bias falls into two categories: One, the stockholders want quick profits, and their short-term view is reflected in the managerial decisions. Two, profit sharing by the managers, i.e., making either whole or part of their pay contingent on performance, tends to make them "quick-profit" oriented. The manager could have some private information profits that is unavailable to the investors, i.e., exclusive information about which project to choose or course of action to take that will yield short-term versus long-term profits. He then *might* make decisions to yield short-term profits at the expense of the long-term interests of the organization. Among other things, Narayanan (1985) shows that the longer the duration of the manager's contract, the lower the probability that he will choose quicker returns that are sub-optimal. The longer the duration of the contract, the more benefit to the manager from future cash flows, and hence reducing his incentive for sacrificing these long-term benefits for short-term ones.

Narayanan's findings have some implications for the NTO context as well. Say we have a situation with an NTO manager whose budgets or salary is subject to determination based on performance. The manager also has private information about which activities that will increase the likelihood of short-term tourism traffic and which activities that will generate long-term tourism traffic. We have discussed earlier (see Section 2.2.2) that information asymmetry advantageous to the NTOs and their managers, is likely to exist in the NTO context. At the same time there might be a pressure from the industry to promote tourism intensively "here and now" so that the businesses could earn short-term profits. The more difficult the businesses' financial situations are, the stronger the pressure to generate short-term sales through heavy tourism promotion. Given that NTOs' budgets and the managements' pay were based on annual tourism traffic increases, the managers could resort to activities that would boost short-term traffic on the expense of long-term sustainable tourism. A manager could, for instance, spend massive resources on promotional campaigns that exaggerate the quality of his country's tourism products and services. This could result in artificially inflated levels of tourism,

yielding great short-term performance statistics, but evidentially create tourism congestion, tourism infrastructure and environment wear-out, and hence customer dissatisfaction. This short-term performance effect would temporarily earn the NTO higher budgets and increase the managers' bonuses. This would then be on the expense of the country's long-term attractiveness as a tourist destination, and thus be negative for long-term sustainable tourism.

Narayanan suggests that to offer long-term contracts can increase the manager's loyalty to shareholders' interests. This technique is used in Japanese firms with apparently successful results. In addition, the managers' task assignments or instructions from the stakeholders should not be changed too frequently. In the NTO context this would be the same as providing NTOs with greater operational freedom. If assignments are changed too frequently, which could happen if many different stakeholders try to intervene and control NTOs, the managers' planning horizon becomes too short, and the propensity for a bias towards quick results increases. This is because the managers' subsequent reputation would usually depend only on their performance in their new assignments, and hence, will be indifferent to old assignments. Performance-based budgeting principles should rid the managers with the problem of frequently changing assignments, since the managers would have the freedom to decide what actions to undertake. On the contrary, a behavior based-principle, where the stakeholders are involved in deciding on the plans and activities, could shorten the managers' planning horizon and incentives for a long-term perspective.

A solution to this short-term bias could be to offer a budget policy that would reflect a long-term perspective. Budgets could be determined for a longer period of time, increasing the usual one-year period to a period of e.g., three years. One could for instance use a sliding three-year average performance measure to determine budgets; a system sometimes used in the private sector. This would reduce the incentive for sacrificing long-term performance for short-term gain. At the same time this can increase NTOs' ability to plan ahead because their budget situation would be more predictable and have less fluctuations from year to year so that NTOs can commit to long-term activities. Performance based-budgeting could reduce the need for the stakeholders to constantly intervene in NTOs' matters and thus avoid frequently changing NTO assignments.

## **2.5.6 Incentives and performance compensation**

In the following sub-sections we will discuss the issues of individual vs. organizational compensation, promotion-based vs. performance-based rewards, and relative vs. absolute performance compensation.

### **2.5.6.1 Individual versus organizational incentives and compensation**

Baker, Jensen and Murphy (1988) recognize that few decision makers in organizations are one hundred percent owners of the residual claims, and this layering of agency problems can induce serious lapses in the incentives of decision makers to devise and enforce efficient contracts and compensation systems. A literature summary by Milkovich (1987) in the personnel literature shows that merit pay and bonuses based on individual performance are less effective than profit sharing, stock ownership, and team-based bonuses. A New York Stock Exchange survey indicates that seventy percent of

firms with profit sharing report that they lead to improved productivity. The NYSE Office of Economics Research study, summarized by Ehrenberg and Milkovich (1987), concludes that “gain sharing can play an important role in motivating people to be more productive” (Baker, Jensen and Murphy, 1988).

In the NTO context, there is usually no profit that can be shared. Of course, one could give the NTO managers individual bonuses based on tourism traffic performance, assuming that this would have a significant impact on NTOs’ productivity and performance. However, Jensen and Murphy (1988) found that the empirical relation between top-level executives and firm performance, while positive and significant, is tiny. When the reward for performance is channeled through the budget of NTOs, this reward system may serve as a team-based bonus scheme for NTO employees. Rather than profit sharing, one would then have residual “resource sharing” among management and employees. A higher budget, as a reward for increased performance, will give the organization advantages that can be enjoyed by all employees - not only top management - and thus have a motivational effect on lower level employees as well as management. According to the findings by Ehrenberg and Milkovich, this would be more beneficial than just linking individual management bonuses to performance. Thus, a merit system that rewards the whole organization through its budget would be preferable to a system that rewards only top executives.

There are some other reasons why we believe organizational incentives through performance-based budgets would be more effective as incentives than individual management merit compensation. First, a budget increase as a result of improved performance would make the top managers have more resources available, which would increase the organizations’ ability to engage in new projects, start promotion campaigns, and other marketing activities. Obviously, a bigger budget is desirable for both managers and employees. By the same token a budget cut would not be desirable from the managers and employees point of view, since it would reduce the level of resources and thus the activity span. From the managers’ point of view, a budget cut would make their working situation more difficult, since they may not be able start new projects, and would possibly have to cut cost and reduce staff, which is normally an unpleasant situation. Likewise, a budget increase would improve their resource-dependent freedom to act and they would avoid unpleasant cost cutting. This may be far more important as a motivating factor than an individual cash bonus, which is shown to have only a minute effect. Secondly, a budget cut due to poor performance would be visible to all stakeholders and NTO employees because NTOs’ general budget information is usually open to the public. Executive pay is usually a less conspicuous matter, and of lesser interest to the stakeholders and general public. So performance visibility through a budget-based reward system would probably be more motivating to the management and employees, since both staff and outsiders can easily see how well NTOs are performing when budget information is made public. Third, when budgets are made performance-contingent it will probably increase the stakeholders’ interest in NTOs’ budgets and how resources are spent. This could increase the stakeholders’ interest in monitoring of NTOs’ performance. Generally, stakeholders are probably more interested in how much financial resources NTOs get and how resources are spent, rather than how much the top manager is paid. Stakeholder monitoring could reduce the opportunities for the managements and

employees to shirk on NTOs' resources undetected. It would, for instance, not be socially acceptable in relation to monitoring stakeholders and employees if the top-managers would award themselves higher pay or persuade the NTO boards or NTAs to grant them pay rises when the NTOs are performing poorly.

Jensen and Murphy (1988) argue that the apparent anomalies in executive-compensation contracts may be explained by the strong political forces operating in both the organization and in the public sector that effectively constrains the type of contracts written between managers and shareholders. Given that top-management performance compensation seems to have only little impact on productivity in the commercial and private sector context, one cannot expect any stronger effects in the often non-commercial and semi-public NTO context either. On the contrary, it would probably be even harder to design top-management compensation systems that are effective in the NTO context. This consideration, along with the arguments listed above, suggests that an organizational performance-based reward system through budgeting is preferable to an individual top-manager performance-compensation system.

### **2.5.6.2 Performance-based systems vs. promotion-based systems**

An alternative to a performance-based reward system is a promotion-based reward system, where good individual performance is rewarded with upward promotion in the organization. This is often used in the public sector, and is probably common reward system for many NTOs. However, there is one important problem with this kind of system. It requires organizational growth to “feed” the reward system. Such a system is likely to generate problems in a slowly growing or shrinking organization (Baker, Jensen and Murphy, 1988). In slowly growing organizations with free cash flow, promotion-based reward systems encourage managers to spend resources on unprofitable growth rather than paying out cash to shareholders (Jensen, 1986a, 1986b). Normally NTOs do not pay out cash to stakeholders, but managers may spend excess resources to expand the organization, which in turn provides promotion opportunities for NTO employees and management. Obviously, stakeholders would not want NTOs to engage in non-productive organizational growth, so that the organizations end up as low-efficiency colossuses. A promotion-based system could even fuel the tendency of public bureaus such as NTOs to budget-maximize (see Sections 2.2 and 2.3 earlier in this chapter).

For example, properly structured compensation policies at all levels of the organization can punish top executives for unprofitable and unproductive growth without degrading the incentives for lower level managers. Finally, it is often argued that promotion contests are desirable since they need only to be based on rank order and thus can reduce risk or random noise common to all contestants – but bonus systems based on rank or relative performance can easily achieve these same objectives (Baker, Jensen and Murphy, 1988).

### **2.5.6.3 Relative performance-based systems vs. absolute performance-based systems**

Contracting theory predicts that pay should not be based on factors beyond the control of the executive – management compensation should therefore be based on performance

relative to the performance of all firms or firms in the same industry, rather than on absolute measures of firm performance (Holmström, 1979). This is to remove the effect of external factors. The theory is compelling, but imprecise; managers should not be insulated from outside factors if they can take actions that reduce the firm's exposure to losses from such sources. This caveat aside, it seems desirable and feasible to base the pay on relative performance instead of absolute performance (Baker, Jensen and Murphy, 1988). However, boards of directors do seldom use relative performance measures. Neither absolute nor relative performance-compensation is common in the NTO context. Jensen and Murphy (1988) show that absolute firm-value changes measured relative to the industry are better predictors of changes in salary and bonuses than value changes measured relative to the industry and the market (Baker, Jensen and Murphy, 1988).

Reverting to the NTO context, we have discussed earlier that NTO managers face many more or less uncontrollable events that may affect NTOs' market performance. However, these factors should also have a similar impact on other comparable NTOs' (i.e., from the same region or targeting the same markets) operation and performance. A relative performance-based system should remove or reduce the effect of some of these factors. Baker, Jensen and Murphy also raise an important point that it is not the purpose to have managers (i.e., the NTO) insulated from outside factors. Given the proper incentive e.g., through relative performance-based budgets, managers could be motivated to act proactively to mitigate the effect of those factors. An NTO manager could do this by e.g., changing key markets, switching to a different market segment, encouraging development of new product/packages, increasing promotion activity, etc. We therefore suggest that relative-based performance budgeting is preferable to absolute-based performance budgeting principles. The empirical results reported in Chapter 5 show that our respondents to a large extent agree with this conclusion.

### **2.5.7 Conclusions from application of corporate governance theory**

The conclusions from this body of theory are summarized in Table 2.11 below. Peabody's (1995) critical study of the WHO brings up some concerns about similar non-commercial organizations that could be comparable to the NTO context. Like the WHO, NTOs may face the same kind of scenario where e.g., goals are vague, there are many different demands from many diverse stakeholders, and organizational output is difficult to measure. In such a scenario, there is a danger that NTOs, as in the case of the WHO, can develop into rule-based procedural organizations. Managements and employees may develop a too strong focus on adherence to rules and procedures rather than on productive output, which is not beneficial for the organizations' work climate and productivity. Thus, there may be a need for structural reform through alignment of goals and incentives for the NTOs' employees, the organizations themselves, and their stakeholders. This can probably be achieved best through the use of performance-based rewards systems, which will turn the focus to accountability and output. It can reduce managements' need to closely supervise staff in terms of rules-adherence, and then free more time and energy that can be made available for strategic marketing work. Introduction of performance-measurement, accountability, and pay-for-performance systems may also help attract more private sector funding.

**Table 2.11**  
**Conclusions from application of Corporate Governance (Finance) theory**

Theory	Consideration	Present in the NTO context	Attractive to use behavior-based control	Attractive to use outcome-based control	Recommendation about governing principle to use	Comments/ references to theory area
Corporate Governance theory	Vague goals, many stakeholders, rule-based system, output difficult to measure	YES	NO	YES	Outcome-based	Ref. WHO-study: NTO may hide lack of performance behind adherence to rules. Performance-based funding can help alignment of goals and funding
	Operational freedom	Probably not	NO	YES	Outcome-based	Performance-based funding may help NTO gain more operational freedom, and stakeholders to relax behavior-based control. Can increase NTO initiative and participation
	Short-term management focus	Probably	N/A	N/A	Long-term budgeting practices	Long-term budgeting practices could make NTO management less likely to only focus on short-term goals and maximize short-term compensation.
	Individual vs. group/team bonuses and compensation	No available information on this issue	N/A	N/A	Outcome-based organizational bonuses	Group/team bonuses and compensation in the form of performance-based budgets may be more effective than individual management bonuses
	Absolute vs. relative performance-based budgets	Neither is presently a common budgeting system	N/A	N/A	Outcome-based budgets based on relative performance	Relative performance-budgeting can remove some the effect of uncontrollable external factors. Can be more fair and motivating for NTO.
	Promotion-based reward systems vs. performance-based reward systems	Promotion – based is probably common	NO (Promotion-based)	YES (Performance-based)	Outcome-based	Promotion-based system can cause undesirable organizational growth. Relative-performance based systems can help avoid this tendency.

Research on the impact of length-of-contact for managers suggests that offering long-term contracts can increase the manager's loyalty to shareholders' interests. A long-term performance-based budgeting system may have the same effect on the incentives for long-term planning for NTO managers. Furthermore, the managers' task assignments should not be changed too frequently, which can be achieved by providing NTOs with more Operational Freedom. Implementation of a performance-based budgeting principle could relax stakeholders' need to intervene in NTO managers' decision process. It should rid the managers with the problem of frequently changing assignments, since the



managers would have more freedom to decide what actions to undertake. On the contrary, a behavior based-principle, where the stakeholders are constantly involved in deciding on NTOs' plans and activities, could shorten the managers' planning horizon and incentives for a Long-Term Perspective.

Conclusions from some of the personnel and finance research literature we have reviewed appear to suggest that team-based bonuses and profit sharing appear to be more effective in terms of organizational performance than top-executive cash bonuses.

We argue that rewards through performance-based budgeting systems will have much of the same traits as a team bonus or profit sharing reward scheme in the private sector. Thus, we believe this kind of reward system will have a stronger effect on organizational performance than using an individual bonus system aimed at NTOs' top executives.

Unfortunately, the kind of promotion-based reward-systems often used in the public sector have an important flaw: It requires organizational growth for the system to have any motivational effect on lower-level managers. Therefore, it can provide dysfunctional incentives for the employees to let the organization grow beyond what is optimal from an efficiency standpoint. Rank-order or relative performance reward systems, which can be tied in with the organizations own performance-based budgeting system, could provide better incentives for efficiency rather than for undesirable organizational growth.

The NTOs and their managers are faced with some external factors that are more or less uncontrollable for the NTOs. These factors can obscure the relationship between NTOs' behaviors and the outcomes in terms of market performance. Contracting theory suggests that managers under performance-based reward system should be insulated from effects of factors they cannot control for the system to be perceived a fair and have a true motivating effect. Management compensation should thus be based on performance relative to the performance of comparable organizations in the same industry or field, rather than on absolute measures of the organization's performance. We therefore suggest that relative-based performance budgeting system, where the NTO is judged on performance relative to its counterparts in comparable countries, is preferable to absolute-based performance budgeting principles for NTOs.

## 2.6 Summary of the theoretical framework

The theoretical framework provides no 100% definite theoretical conclusions as to what type of governance system, i.e., behavior-based versus outcome-based type of principles, or public versus private ownership and funding arrangements, which is best suited for the NTO context. However, most of the theory reviewed and applied in the NTO context suggests that performance-based budgeting is necessary and beneficial for effective NTO governance. In the following sub-sections we will sum up each body of theory as they relate to the context of NTOs.

## 2.6.1 Theoretical arguments for performance (outcome) – based budgeting principles

*Market orientation* theory describes what market orientation entails (e.g., market intelligence competitor intelligence, and information dissemination, etc.) The theory asserts that organizations should strive to be market oriented, and that market-oriented organizations perform better - rather than *how* to make them behave in a market-oriented way. However, non-profit organizations, like most NTOs are, probably need incentives to become market-oriented. Based on market orientation theory we argue that Market Focus best can be achieved through an outcome- or performance-based budgeting system. *Agency* theory, in its simple form and seen from the principals' angle, tends to prescribe an outcome-based system as well. This is because of the problems with information asymmetry and goal conflict, which can result in moral hazard (less than optimal effort on the part of the NTO) and adverse selection (sub-optimal selection of the NTO as the marketing agent). *Transaction cost* theory prescribes outcome-based principles due to lower monitoring and maladaptation cost incurred under such a regime. The application of *Public choice* theory also leads toward an outcome-based system. The main reason for this is the public nature of most NTOs. NTOs are usually not commercial organizations, and do not face the disciplinary mechanisms from owners' residual claims. Both NTOs and some stakeholders can benefit from slack in NTOs' resources. NTO employees could engage in shirking or divert resources to benefit themselves or certain stakeholders. Socially undesirable budget-maximization behavior and cost inefficiency can be a consequence of that, if left unchecked. Our application of *public economy* theory also suggest outcome-based budgeting, because it is necessary to motivate NTOs for efficient production and at the same time extract the pure rent to some degree. Outcome-based budgeting can serve as means to entice the NTOs to tailor their production to their true cost, and to produce no more or no less than optimal effort (This is also in line with Gunning's discussion of budget- maximizing behavior, see Section 2.3.2). Finally, the review and application of *corporate governance theory* concludes that using a performance-based principle, where both management and staff are evaluated, rewarded, and made accountable based on measurable output, would help align employees', NTOs', and stakeholders' goals, as long as all parties are made dependent on the same outcome. That would allow staff to work for their own self-interests, as well as for NTOs' and stakeholders' interests at the same time. Furthermore, a performance-based budgeting principle can maybe help NTOs get increased funding, particularly from the private sector, which can be beneficial. Performance-based budgeting could also reduce the stakeholders' need and incentives for monitoring NTOs, which can allow the stakeholders to provide NTOs with more Operational Freedom. Operational Freedom can increase NTOs' initiative, participation, and productivity.

Theory also suggests that to offer long-term contracts, i.e., budgets based on longer periods of time, can increase the managers' loyalty to shareholders' interests both short-term and long-term. Corporate governance theory suggests that team- or organizational performance-based incentives are more effective than individual management performance based compensation. Performance-based incentive systems are also preferable to promotion-based reward systems. Finally, the theory suggests that relative performance-based systems are more desirable and feasible than absolute performance-

based systems. We believe relative reward systems are especially important in the NTO context, since NTO managers are exposed to many uncontrollable external factors.

### **2.6.2 Theoretical arguments for behavior (activity) – based budgeting principles**

The a) commercial/profit-maximizing and b) one-principal only point-of-reference assumed in traditional *agency theory* is somewhat useful for our purposes. However, it is not very descriptive of the situation in NTO context. In this context stakeholders are many in number and diverse in character, and they may have conflicting interests. Many clients do not pay for the services directly, and some principal-agent relationships are unclear. This can make goals for NTOs ambiguous, and thereby make NTOs' managements unsure of which goals to prioritize. When there is such conflict of interest and unclear goals, it may be unfair to hold NTOs accountable (through outcome-based budgeting principles) for their governing stakeholders' supposed inability to provide clear directives. Furthermore, the cause and-effect-relationships between NTOs' behavior and market performance are not necessary direct. Many other factors beyond NTOs' control can influence the outcome. In terms of NTO as public agencies, one can expect resistance to performance-measurement from both the agent-NTOs and some NTA stakeholders, which will make well functioning performance-based principles hard to implement in practice.

In addition, there are the considerations regarding the cost of transfer of risk to the agent, outcome measurability, length of relationship, etc. as commented on earlier under the agency theory discussion. All these aspects increase the attractiveness of behavior-based systems to both the controlling stakeholders as principals and the NTOs as agents. An obvious practical problem with more sophisticated kinds of regulation systems, such as outcome-based budgeting, is their complexity. Some resources will have to be consumed by both the governing stakeholders and the NTOs to set up and follow up and adapt to the system. The parties involved may not want to spend those resources and put forward the needed effort, unless the parties perceive that the benefits outweigh the costs of changing the current regime. Given the particularities of the NTO context as discussed above, one can thus expect a dominance of behavior-based systems in practice. We shall see later that is also the case (ref. Table 5.1 in Chapter 5)

### **2.6.3 Theoretical arguments for public vs. private funding and ownership**

A combination of both public and private sector funding and ownership/control may be the best solution. This is because private sector influence may be beneficial for the organizations' Market Focus, their cost-efficiency, their accountability, and reduce tendencies of budget-maximization behavior. It could increase NTOs' competence on tourism and marketing through more industry participation; and increase the industry's commitment and interest in NTO matters.

Public ownership and funding also has some merit. Government influence may be needed to secure that important societal concerns beyond cost-efficiency and profit-maximization

are taken into consideration. Government funding may represent a more stable source of income e.g., due to a more stable budget situation than private businesses' collectively, as well as the governments' ability to commit to long-term contracts. There is also the problem with the common good nature of NTOs' output, along with the private sector funding problem related to that. Stable government funding could aid NTOs' ability to adopt a Long-Term perspective. As Olsen pointed out, some of Niskanen's assumptions from public choice theory, e.g., over-confidence in private sector ownership as disciplinary mechanisms, etc. discrediting government operation can also be questioned. The issue of government vs. private ownership is much debated in the theory we have investigated here, and different authors have conflicting views on this issue.

#### **2.6.4 Overall conclusions from the theory review and application**

There are parts of the theory reviewed and applied that favor an outcome-based system, while other parts leads to behavior-based systems. Some considerations call for government control and funding, while other aspects call for strong private sector presence. Consequently, the theory discussed does not provide us with absolutely distinct, clear-cut recommendations with regards to which type of NTO governance system that would be the most beneficial taking all stakeholders into consideration. However, most of the theory reviewed and applied in the NTO context leads toward recommending the performance/outcome-based principles.

Decisive recommendations in terms of ownership and funding source are not easy to make based on the theory we have reviewed and applied in this chapter. Thus a combined industry/government funding- and ownership scheme might be the best solution.

However, implementation of performance-based budgeting principles may also reduce the role of public versus private ownership.

Appendix 3 shows various conceivable control-principles applicable for NTOs and how these principles relate to the theory discussed in this chapter, including some potential benefits and negative consequences. These principles also constitute the core of the independent variables presented later in this thesis. How these independent variables are operationalized in detail is shown in Table 5.1, and the corresponding dependent variables are shown in Appendix 4.

**Table 2.12**  
**Summary of different areas of reviewed theory and their relevance**  
**to the *independent* and *Dependent* variables**

<b>Theory relevance</b>	<b>Market Orientation</b>	<b>Agency</b>	<b>Public Choice</b>	<b>Public Economy</b>	<b>Corporate Governance</b>
<i>Budgeting principle</i>	* NTO probably needs additional incentives to be market-oriented, since M.O. activities consume extra resources	* Defines the agency-problem. * Discusses pros and cons of behavior- vs. outcome-based contracts.	* Identifies the control problem in bureaus, where market competition lacks as disciplinary mechanism	* Performance contracts in public sector have been unsuccessful due to problems with odd incentives and governments' commitment to the contracts	* States that performance measurement and rewards can align goals of stakeholders and NTO * Discusses the advantages of various performance-based incentives
<i>Funding source</i>	* No link between NTOs' income /budgets and market performance may lead to sponsor orientation rather than M.O.	* Information and influence on the NTO can be bought through a sponsorship role	* Discusses a) differences in demands from taxpayers vs. private sector as NTO financiers * b) budget-maximizing behavior in bureaus	* Performance-based budgeting will transfer some outcome-risk from sponsors to NTO and possibly increase private sector's willingness for NTO funding	* Performance measurement and rewards can increase willingness for private sector funding
<i>Ownership /control</i>	N/A	* Organizational control can be exercised through formal ownership or board membership, reporting procedures etc.	* Public owners might not be as concerned with efficiency as private owners. * Discusses government alternatives for NTO regulation under a market failure situation	* Public ownership is cost-inefficient * Concentrated private ownership might not be beneficial * Public ownership might serve important societal concerns beyond efficiency	* Many stakeholders with many demands make it difficult to agree on specific performance-measures. NTOs might become a procedural agencies
Market Focus	* Defines M.O. * Establishes that M.O. is important for organizational performance	* Dependence on outcome (market performance) will entice NTO to seek market-oriented info.	N/A	N/A	N/A
Long-Term Perspective	* Long-Term Perspective is important for performance, and is tied in with M.O.	* Long-lasting relationships between actors reveal agent behavior and thus reduce need for performance contracts	N/A	* For desirable Long-Term Perspective of the NTO, government funding/and or control could be beneficial for the organization's long-term operational focus.	* Long-term contracts are beneficial for L.T.F. * Intervening and frequent changing of assignments (low O.F.) could make NTO focus on short-term results
Operational Freedom	* Incentives to lobby sponsors or owners for recourses and support rather than to focus on the market	* Performance-/ outcome-based contracts reduce the need to monitor agent	* Deals with organizational control problems of bureaus in terms of effectiveness and efficiently	N/A	* O.F. is important for initiative and participation of the agent NTO

### **3.0 A framework for understanding the market performance of NTOs**

The theoretical framework presented in Chapter 2 leaves us with no 100% absolute directions as to which principles would be most beneficial for NTO governance. Some of the theory implications are relatively clear, while other areas of theory provide more incoherent implications. In this chapter we will consider the multi-sided implications derived from general theory and apply them in the particular NTO context in order to develop the theory framework further. This can be done by the inclusion of some contextual, practical, and political considerations in the theoretical framework. The purpose is to arrive at solutions that are both theoretically sound, practically implementable, and politically viable to the various stakeholders.

Three issues will be discussed in this section:

1. What conditions may promote market goals and facilitate market performance of NTOs?
2. What parties constitute the stakeholders of the NTO?
3. What goals exist for organizations like NTOs?
4. In a practical manner, how can organizations like NTOs be controlled, so that NTOs fulfill the stakeholders' objectives?

#### **3.1 What determines market performance?**

The market performance of the NTO is dependent on a number of factors, some external/exogenous and some internal/endogenous. Some of these factors can be controlled or influenced by the NTOs stakeholders, some by the NTO itself and some are more or less beyond the control of either party.

##### *Exogenous factors*

It is rarely possible to isolate market performance as a pure organizational achievement. The market performance of an NTO has to be estimated rather than measured as stated above. The reason for this is that market performance, e.g., in terms of increase in number of tourists or value of tourism, never will be the accomplishment of the NTO alone, but most likely will depend on a number of exogenous factors. Such factors include political, economic and climatic conditions in addition to a host of other variables as illustrated in Figure 1.1 presented in the introductory chapter in Section 1.3. These factors are of course important, but are not within the main scope of this study. The factors we are interested in are the ones shaded/highlighted in Figure 1.1, because they are the ones the stakeholders can control from a governance perspective.

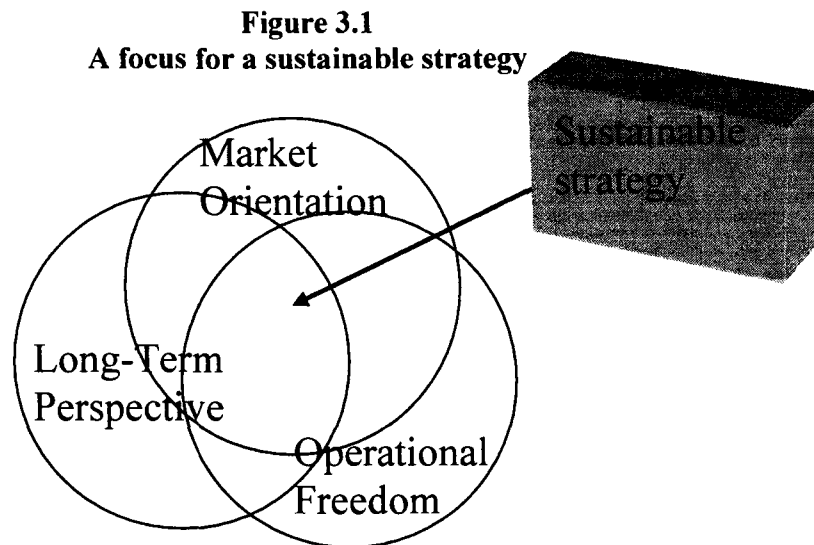
##### *Characteristics of the NTOs' decision-making*

We assume that three characteristics of NTOs' decision making will affect their ability to influence the market positively:

- *Market Focus* – i.e., the degree to which the market gives the premises for NTOs' decisions and activities, e.g., the design of promotional material and campaigns, choice of market segments and positioning of products and travel destinations.
- *Long-Term Perspective* – i.e., the NTOs' ability to make decisions that are optimal in the *long run*, (of course without ignoring short-term activities) and
- *Operational Freedom* – i.e., the degree to which the NTO has the freedom to make decisions without interference from other organizations

Neither of these characteristics are, in isolation, sufficient conditions for good market performance, but we believe that a sustainable strategy will require a combination of the three, i.e., market success requires not only a market focus, but long-term perspective and operational freedom as well.

We believe a sustainable strategy will be in the intersection between Market Focus, Long-Term Perspective and Operational Freedom as illustrated in Figure 3.1:



#### *Organizational make-up and resources*

The three aspects above will reflect the internal organizational make-up with respect to a number of factors as illustrated in the figure:

- human capital
- professional attitudes
- financial resources
- organizational culture

Based on our research we strongly believe that the NTOs vary considerably in terms of the characteristics listed. Human capital varies obviously both quantitatively and qualitatively and economic resources vary from less than a million US\$ per year to more than 100 million. In some NTOs the government receives considerable attention, while others appear much more oriented toward their markets.

To the extent such organizational traits determine the market performance of the NTO through their impact on the way the NTO makes its decisions; an important issue is how the stakeholders can influence these traits. This influence can obviously be achieved directly by taking part in e.g., hiring decisions. However, influence can also be attained through other sources of control.

### *Sources of control*

There are reasons to believe that the nature of organizations and the way they act are partly determined by the following factors:

- on *what basis* are the financial sources provided, i.e., what budgeting principles are in use?
- *who* provides the financial sources?
- *who* owns the organization or in some way exerts control on it

### *Budgeting principle*

The amount of resources devoted to the NTO can be based on the acceptance of activity plans or activities carried out; or tied to organizational performance (i.e., the performance of the tourism industry in term of influx of tourist or economic value of tourism). Alternatively, they can be allocated as a more or less fixed sum from year to year.

In the empirical part of this thesis we have included eight budgeting principles, some of which can be termed mainly performance-based, and some that are mainly activity-based. Some of these principles are currently in use in NTO administrations, while some are interesting potential principles not in use today.

### *Funding source*

It is reasonable that contribution of resources is an important source of power. Organizational control will to a certain extent be exchanged for monetary resources. The character of organizations like NTOs will thus partly reflect who provides its economic resources. To the extent the financing stakeholders differ with respect to how they perceive goals should be prioritized, and perception of reality and cause-effect chains, the funding source should be an important issue.

We have included three alternatives in the empirical part: public funding, funding by the travel and tourism industry, and a combination of the two.

### *Organizational “ownership”*

Who “owns” or controls the organization (i.e., what entity the organization is responsible towards or what entity/coalition is above the organization in line of command) will most likely influence the organization as well. Control of the organization can also be attained through power over appointment of key staff or by board representation, which in turn will influence the decisions made by the organization and the priorities of the NTO.

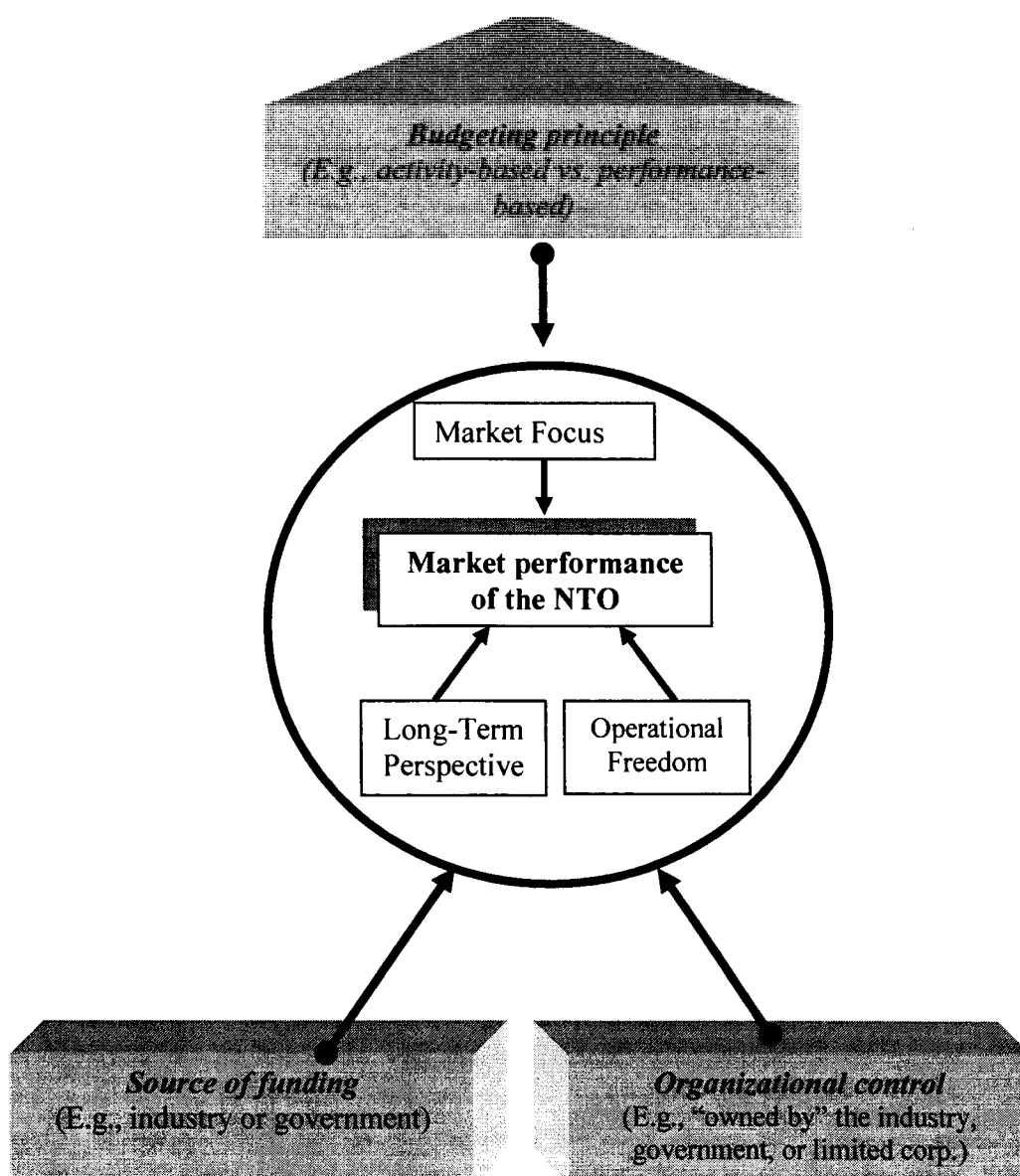


Organizational control is often interconnected with the funding source, but it is conceivable that no direct relationship exist between the two. For instance, some NTOs are completely government funded, but at the same time have strong industry board representation.

*A simplified research model*

The model depicted in Figure 1.1 in Chapter 1 is quite unwieldy and does not lend itself easily to empirical investigation. The simplified version shown in Figure 3.2 contains the shaded parts of the more complete model and provides the conceptual framework for the empirical part of this thesis.

**Figure 3.2**  
**A simplified research model**



## 3.2 Stakeholders, goals, and activities of the NTO

We will continue our contextual analysis by identifying NTOs' stakeholders and discuss the organizations' activities and goals.

### 3.2.1 NTOs' stakeholders

Through efficient and effective use of NTO's resources the domestic tourism industry as a whole can benefit through increased business from incoming tourism. Hence, the performance of an NTO is important for the *tourism sector*. Most businesses in the tourism industry depend on access to both domestic and international customers for the businesses to survive and prosper. NTOs often have a vital function in the process of generating international demand for the industry's products and services. Besides its promoting role, an NTO may also play an important role as a provider of strategic advice, input to product development, strategic market information, tourism industry education and public statistics. This kind of NTO-activity can be of outermost importance to the competitiveness of the domestic tourism industry in international markets.

In addition, the local and national *governments* have an interest in that NTOs' resources are spent in an optimal way. Incoming tourism can help generate tax revenue and influx of foreign currency, as well as supporting the balance-of-payments for a country or region. Thus, the local and national governments will obviously benefit from the prosperity of the tourism industry as well. Clearly *society*, e.g., local and national community and tax-payers, also has a stake in the actions and achievements of the organization. This is because a well-performing NTO-organization can contribute to make the tourism industry profitable, and society in general can harvest the spin-off from that. Tourism can help maintain population employment, contribute to development of infrastructure and public services, and attract foreign and domestic investments. In some countries revenues from tourism comprises a major portion of the GDP, and some countries' economies are heavily dependent on incoming tourism. It is often crucial to such a country that its NTO is well-functioning and well-performing in terms of creating incoming tourism demand.

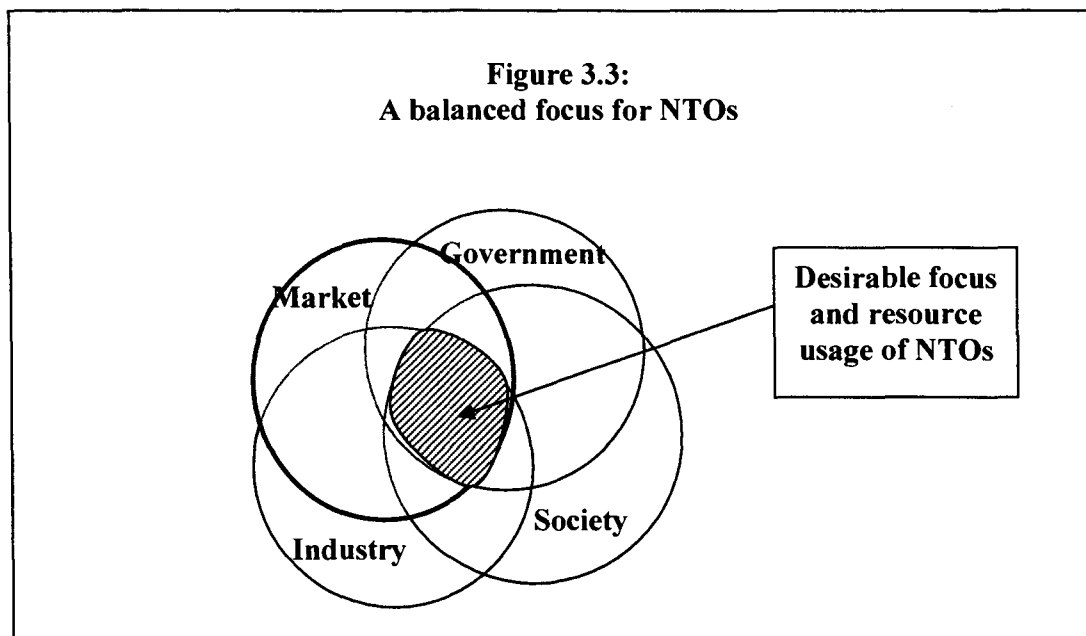
Furthermore, the *international tourism market*, as current and potential visitors to the country, has an interest in receiving the travel assisting services provided by the organization as well. Last, the internal stakeholders, which are the *employees and management* of the NTO, benefit from a well-functioning organization that can provide secure employment and career opportunities.

Clearly, a typical NTO has a number of stakeholders within the organization itself, as well as within and beyond the tourism industry. The diverse make-up of different stakeholders with different interests makes the task of finding an optimal set-up and government of such organizations quite a complex problem to solve. Particularly is this a challenging task if one really wants to safeguards the interests of all the NTOs' stakeholders in a *pareto*-optimal way.

It should then be apparent that in any given country with an NTO in operation there are at least four kinds of external NTO-stakeholders - whose constituents and interests only to some extent overlap:

1. The travel and tourism industry<sup>22</sup>
2. Local and national government
3. Society (non- tourism industries, taxpayers, the environment etc.)
4. The international tourism market (i.e., users of the NTO's tourism services, such as travel advice and information, product information/promotion, product bundling/packaging etc.)

These stakeholder groups may have coinciding interests, as well as conflicting ones. The set-up and governance problem of NTOs revolves around safeguarding the interests of all stakeholders, which may seem impossible. A "mutual interest" alternative appears to be the most appropriate, as shown in Figure 3.3.



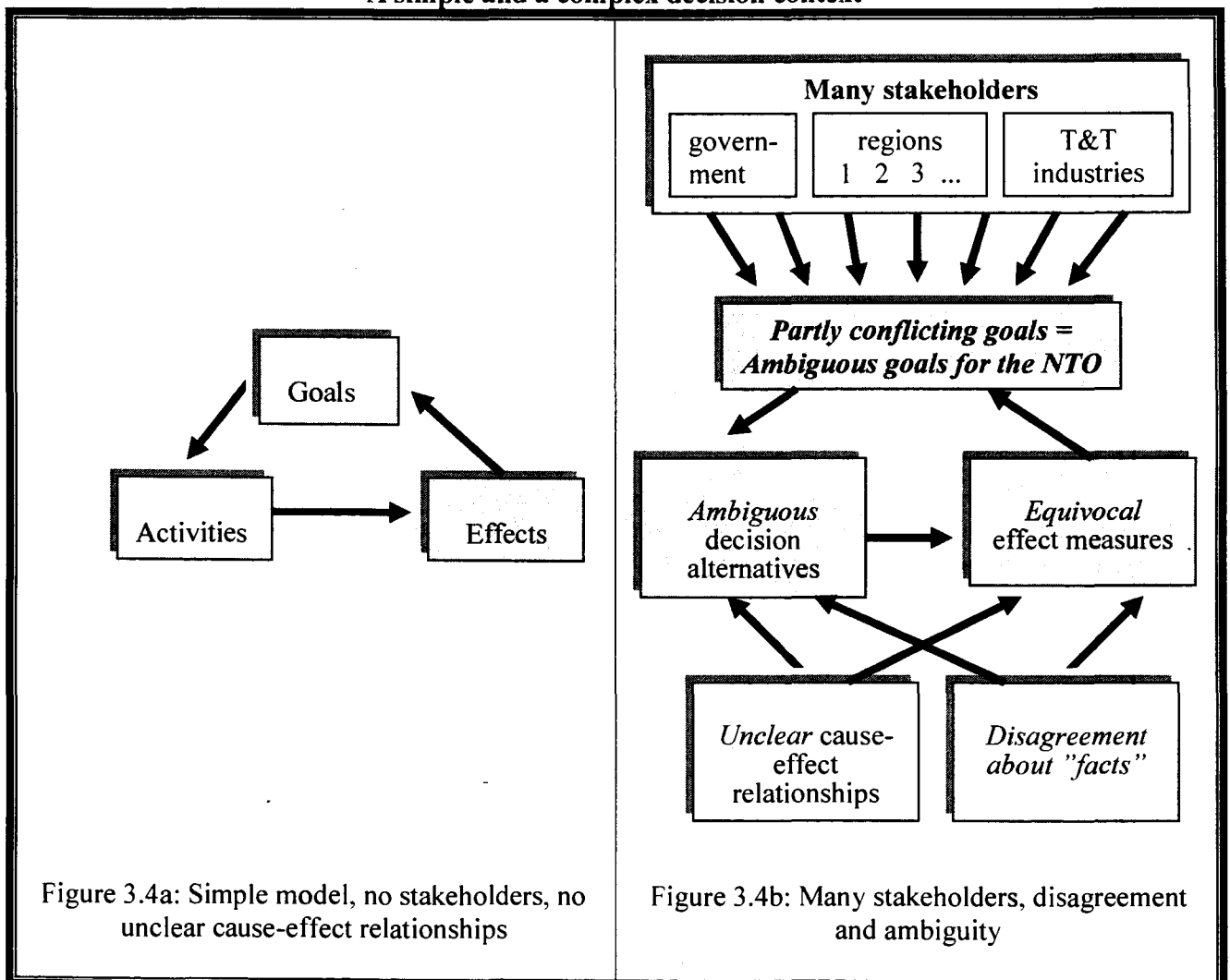
Thus, an important purpose of this study is to determine how NTOs best can be set up and governed in order to serve the interests of all of its stakeholders, and not only selected groups with special interests. Through a *market focus* of the organization - so that the organization spends most of its time, effort and resources working with the market - government, industry and societal interests will also be served, as depicted by the shaded area in Figure 3.3.

<sup>22</sup> "Tourism industry" is termed here as defined by the World Tourism Organization (WTO) 1999; ref. "Tourism Satellite Account (TSA) - The conceptual framework", pp. 6-7.

### 3.2.2 Goals and activities of the NTO

As outlined in Chapter 2 (e.g., sections 2.2.2.1, 2.2.5.3, and 2.3.2) an organization will have some external and internal goals. To achieve these external and internal goals the organization will engage in activities assumed to lead to the fulfillment of the objectives related to these goals. A rational organization will retrospectively evaluate if these activities and strategies in fact had the desired effects (see Figure 3.4a). Based on the appraisal the organization will engage in new activities and continue activities assessed to be successful, as we explained in Section 1.4.1. The simple model depicted in Figure 3.4a assumes that goals are clear, that relevant decision alternatives are known with close to certainty, and decision-outcomes are unambiguous. It also assumes that organizations have the freedom to make decisions quite independently of other organizations and that they have jurisdiction and authority over their resources and actions. Prescriptive theory prompts managers to identify goals and craft strategies to attain these goals, and to accumulate resources and acquire the necessary support to do so.

**Figure 3.4**  
A simple and a complex decision context



For some organizations, and particularly for NTOs, the simple model does not provide a good description. Due to ownership and funding arrangements there are constraints in many organizations autonomy and ability to exercise discretion. Powerful stakeholders may matter more than the potential success of a given action.

For many reasons the way in which goals are related to activities and effects can be quite problematic for NTOs. First of all,

- the NTO has *several stakeholders*
- that may have *partly conflicting* goals and aspirations for the organization (see Figure 3.4b)

Different political institutions at the national level, e.g., ministries of finance, industries, and ministry of labor (see first column in Table 3.1), may perceive different goals for the organization such as the ones listed in the second column in Table 3.1. Different regions and local destinations may have different ideas as to how the advertising budget and alternative destinations should be prioritized to attract tourists. Furthermore, since the tourism sector comprises several industries (transportation, lodging, restaurants, etc) many potential and partly conflicting goals may exist among the stakeholders and result in goals for the NTO that are difficult to re-conciliate.

The ambiguity with respect to goals and decision alternatives is not only a result of antagonistic goals and values among the shareholders, but may also be a consequence of

- disagreement about "facts" and
- unclear cause-effect relationships.

In a tourism setting, different regions or various types of accommodation-providers may have conflicting views on "facts", such as e.g., the quality, attractiveness and the value for money of their offering. Furthermore, conceptual models of *cause-effect* chains may differ or may be unclear. It will always be difficult to assess whether changes in the influx of tourists are due to

- economic trends
- changes in the nature or quality of the tourism product that is provided
- changes in the relative prices
- climatic conditions
- changes in the domestic NTO's activities, or
- actions brought about by foreign NTOs (i.e., competitors).

In addition to the ambiguity imposed on the organization by its external stakeholders, the internal stakeholders, the employees and various departments of the NTO, may perceive cause-effect relationships differently and may have objectives for the organization that may not entirely coincide with those perceived as important by the principals.

**Table 3.1**  
**Examples of areas of ambiguity and conflict among stakeholders**

Stakeholders that may disagree	Areas of disagreement/ambiguity		
	Goals and objectives	"Facts"	Cause-effect chains
<ul style="list-style-type: none"> <li>• <i>Government</i> <ul style="list-style-type: none"> <li>• Ministry of labor</li> <li>• Ministry of finance</li> <li>• Ministry of regional development</li> </ul> </li> <li>• <i>Regions</i></li> <li>• <i>Destinations</i></li> <li>• <i>Tourist industries</i></li> <li>• <i>Trade unions</i></li> <li>• <i>Etc.</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>contribution to</i> <ul style="list-style-type: none"> <li>• <i>balance of payment</i></li> <li>• <i>employment</i></li> <li>• <i>tax revenue</i></li> </ul> </li> <li>• <i>"green tourism"</i></li> <li>• <i>economic value of tourism and regional development</i> <ul style="list-style-type: none"> <li>• <i>region A</i></li> <li>• <i>region B</i></li> <li>• <i>city A</i></li> <li>• <i>city B</i></li> <li>• <i>industry A</i></li> <li>• <i>industry B</i></li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• <i>attractiveness of</i> <ul style="list-style-type: none"> <li>• <i>destination A</i></li> <li>• <i>destination B</i></li> <li>• <i>type of accommodation</i></li> </ul> </li> <li>• <i>market potential for given products</i></li> <li>• <i>attractiveness of given markets and segments</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>the impact on number of tourists of</i> <ul style="list-style-type: none"> <li>• <i>price level</i></li> <li>• <i>various types of campaigns and promotional tools</i></li> <li>• <i>economic trends</i></li> <li>• <i>climatic conditions</i></li> <li>• <i>taxation</i></li> <li>• <i>travel distance and accessibility</i></li> <li>• <i>product quality</i></li> </ul> </li> </ul>

Conflict among stakeholders and ambiguities with respect to goals, "facts" and cause-effect relationships raise many organizational challenges. It is difficult to imagine "correct" solutions, as the "rules of the game" may change as a function of changes in the NTO's constituencies. Consequently, political processes may often to some extent determine the organization's goals and actions. (For an organizational comparison, refer also to the World Health Organization case discussed in Section 2.5.)

### 3.3 Principles for governing NTOs

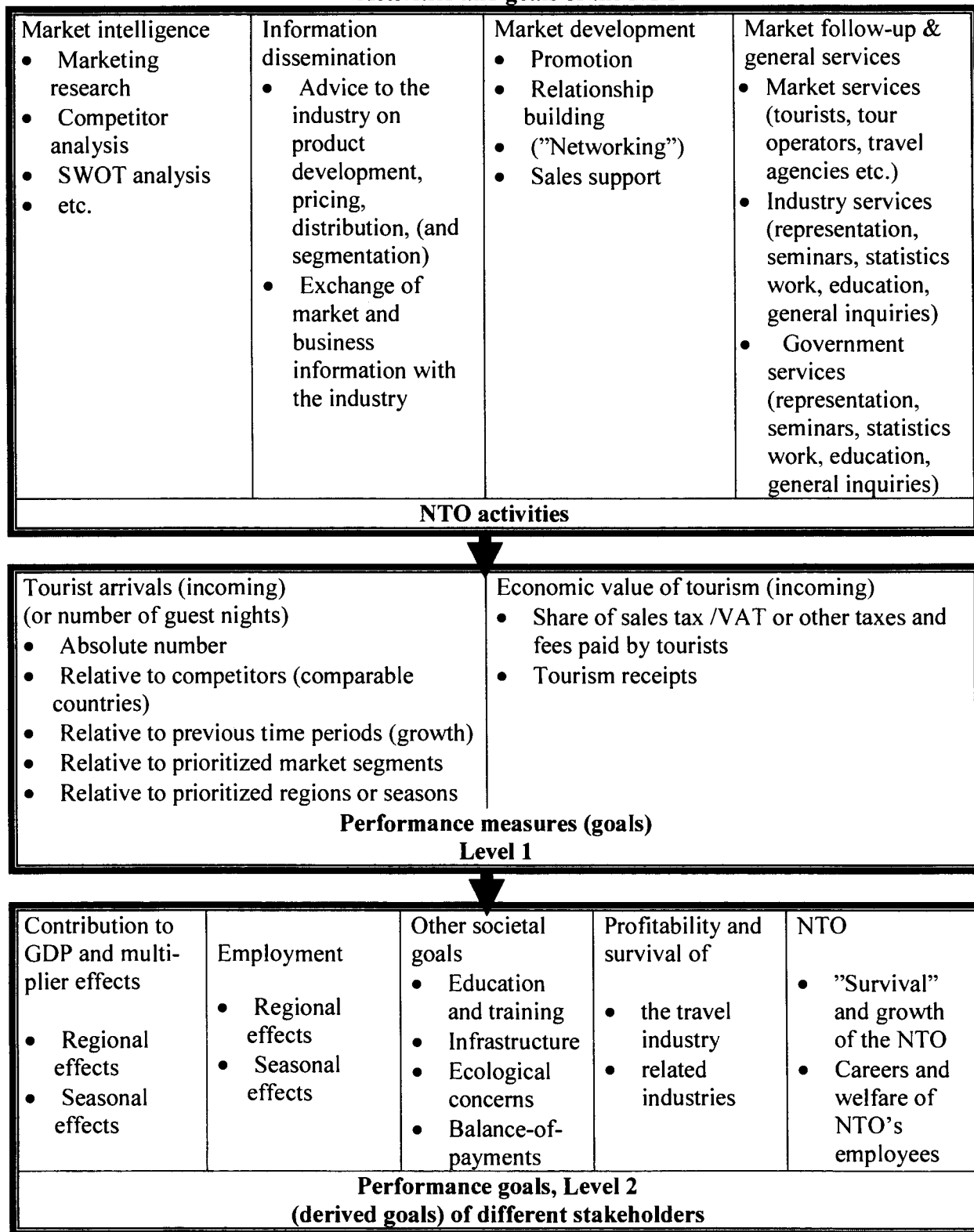
How can stakeholders assure that the organization acts according to their interests? As explained earlier, two fundamentally different types of budgeting principles can be applied that may have different consequences for the organization:

- One can either decide on, or try to influence, *the activities* of the organization;
- or govern the organization *by monitoring the effects of its activities*.

#### 3.3.1 Criteria for evaluating governing alternatives

In Figure 3.5 we have listed goals or performance measures at two levels. At level one we have listed activities that are directly tied to tourism, e.g., the number of incoming tourists and/or their expenditures during the visit. Level two encompasses secondary or indirect effects: Contribution to GDP, employment, profitability, etc. Level-two effects also encompass the direct impact on variables of vital concern to the NTO as an organizational entity. In the ideal and unlikely situation where goals are non-conflicting and cause-effect relationships are known and clear, it does not matter at all what kind of

**Figure 3.5**  
**Activities and goals of the NTO**



governing principle is chosen. Uncertainty of outcomes often tends to make organizations and their people reluctant to take on high risk, particularly when stakes are high, e.g., when there is a chance for substantial negative outcomes. In theory, this will make the stakeholders want to govern the organization on the basis of achieved effects (results) and thereby push the "risk of failure" upon the organization ("It's your fault, you didn't get the job done"). The organization on its side would maybe want to be governed on the basis of activities, and thereby push the "risk of failure" upon the external stakeholders ("It's not our fault, we just followed directions").

A number of activities of NTOs can be decided on or influenced by external stakeholders (see upper part of Figure 3.5). For instance, it could be to decide the nature of and/or amount of money or other resources spent on activities ranging from market intelligence and information dissemination to market development and various types of services (behavior/activity-based budgeting). (See Section 2.2.3 for theory details). A criterion for evaluating the adequacy of an activity-based governing principle should focus on both effectiveness and efficiency.

- To what extent does carrying out activities lead to desirable outcomes?

Control of the NTO through activity-based budgeting can be effective if the execution of the various activities will with reasonable certainty lead to the desired level-one and level-two goals. The stakeholders can then pay the NTO *ex ante* to carry out these activities or reward the NTO *ex post* for the successful completion of these activities.

However, such a procedure requires the governing stakeholders to be well-informed of the cause-and-effect relationships between the activities to be carried out and the goals to be achieved. The stakeholders must also agree amongst themselves and with the NTO about which activities that should be undertaken and to what extent they should be carried out. Furthermore, the stakeholders need to know something about how much money these activities would cost to carry out in order to arrive at reasonable budgets for the NTO. In addition, the stakeholders will have to monitor the NTO's execution of activities and collect information *ex post* in order to assess whether the NTO has done the agreed-upon activities satisfactory. We have already pointed out in Section 2.2 the information problems that can occur due to information asymmetry, such as *moral hazard* and *adverse selection* as well as the transaction costs incurred in the form of *monitoring- and maladaptation costs*. Another profound problem is that there will be stronger incentives for the NTO to focus on the activities (upper part of Figure 3.5) and not the desired results (central and lower part of Figure 3.5). In turn this can give the NTO incentives to maximize the *amount and magnitude of activities* and not the goal-related *outcome of the activities*. Assuming that sane activities are determined by the stakeholders and the NTO, and these are carried out accordingly, activity based budgeting can in some instances be effective. However, such a procedure does not provide incentives for efficiency, as we have pointed out in Section 2.4.3-5.



Another alternative is to govern the organization by measuring and reward its performance against the specified goals and objectives and by allowing the NTO the freedom to decide how to accomplish these goals (performance-based budgeting). (See Section 2.2.4 for theory details). Assuming that e.g., increased employment or economic growth is the ultimate purpose for establishing an NTO, does not imply that such goals also should be the goals by which the NTO's performance is judged. A number of criteria for evaluating the adequacy of a given performance measure can be listed:

- To what extent is the performance measure reflecting the outcome of the NTOs' actions?

Ideally it should be possible to identify the direct impact of the NTO's actions. Effects can, however, at best be estimated – and rarely measured directly. The reason for this is that only a limited amount of the variation in the various performance variables listed in Figure 3.5 are attributable to the actions of the NTO. Changes in employment, for instance, do not only reflect the success of the NTO in attracting more tourists, but can be attributed to employment procedures and wage levels as well as to various demand and economic factors beyond the control of the organization. However, this situation is not unique, neither for the tourism sector nor the NTO itself. The success of most companies in the tourism sector as well as in other industries is not solely attributable to the company itself, but is the outcome of a number of circumstances and exogenous factors. A minimum requirement is, however, that the performance measure (at least partially) reflects the "true" performance of the NTO. We believe this particularly will be the case for the level-one performance measures listed in Figure 3.5. By choosing the most beneficial market segments, making professional decisions with respect to marketing and promotional activities and disseminate market relevant information to decision makers in the tourism sector, the NTO should at least partly influence performance variables like tourist arrivals and measures of the economic value of tourism. Performance variables at level two will be more indirectly related to the NTO's decisions than the ones at level 1.

- To what extent are the performance measures related to ultimate goals?

If we assume that the various economic goals listed at level two are legitimate goals and reasons for marketing the country as a tourist destination the question is how closely these goals are related to the level one measures. It seems plausible to assume that although other factors (such as relative prices, exchange rates and managerial practices in the tourism sector) will obscure the relationship between level-one and level-two variables, the relationship will be reasonably strong.

More problematic are the relationships between e.g., tourism arrivals and variables that are relevant from an ecological or sustainable tourism perspective. A performance measure tied to tourism expenditures/receipts rather than tourist arrivals could motivate the NTO to focus on quality tourism rather than quantity tourism. It could entice the NTO to try to market its destination(s) to a more upscale market that is usually better educated, more ecologically and culturally concerned, and fewer (i.e., fewer visitors needed to

generate the desired level of tourism receipts). One could also introduce a take-care-of responsibility (as we discussed in Section 2.4.5) as part of the performance-measure(s).

- To what extent can performance measures be directly tied to "success criteria" and internal goals of the NTO?

It is desirable that performance measures are strongly related to internal goals and success criteria for the NTO. This can be obtained through some incentive mechanism that ties e.g., influx of tourists or tourism derived income to the budget of the NTO so that the resources available for the NTO will be correlated with the performance variable the organization is assumed to influence. Through this incentive mechanism the NTO will to some extent be "self-monitoring" and thereby make it less required for external stakeholders to monitor and control the organization. Market related performance measures should in a sense promote markets and customers to become the NTO's most important stakeholder.

A third way of controlling the NTO is through funding and a fourth way through ownership. Any governing stakeholder can in theory exert decision power or influence through funding (financial authority) and/or ownership (formal authority) of the NTO. We believe that this kind of control will be more important under an activity-based budgeting regime than under a performance-based one. This is because the stakeholder will want to influence the determination of goals and activities and monitor the NTO under an activity-based system, while this is not necessary to the same extent under a performance-based system.

- To what extent will the funding source influence the NTO's priorities, activities and goals?

It is reasonable to believe that an existing or potential financial sponsor would have certain motives connected to their contribution of funds to the NTO's budgets. One can probably expect that private sector or industry sponsors would be even more concerned with efficiency and effectiveness "getting their monies worth" with their sponsorship of the NTO than the government would be. This is because the industry will have to spend their own corporate funds while the government spends taxpayers' money. The industry faces market competition and thereby an inherent pressure for market performance (effectiveness) and conserve scarce resources (efficiency). The businesses in the industry are for the most part comprised of profit-maximizing organizations, and could be expected to focus on goals related to market performance that can be enhanced e.g., through Market Focus. The benefits of the NTO's activities will be allocated directly to the businesses in the industry. That would give the businesses strong incentives to push on the NTO to come up with good market results. On the other hand, public funds are not first and foremost dedicated to maximizing profits, but probably more geared towards attaining political and societal goals. Because one is dealing with public funds with political and societal concerns attached, there may be more restrictions and procedures related to how the NTO can spend such money, limiting the organization's operational freedom. Furthermore, the benefits of NTO's activities will not be allocated to the individuals or entities providing the public funds (in theory - and then disregarding

shirking) but the industry, government, and society stakeholders as whole. There is then a lesser incentive to push for performance than for private sector sponsors. However, given that the government is fairly stable in their priorities and policies, government may be able and willing to adapt a more long-term perspective in funding matters than the industry, which is facing a bottom line requirement each year.

The ownership of the organization or board of directors' control would be reflected upon the people (and their priorities and ways of working) who can exert formal control of the NTO. It is then safe to assume that this will influence how they will try to make the NTO operate. It is then relevant to consider

- to what extent will the ownership/control influence the NTO's priorities, activities and goals?

It is reasonable to believe that industry stakeholders would have more professional competence on e.g., the industry and marketing than government bureaucrats. Industry representatives could also be expected to have a more business-oriented attitude than government representatives. The background, whether it is industry or government, of the various board members can affect their ability and willingness to try to influence the NTO to become more business and market-oriented.

It is also conceivable that an NTO controlled by the government would be more bureaucratic, procedural and less flexible than an industry led organization. On the other hand the industry representatives could maybe be expected to push more for their own interests and less for the whole industry and society, whereas government representatives would focus more on collective benefits. How the board is put together probably have an impact on the NTO's operational freedom in terms of pressures to focus on special interests.

### 3.3.2 Theory and context-based recommendations for choice of funding principle

It seems reasonable that performance-based control is in most concerns preferable to activity-based control of the NTO – however difficult it might be to find adequate performance measures that also will be satisfactory to the various stakeholders. Performance-based control mechanisms have several advantages, albeit a few disadvantages, compared to activity-based mechanisms:

1. Performance-based control will make the NTO accountable for its decisions and the outcome of its actions.

Since the NTO should possess the most adequate expertise in international tourism marketing, it seems natural that the NTO should be the most competent organizational entity in translating goals into actions. Performance-based control should motivate the NTO to seek success and avoid failure because

2. Performance-based control will make it simpler for the stakeholders to monitor the performance of the NTO, and at the same time reduce the need for the NTO to engage in justification-for-existence-efforts.

Activity-based control mechanisms require considerable effort – particularly if the various stakeholders are well involved in the planning processes. For instance, the stakeholders and the NTO will have to agree on clear and unambiguous goals and specify activities to be performed.

Both stakeholders and the NTO will incur higher transaction costs, such as monitoring and mal-adaptation cost, under an activity-based regime.

In the NTO context the agency problem related to information asymmetry and adverse selection is particularly pronounced. Performance-based control could align the goals of both stakeholders and the NTO because they all depend on the same outcome.

3. Performance-based control can reduce the agency problem in the NTO context.

Due to its private information advantage the NTO may use this information to negotiate budgets higher than socially desirable and shirk on slack resources. This is a lot easier to achieve under an activity-based system in a non-commercial context, where NTO can be able to exaggerate its cost-of-operation estimate in budget negotiations.

4. Performance-based control will make it harder for the NTO to resort to budget-maximizing behavior.

Thus, performance-based control should make the NTO focus on cost-efficiency and market performance rather than budget-maximizing lobbying effort.

Performance-based control will reduce the need for stakeholders to supervise the NTO, and allow the stakeholders to relax their intervention in NTOs operational matters.

5. Performance-based control allows considerable autonomy to the NTO.

This may be particularly important when conditions change that call for quick adjustments. Autonomy will reduce the need for the organization to justify its actions and to seek acceptance and approval of its decisions. It could also increase the NTOs participation and motivate for innovative behavior because NTO would not have to be worried about being constantly overruled by its stakeholders.

In order to be successful under a performance-based system that is dependent on performance, the NTO will need to acquire competent staff that can improve market results. It will, for instance, give the NTO stronger incentives to hire skilled marketers rather than skilled lobbyists.

6. Performance-based control will motivate and require the NTO to acquire necessary expertise.

In an activity-based system, the NTA<sup>23</sup> or other dominant stakeholder-entity will have to build sufficient competence to define sensible activities and goals. This is in fact paradoxical to the establishment of an NTO in the first place, since the main reason for establishing an NTO is that the organization has unique competence to market the nation as a tourist destination. In a performance based control regime it is the NTO's responsibility *and motivation* to acquire the human resources needed for goal fulfillment.

One of the probable reasons why many NTOs under activity-based systems have not garnered more regular private sector budget funding is that a lack of accountability has widened the gap among payments, promises and performance. Performance-based budgeting principles can help close this gap.

7. Performance-based control could generate more private sector funding.

Due to the common goods-problem in the NTO context it is hard to generate sufficient private sector funding. Performance-based control cannot let alone rid us with the common goods problem entirely. However, it could increase the private sector's willingness to contribute funds, since it introduces accountability on the part of the NTO, and the NTO "gets what it deserves" in the eyes of the private sector. It also reduces the private sectors payment risk (ref. Section 2.4.4).

**Thus, the theory reviewed and special considerations in the NTO context lead us to conclude that *performance-based principles* (i.e., Principles P1, P2, P7 and P8) should be beneficial for both the NTO's Market Focus and Operational Freedom.**

However, there are also some reasons to include a non-performance-based component in the budgetary mechanism. One could argue that organizations like NTOs are particularly vulnerable to fluctuations in budgets, or other things that are hampering NTOs' ability and motivation to adapt a Long-Term Perspective. The nature of the performance-based budgets is so that the NTO could experience fluctuations in the budgets, sometimes partially due to factors beyond their control (e.g., war and terrorism, recession, currency rates etc.). Besides the motivational value of performance based budgets it could be beneficial for the NTO to have at least some part of the budget relatively fixed. In that way it would be easier to commit to long-term engagements.

1. A fixed amount as part of the budget would help planning and implementation of long-term engagements.

We will make a case later in Chapter 5 and Appendix 7 that long-term operation could in some instances be attained also under performance-based principles, but we believe that a

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<sup>23</sup> NTA= National Tourist Authority, the government body responsible for tourism matters. Can often, for instance, be an integral part of the Ministry of Transport, Trade, Culture etc, in a given country.

fixed component type of budgeting principle can function as a safety-net needed to motivate the NTO for investments in long-term activities.

**Thus, the theory reviewed and special considerations in the NTO context lead us to conclude that *non-performance-based component* (particularly Principle P5) should be beneficial for the NTO's Long-Term Perspective.**

### 3.3.3 Theory and context-based recommendations for choice of funding source

We will see later from the survey on current practices included in Chapter 5 that government funding and ownership/control is the dominating governance form today. However, we believe that increased industry participation in funding of the NTO will be beneficial for the performance of the NTO.

1. Industry participation could put additional and beneficial efficiency and effectiveness pressures on the NTO.

Monies stemming from private sector funding would probably have stronger demands in terms of market results and reasonable return on investments attached to them than taxpayer's funds would. That would put more pressure on the NTO to perform well. It could in turn entice the NTO to become more market-focused, since that would increase the chances of being able to perform better in the marketplace.

2. Pure government funding could make the NTO resort to budget-maximizing behavior.

We have already discussed the tendency of bureaus to resort to budget-maximizing behavior (ref. Section 2.3.2). A government-funded type of NTO could maybe be anticipated to spend some amount of effort and resources on such counter-productive behavior, diverting the NTO from a market focus. Industry participation in funding matters to could possibly reduce this propensity.

**Thus, the theory reviewed and special considerations in the NTO context lead us to conclude that *industry* participation in funding (i.e., Principles P10, and possibly P11) should be beneficial for the NTO's Market Focus.**

However, there are also some important reasons why we believe the government should continue its involvement in funding of the NTO's budget.

1. Government funding can secure a more stable and long-term source of funds.

Given that the government is committed to work seriously with tourism, and does not simply cuts budgets dedicated for NTO purposes arbitrarily from one year to another, the government can contribute to help NTO retain a Long-Term Perspective. The government is not as vulnerable to fluctuations in revenue/income as the private sector in one single industry. Normally, the government should have the "financial muscle" to be

able to commit to long-term engagements in NTO matters. Pure private sector financing may not be as stable as a source of funds.

2. The government “can afford” to have a more Long-Term Perspective in NTO matters.

Related is the notion that the government is not that dependent on immediate payback in investments in NTO operation as businesses in the private sector. Commercial actors may be more dependent and focused on short-term engagements and more quick return on investments and market results. One indication of this situation is that private funding often comes in the form of financing of specific projects with limited time span, rather than long term commitments to the general core budget of the NTO (ref. Section 5.2).

3. Government contribution of funding is “fair” from a societal perspective.

We have also pointed out in Section 3.1 that there are many stakeholder beneficiaries beyond the travel and tourism industry itself. Many different stakeholders, including the public sector, are beneficiaries of incoming tourism. Since tourism often generates substantial benefits of societal value, it is only fair that government contributes to NTO operation. At least some portion of public funding may be necessary to avoid a situation where the businesses in the tourism industry refuses to contribute because they would feel it unfair that they would have to pick up the entire bill for NTO’s operation, as long as tourism benefits other stakeholders beyond the tourism industry. A focus on societal concerns also requires a long term-perspective in funding policies.

**Thus, the theory reviewed and special considerations in the NTO context lead us to conclude that *government* contribution to funding (i.e., Principle P9, and probably P11) should be beneficial, particularly for the NTO’s Long-Term Perspective.**

We have discussed the special nature of generic international tourism marketing in relation to the common goods-problem. Thus one can make a case that

1. Government funding could be necessary to secure sufficient financing of NTO’s budget.

As pointed out there are (short-term) incentives for industry actors to free-ride on the benefits of NTO’s operation. This makes it difficult to obtain stable financing from the private sector. An NTO that is under-financed will also face serious constraints on its operational freedom, and may not be able to carry through activities and efforts needed to satisfy a professionally sound market strategy.

2. Government funding could be necessary to avoid an over-focus on private interests.

Moreover, an NTO solely dependent on the industry to provide it with necessary funding could be forced to accept projects or engagements that favors special interest in the industry and that is not in line with its overall strategy. The NTO could also be subject to

undesirable pressure from special groups with private interest, or large commercial actors that want to support their agenda on the expense of smaller stakeholders. It may force the NTO to spend too many resources on securing funds from the private sector, and lead the NTO towards an industry or product focus rather than a market focus. That would probably reduce NTO's Operational Freedom.

3. Government participation in can help secure funding for efforts directed at societal concerns beyond the profit-maximizing interest of the industry.

Although this is disputed by some scholars (e.g., Shleifer and Vishny, 1997), government participation can help secure that important societal concerns beyond private profit-maximization are considered, and that the interests of all stakeholders are safeguarded. Along with the common goods-problem, this is probably one of the most important reasons why government is still so much involved in NTO matters worldwide.

**Thus, the theory reviewed and special considerations in the NTO context lead us to conclude that *government* contribution to funding (i.e., Principle P9 and possibly P11) should be beneficial, particularly for the NTO's Operational Freedom**

### 3.3.4 Theory and context-based recommendations for choice of ownership principle

Many scholars justifiably argue that private operation is more resource-efficient than public operation. The industry is operating in a competitive environment, and business managers are used to face efficiency and effectiveness constraints on a day-to day basis. More industry participation in ownership/control would bring more business executives into the NTOs' boards, and these managers could be expected to bring their business-oriented attitude with them. Under pure government operation these beneficial demands and influences on the NTO are probably not so pronounced, since the board would be dominated by bureaucrats or ex-bureaucrats not that used to think in terms of efficiency, effectiveness and market performance.

1. Industry ownership participation could increase the degree of professionalism in the NTO.

More industry representation in NTO's boards could help the NTO to become more professional as a marketing organization. Industry representatives could be expected to possess more expertise in e.g., marketing, corporate strategy, finance etc. than bureaucrats.

2. Industry ownership participation could increase the degree of commitment and interest in NTO-matters.

The legitimacy problem stemming from the odd (but still common) situation where the NTO is for the most part controlled by the government, and at the same time set to do marketing tasks on behalf of an industry that is only to a limited degree involved in its operation, could be somewhat reduced by assuring more industry ownership



participation. With sole government ownership/control of the NTO, the businesses in the industry may feel detached and somewhat uninterested in what the NTO is doing. More industry participation can probably increase the likelihood that the industry will be more interested to co-work with the NTO, and thus support and adhere to national strategies for tourism marketing developed and implemented by the NTO. That could give the NTO room to focus on its market-oriented tasks rather than to spend resources on legitimacy-related activities directed at the industry.

**Thus, the theory reviewed and special considerations in the NTO context lead us to conclude that industry ownership/control (i.e., Principles P12 and possibly P14) should be beneficial for the NTO's Market Focus.**

In terms of Operational Freedom, government ownership/control can make the NTO less susceptible to pressure to do what the private sector wants.

1. Government ownership/control could shield the NTO from undesirable pressure from powerful industry stakeholders.

We have discussed in Section 2.4.1 the danger of concentrated private ownership. Large private firms with large investors might pressure the NTO to under-provide quality and otherwise shortchange the NTO's other smaller stakeholders because of their potential single-minded focus on special interests or short-term profits. Such private motives could prompt industry owners to intervene in NTO's operation and put undue restrictions on NTO's Operational Freedom. Government ownership could help secure that all stakeholders are treated equally and that societal interest is taken into concern. There is, however, some controversy about this in the privatization debate, as mentioned earlier.

**Thus, the theory reviewed and special considerations in the NTO context lead us to conclude that government ownership/control (i.e., Principle P13) should be beneficial for the NTO's and Operational Freedom.**

Considering Long-Term Perspective it is more difficult to come to any clear conclusions in terms of preferable ownership/control. On one hand one could argue that the industry would constitute a more short-term oriented owner, since the tourism industry is often more focused on short-term profits than the government as an owner would be. On the other hand, government coalitions (in democratic countries such as the OECD members in this study) do change from time to time and from one election term to another. Government policies and priorities also change accordingly, which could make the NTO have to deal with frequently changing assignments and owner priorities. Neither of these situations could be considered beneficial for the NTO's Long-Term Perspective. We therefore have no decisive conclusions on this issue based on the theory reviewed and special considerations in the NTO context.

## 4.0 Methodology

The following section explains the choice of research method of this thesis and how the empirical part was carried out.

### 4.1 Research method and data collection

The empirical research method we have used is an “experimental laboratory approach” with controlled focus groups, using a scenario technique derived from conjoint analysis design. The technique uses descriptions of the NTOs in terms of the 3 categories of principles (*budgeting principle*, *funding source*, and *organizational ownership/control* as independent variables) systematically combined into scenarios. The “experiment” involves having all the proposed scenarios evaluated in terms of the expected consequences by practitioner respondents from different cultural and professional backgrounds within the OECD community. The data is then compared with current practices and theory recommendations. The said consequences were operationalized in a questionnaire in terms of estimating the effect on the organization’s Market Focus, Long-Term Perspective and Operational Freedom, comprising the dependent variables. Thus the research design entails a measurement and analysis of the relationship between the principles (independent variables) and the expected effects (dependent variables). The principles’ applicability for NTO governance were evaluated by international key-informants with backgrounds from both NTOs and involved stakeholder groups, i.e., government and industry entities along with some independent informants representing the society-stakeholders. Because many of the respondents had prior experience with several of the principles, and generally possessed a thorough understanding of the workings of “real world” NTO contexts, we found these respondents capable of making qualified judgments of the expected consequences of the scenarios. This was done for both the already implemented principles and the alternative suggested principles not yet in use. As mentioned earlier, pre-existing theory from research literature is not, in isolation, sufficient to provide us with such qualified judgments. This was the rationale for the chosen research design shown in Figure 2.1, and the approach to the empirical part of this study as described next.

The main goal of the present study was to assess the perceived consequences of different potential arrangements for financing and controlling NTO's. Consequently, we were not searching for one optimal arrangement, but were more interested in the perceived consequences of different arrangements from the perspectives of the NTA, NTO and the travel industry, (and in a few cases, the society). A heterogeneous make-up of the respondent groups, representing various stakeholder interests, was necessary to safeguard that the interest of *overall* stakeholders were reflected in the evaluation of the principles (ref. Figure 3.1). Furthermore, the theory review and contextual framework suggest several interesting potential principles that are not in use in NTO administrations today. Thus, we were not only concerned with arrangements currently in use, but also with several potential arrangements that are not in use today. These arrangements were included to provide a more complete assessment of potential alternative financing and

control arrangements, instead of confining the evaluation to existing arrangements with the danger of leaving out promising candidates.

## 4.2 Data sample

The effect of different arrangements with regard to budgeting principles, financial source and organizational control was assessed through 2 sets of group interviews conducted a) among 14 groups of practitioners in different OECD-countries and, b) among a group of theory experts with experience from different relevant areas of theory. In this section we will present the data samples and the data collection procedures.

### 4.2.1 Practitioners' sample

The practitioners' data collection was based on a convenience sample including OECD-countries that agreed to participate. Agreement and assistance from the involved tourism administrations were necessary to recruit the desired group make-up representing stakeholders and NTOs. However, despite the use of a convenience sample, we have reason to believe that the respondents are representative of individuals in the real world setting of interest. We have purposely sampled individuals who vary on important dimensions (i.e., stakeholder type and cultural background) that characterize the members of the target population, as suggested by Calder, Phillips and Tybout (1981). The group interviews and data collection procedures were conducted in the following countries in the order as shown:

1. Norway
2. Sweden
3. Denmark
4. UK (British Tourist Authority)
5. The Czech Republic
6. Slovakia
7. Austria
8. Luxembourg
9. Spain
10. Portugal
11. South Korea
12. Japan
13. Canada
14. Finland

Three to eight persons representing the government (NTA), the NTO, and in most instances, the travel industry took part in the interviews<sup>24</sup>. The interviews were conducted between June and September of 1999. With the exception of the UK and South Korea, where only one person was responsible for the interviews, a team of two researchers were conducting the interviews.

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<sup>24</sup> In a few countries people from research institutes and consultants participated as well, presumably representing neutral stakeholders.

The research design was pre-tested on 1) a group Ph.D. students at The Norwegian School of Economics and Business Administration, and 2) a group of executives from two local Norwegian tourism organizations.

#### 4.2.2 Theory experts' sample

The theory presented in Chapter 2 is necessarily of a more qualitative character than the data from the practitioners' scenario evaluations in our international sample. Thus, it is difficult to compare the two sources of information directly. It was necessary to "reduce and focus" the rather comprehensive qualitative data from the theory discussion into a more compact, quantitative form more comparable with the data derived from the practitioners' evaluations. A way to handle this problem is to have a group of theory experts "quantify" the relevant theory through use of the same series of scenario evaluations as the practitioners evaluated. In this way we could investigate any discrepancies between theorists' and practitioners' views on how NTOs best could be organized and governed in terms of the principles we are interested in. In other words, we were concerned about determining if the way the practitioners think and reason about the issues at hand is congruent with theoretical knowledge as represented by the judgment of theory experts. This procedure is meant to make the two types of data (research-based theory versus practitioners' espoused theories and theories-in-use) far more comparable, since the data would then be in the same format.

Furthermore, there is some degree of inconclusiveness in certain areas within the theoretical framework in terms of recommendations about what principles should be applied for NTO governance. Thus, the quantitative data from the theory experts' evaluations was meant to be a supplement to the qualitative information from the theory review in Chapter 2. We wanted to check the concordance between the literature theory recommendations and the results from the theory experts' scenario evaluations. A relative match between the two would contribute to validate the theory side of the study. In areas where the theory recommendations are somewhat inconclusive, the results from the theory experts' scenario evaluations can be used to arrive at more decisive recommendations from the theory side of the study.

Therefore, we asked a panel consisting of theory experts<sup>25</sup> to do the same procedure as the practitioners did in the international sample as explained in the next section. The results of scenario evaluations made by the practitioners and the theorists are presented, analyzed and compared in Chapter 5.

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<sup>25</sup> The panel was made up of academic personnel (professors, assistant professors and researchers) from *the Norwegian School of Economics and Business Administration* and the *Foundation for Research in Economics and Business Administration*. The group had six members with expertise from different areas of theory relevant for the issues at hand, and thus representing the theory areas discussed in the theory chapter of this thesis (e.g., marketing, organizational sciences, agency theory, public choice, public economy theory etc.).

## 4.3 Data collection

In the following section we describe the data collection procedure, the scenario design, and some advantages of using this approach.

### 4.3.1 Procedure

The following procedure was used for the focus groups and scenario evaluations:

1. A brief introduction to the project was presented to the participants.
2. The second stage included a presentation of the various principles for budgeting, funding sources, and ownership/control arrangements. The participants in the practitioners' groups were then asked to compare these principles with the current practice for their own country. The group members collectively participated in this process in each country.
3. Then the groups were introduced to 3-4 scenarios containing combinations of budgeting principles, funding source and ownership arrangements to familiarize the group with the procedure.
4. Finally, group members individually evaluated the likely consequences of 3-7 scenarios each so that every national group in total evaluated a set of 22 scenarios<sup>26</sup>.

The purpose of stages 1 through 3 was to familiarize the group members with the research design and data collection procedure. Furthermore, stage 2 provided useful information for comparison of the different arrangements found in the participating countries (practitioners' sample only). Stages 1 through 3 in the practitioners' sample was videotaped for further analysis of any verbal statements, and contextual information that surfaced during the presentation and the group discussion. Stage 4 was important to obtain a systematic comparison of different potential arrangements, including principles not currently in use in any participating countries.

Each of the 22 scenarios consisted of:

- a) one budgeting principle (out of 8 principles in total)
  - b) one source of funding (out of 3 possible sources)
  - c) and one form of organizational control (out of 3 possible forms)
- (See Table 5.1 for a list of the independent variables (principles))

The scenarios were developed according to a factorial design similar to that used in Conjoint-analysis. Conjoint-analysis is a method used to estimate how preferences (or *utility*) for alternative unique *combinations of attributes* (here "scenarios") are determined by the partial preference for the different *attributes* (here "principles"). By presenting the respondents various alternatives that systematically vary on the attributes thought to have an impact on the preferences, it is possible to get an estimate of how each attribute contributes to the overall preference (or utility) of the alternative. In our case, the respondents are asked to evaluate alternatives in the form of so-called "scenarios" that

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<sup>26</sup> An explanation of the rationale for the choice of this number of scenarios (22) is given on the following page.

systematically varied with respect to budgeting principle, funding source, and ownership/control of the NTO. Conjoint computer software was used to arrive at the optimal number of scenarios given the combination of 8 x 3 x 3 independent variables. The computer software reduced the number of (potential) scenarios down to 24, which was the optimal number computed using the conjoint logarithm. Two scenarios had to be deleted from the set, since they constituted unrealistic scenarios in practice (e.g., Budgeting principle = taxation of visitors, NTO funded by the industry, and NTO owned/controlled by the government). Each of the remaining 22 scenarios presented to the groups were then scored on the basis of 18 different evaluation items representing the dependent variables. Any one of these scenarios was evaluated for its perceived impact on NTO's Market Focus, Long-Term Perspective, and Operational Freedom. (See also Appendix 3 for the item list, factor analysis and interview guide/questionnaire; and a sample of the scenarios in Appendix 4). Four of the items were later deleted from the final analysis based on the factor analysis, which resulted in 14 items used for the analysis in the end.

In a traditional conjoint-analysis design each individual would have had to evaluate all 22 scenarios. In our research design, this would have meant that each respondent would have had to score the same 18 items 22 times during one session, resulting in 396 judgments (22 scenarios x 18 items each) altogether. This would be way beyond reasonable time and work load capacity limits of the respondents. Instead, the 22 different scenarios were distributed evenly among the respondents in the national groups. Any one national group consisting of 3-7 respondents each would then equal "one individual" in a traditional conjoint-analysis design. Thus, each set of scenarios consisting of 22 scenarios was evaluated two times by the theory expert panel and 14 times altogether by the country groups combined. This resulted in 44 cases (2 x 22) for the theory expert group and 308 cases (22 x 14) for the national groups combined. Among the practitioners' evaluations only 304 cases were kept for analysis<sup>27</sup>. This meant that each of the 8 *budgeting principles* were then evaluated 6-4 times by theory respondents combined and 42 - 27 times by the practitioners combined, depending on the make-up of the scenario set. The three *funding source* and three *ownership* principles were evaluated 18 - 12 times each by the theory experts combined and 125 - 83 times by the practitioners combined.

Following the scenario evaluation session, a "debriefing" was conducted where the group members were asked to express their views on the research design and procedure. The purpose was to elicit any qualitative additional information that may not have been captured by the quantitative scenario design, and to discover any possible misunderstandings or problems that could help explain any odd responses in the scenario evaluations.

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<sup>27</sup> 4 scenarios evaluated by one single respondent were deleted from further analysis because this individual was deemed "careless respondent" (constant mid-scale (score 4) responses on all 18 items on all 4 scenarios he had been allocated).

#### 4.4.2 Avoidance of strategic evaluations

Apart from the technical advantages the scenario design offers - it was also chosen for tactical reasons. The results from this study, as they were also reported to the OECD Tourism Committee, could potentially prompt NTO administrations to change current practice. Particularly in the case of practitioners' evaluations of principles, one could foresee that some of the respondents would have incentives to evaluate principles strategically according to self-interest, rather than to evaluate a principle as to its potential merits for NTOs' operation. For instance, a stakeholder respondent interested in preserving the *status quo*, and thereby maintaining power, influence or resources, could have incentives to evaluate a typical status quo scenario or principle more positively than that principle "deserves" from an objective general stakeholder's point of view. That is, to systematically over-score a given "favorable" (for the respondent) principle or under-score principles that would change status quo if implemented.

In the scenario design we have used, the respondent is not asked to state whether he or she likes a given scenario or not, or to rate scenarios according to own preference. The respondent is "forced" to evaluate the likely consequences of a given scenario on specific items thought to be important for NTO's performance. If a respondent were to evaluate strategically purely according to self-interest, he or she would have to intentionally and systematically misrepresent any given scenario on a number of different items. We firmly believe that this is more difficult to do in our set-up than if the respondent were to simply rank scenarios according to own preference, or asked directly what kind of system they prefer.

In terms of a potential propensity to evaluate scenarios strategically, our theoretical experts are not really stakeholders in NTO matters, and should have few incentives to make any intentional misrepresentations in the scenario evaluations. As we will see later in the data analysis chapter, the evaluations made by the theorists were cross-checked with the corresponding practitioners' evaluations to look for indications of strategic evaluations. The evaluations of the two groups appeared to concur to a high degree, which should indicate that it is not likely that the practitioners in fact evaluated the scenarios strategically.

Furthermore, if the scenario evaluations made by the practitioner respondents were to be in concurrence with current practice, that could be an indication that the respondents may have evaluated the scenarios strategically to preserve the status quo. However, as we will report in the next chapter, neither of these two conditions seems to be the case. The theorists and practitioners evaluations appear to concur, and at the same time, practitioner's evaluations appear to differ from what is current NTO practice, i.e., defying status quo. We chose to interpret that as evidence that the respondents have not evaluated the scenarios strategically according to pure self-interest.

## **5.0 Empirical Results: Description of current practices, Scenario evaluations, and Gap-analysis.**

In this chapter we will present the analysis of the results of the sample practitioners' group consisting of all 14 countries combined, as well as the results from the theory experts' group.

### **5.1 Outline of results-section**

1. First, the combined results originating from the group assessments of the current governance practices will be presented and discussed. These results will be discussed as to the degree of
  - activity/behavior-based budgeting,
  - performance/outcome-based budgeting,
  - government vs. industry funding, and
  - government vs. industry ownership/control or shareholder ownership/control.
2. Second, we will discuss how each of the three main groups of principles:
  - 1) *budgeting principle*,
  - 2) *funding source*, and
  - 3) *ownership/organizational control*,are estimated by the theory expert and practitioner respondents to have an impact on:
  - 1) Market Focus,
  - 2) Long-Term Perspective, and
  - 3) Operational Freedom.
3. Third, we present a comparison of the:
  - practitioner representatives' vs. theory experts' evaluations, and
  - current governance practices vs. practitioner representatives' evaluations

### **5.2 Existing practices described in terms of the principles**

Table 5.1 below depicts how the proposed 14 principles are assessed to be descriptive for the practices currently implemented across our sample of OECD countries. The scale used ranges from 1 (does not describe the situation) to 7 (describes the situation), i.e., the higher the average score of a given principle is, the more descriptive the principle is for existing governance practices of a "average" country in the sample. Based on Table 5.1, the principles can be split into three categories:

- 1) Principles that describe the current practices well (High mean scores)
- 2) Principles that in some instances are descriptive for the current practice



3) Principles that have little resemblance with the current practice (Low mean scores).

**Table 5.1**  
**The degree to which the principles are descriptive of current practices**  
*(1=Does NOT describe the situation, 7=Describes the situation)*

Type of Principle	Country sample (N=14 NTOs) Principle description	Mean score (standard deviation)	Most frequent score (# of countries)
<b>Budget principle (8 principles)</b>	1. NTO's budget one year is based on last available estimates of the amount of money spent by incoming visitors and/or estimated number of incoming visitors the previous year	1.18 (0.52)	1(12)
	2. NTO's budget one year is tied to the increase/decrease in the amount of money spent by incoming visitors (or the number of visitors in NTO's country) relative to "comparable" countries the previous year	1.07 (0.26)	1(13)
	3. NTO's budget is based on sale and participation in specific projects	2.77 (1.10)	2(4)
	4. NTO's budget is negotiable and funded based on overall evaluation of the NTO's marketing plans each year	2.19 (1.34)	1(6)
	5. NTO's budget is based on a fixed sum decided each year	5.45 (1.60)	6 and 7 (4)
	6. NTO's budget is tied to the achievement of a number of goals that are agreed upon each year	1.68 (0.93)	1(8)
	7. NTO's budget is based on the revenue generated from taxation on visitors and the traveling public	1.07 (0.26)	1(13)
	8. NTO's budget is based on the revenue generated from fees and taxes paid by the travel and tourism industry	1.00 (0.00)	1(14)
<b>Funding source (3 principles)</b>	9. NTO is funded by the government	5.17 (1.50)	4, 6 and 7(3)
	10. NTO is funded by the travel and tourism industry	2.34 (0.96)	2(5)
	11. NTO is funded jointly by the travel and tourism industry and the government	3.53 (2.77)	1 (7)
<b>Ownership/control (3 principles)</b>	12. NTO is a non-profit organization owned by and responsible toward the travel and tourism industry	1.70 (0.96)	1(8)
	13. NTO is a non-profit org. owned by and responsible toward the government	6.23 (1.27)	7(9)
	14. NTO is a limited corporation owned by shareholders within and outside the travel and tourism industry	1.43 (1.57)	1(13)

## 5.2.1 Principles that describe current practices well

The four principles that most often describe current or existing governing practices are listed below. In most countries in the sample the budgets are based on a fixed amount that is decided each year, but the amount is usually in line with the amount allocated last year. Four countries gave this principle a score of 7, another four gave it a score of 6, and three countries gave it a score of 5. Only one country reported that this was not a principle descriptive of their practices. In Denmark and Great Britain the government portion of the budget is allocated for a period of three years at a time. (In the listings below mean scores are typed in **boldface**, and the corresponding standard deviations in normal type).

- P5: NTO's budget is based on a fixed sum decided each year (**5.45**; 1.60)<sup>28</sup>
- P9: Central (national) government is the source of the funding (**5.17**; 1.50)
- P11: NTO is funded jointly by the government and the tourism industry (**3.53**; 2.77)
- P13: NTO is "owned", controlled, or responsible towards the government (**6.23**; 1.27)

In most instances the central (national) government is the main source of funding for NTOs. Three countries gave this principle a score of 7, and four gave it a score of 6. One country gave this principle a score of 2, and one gave it a score of 3. It should be noted that one cannot always equate the amount obtained from the industry with private sector funding, since some of the non-central government funding may originate from other public funds. Often there are two parts of the budget: one central government (core)-part, and one part provided by the private sector. In most countries the government-part of the budget is decided on each year, but it does not vary considerably from one year to another. Six countries reported that joint funding was common (five gave this principle a score of a 7, and one gave it a score of 5), while seven countries did not rely on joint funding with the private sector (score 1).

In addition, the NTO is in most cases perceived to be "owned", controlled, or responsible towards the government (given a score of 7 by nine countries, and a score of 6 by another two). In some countries industry representation in NTO boards contribute to increase the score on principle # 12 in Table 5.1 ("owned" or responsible towards the industry). Two countries gave this principle a score of 3, and another three gave it a score of 2. Eight countries reported no industry involvement in NTO ownership/control (score 1).

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<sup>28</sup> The item representing fixed sum-budgeting was changed after interviews were conducted in Norway, Sweden and Denmark so that "NTO's budget is based on a fixed sum decided for a three-year period" was changed to "NTO's budget is based on a fixed sum decided **each year**".

## 5.2.2 Principles that in some instances are descriptive of current practices

The principles listed below are in some instances (or partially) descriptive of current practices in the sample countries. The tourism industry contributes with funding of specific projects quite frequently. These co-operative projects are in some instances initiated by the NTO itself, while in other instances, the projects are initiated by the industry. One country depends quite often on this form of financing (score 5), while three other countries use it partially (score 4). Most countries use project budgeting to a limited degree: Four countries gave the principle a score of 3 and another four gave it score of 2.

- P3: The budget is based on sale and participation in specific projects (2.77; 1.10)
- P4: The budget is negotiable and based on an evaluation of NTO's marketing plans each year (2.19; 1.34)
- P10: NTO is funded by the industry (2.34; 0.96)

Some smaller amount of private sector funding is common in the majority of our respondent countries. Eight countries gave this principle (P10 in Table 5.1) either a score of 3 or 2. In some cases, the funding contributed by the industry originates from public funds - first channelled to the industry and later (partially) redistributed to the NTO. Some groups reported that prior to money being allocated to the NTO from government funds there were some form of "negotiations" with the government on the size of the budget based on NTO's plans for next year's activities. Six countries indicated that P4 had some resemblance to the budgeting process in their country (three gave it a score of 2, and another three gave it a score of 3), while two countries uses this kind of budgeting more often (score 4 and 6, respectively). However, in most such cases the final size of the budget is rarely a direct result of these "negotiations". More frequently, the size of the budget is a consequence of the government's overall budget situation, resulting quite often in a situation where prior years' precedence determined the final NTO budget the following year. However, that could in some cases result in the budget being cut or increased arbitrarily fairly unrelated to NTO's activities or performance, depending on the government's budget and priorities.

In theory, both project-based financing and funding based on activities and plans are behavior- or activity-based budgeting principles. In practice, the degree of activity-based budgeting practice depends on the NTO's freedom and ability to set goals and to decide on the project activities. It also depends on the NTO's freedom and financial ability to decline certain projects (or goals) that are not found to be compatible with a professionally based overall market strategy.

Why industry funding has a "score" higher than 1.00 (score 2.34), can be explained by the fact that the industry quite often contributes to the NTO's budget through (partial) financing of various projects. The industry contributes usually in one of two ways: In some cases the industry contributes financially to specific projects without this practice being a formal requirement from the NTA (government) – as opposed to cases where there is a formal matching-requirement. In other cases, there is such a matching requirement, designed so that the government will match the amount contributed by the

industry. Consequently, the NTO budget in such countries contains both a government and industry portion.

As noted earlier, industry funding has a relatively high “score”, which may contribute positively to the organization’s professionalism and market orientation, particularly if the tourism industry in the country is highly market-oriented as well. Substantial levels of industry contributions may increase the industry’s commitment to the organization and interest in its activities, goals and performance as discussed in the end of Chapter 3. Furthermore, in some countries industry contributions appear to increase the NTO budgets to levels that are more competitive in the international tourism market, and reach levels that would have been hard to reach with government funding only. Industry funding can also give legitimacy to the NTO and be considered as evidence that the organization is professional and also deserves financial support by the government.

However, as the practitioners’ scenario evaluations show, industry funding may put some constraints on the organization’s freedom to act and long-term planning perspective. It is possible that marketing efforts directed at gaining the support of the industry (“industry lobbying”) could absorb resources better spent elsewhere.

### 5.2.3 Principles that are not descriptive of current practices

The principles listed below are rarely or never descriptive of the current practice:

- P6: NTO’s budget is tied to the achievement of a number of goals that are agreed upon each year (1.68; 0.93)
- P1: NTO’s budget one year is based on last available estimates of the amount of money spent by incoming visitors and/or estimated number of incoming visitors the previous year (1.18; 0.52)
- P2: NTO’s budget one year is tied to the increase/decrease in the amount of money spent by incoming visitors (or the number of visitors in NTO’s country) relative to “comparable” countries the previous year (1.07; 0.26)
- P7: NTO’s budget is based on the revenue generated from taxation on visitors and the traveling public (1.07; 0.26)
- P8: NTO’s budget is based on the revenue generated from fees and taxes paid by the travel and tourism industry (1.00; 0.00)
- P12: NTO is a non-profit organization owned by and responsible toward the travel and tourism industry (1.68; 0.96)
- P14: NTO is a limited corporation owned by shareholders within and outside the travel and tourism industry (1.43; 1.57)

As shown in Table 5.1, performance- or outcome-based financing is not practiced in general. Principles # 1, 2, 7, and 8 in Table 5.1 are not common in international practice. For instance, tax on the industry is not used by any countries, while only one country

(Austria) has a visitor tax connected to NTO budgets. In several countries, law or established practice does not allow tax revenue to be earmarked for any particular purpose. Thus, tax revenue collected from tourists or the industry (which in principle reflects the amount of revenue generated from tourism business and could in theory be considered as an indirect performance measure) will not be earmarked for funding of the NTO as of today. Principle 7 and 8 are performance-based to the extent that the budgets of the NTO do not reflect changes in tax rates, but only reflect changes in the bases on which the taxes are levied. However, on the local or regional level in some countries, such tax links are in effect: Local tax revenues (e.g., “kurtax”) are sometimes used for financing local/regional tourism marketing organizations (e.g., Austria and Spain). However, it is probably incorrect to claim that NTOs are entirely free of performance-based budgeting practice. The reason why most of the principles linked to performance (Principles 1, 2, 7, and 8) do not have a score of 1.00 (lowest = non existent), is because in a few instances was expressed that good market performance one year could provide a basis for determining the size of the next year’s budget - without this being established in a formal way. Two countries indicated practices with a slight resemblance to P1 (score 2 and 3) and one country gave P2 a score of 2. It was pointed out that a lack of measurable results or no results of NTO projects most likely could cause private sector and government to curb their spending on the NTO – at least in the long run.

Why the limited corporation ownership principle does not have a score of 1.00 (lowest) either, is because that in some countries (e.g., Portugal) the NTO itself has control of or owns commercial companies. In instances where the industry has significant board representation, the NTO is sometimes perceived as being partially owned or controlled by the industry. One country gave this principle (P12) a score of 4, three countries gave it a score of 3, and two more gave it a score of 2 - indicating at least some degree of industry control of the NTO in about half of our sample countries.

Generally, the “typical/average” NTO holds the following characteristics:

- |  |
|--|
| <ul style="list-style-type: none"> <li>• Fixed sum (core) budgets are decided upon each year</li> <li>• Project financing is quite common</li> <li>• Budgets based on evaluations of marketing plans is also common</li> <li>• Budgets are not performance-based in the sense of being tied to quantifiable effects in the <i>tourism market</i></li> <li>• The NTO is predominately funded by the government, and in some instances jointly by the government and the industry</li> <li>• The NTO is owned/controlled by the government, i.e., under the authority of a ministry or other government body.</li> </ul> |
|--|

From the descriptions of current practices shown in Table 5.1 it becomes apparent that there is very little variation in how NTOs are organized and governed worldwide. Many of the principles we are studying have low mean scores, indicating that they are non-to-rare in existence. The standard deviations are relatively small for most of the 14 principles, indicating only small variations in the degree of those principles’ use in practice. This fact is important to note, because it puts substantial restrictions on the

number of feasible research designs. As discussed in Chapter 4 this precludes the ability to choose a purely experimental design, or to do natural experiments and case studies. Generally there is too little variation in the independent variables (principles) to make any such comparisons meaningful. The only principle that has some degree of variance worth to mention is P11 (st. dev. = 2.77), which is *joint funding*. The variance stems for the most part from what degree (proportion) of the budget is funded by the government, and how much funded by the industry in a combined funding scheme. (We will investigate the empirical relationship between the funding source and NTO's market focus in more detail later in Appendix 7.) At the same time it is then difficult to find any "best" or "worst" cases in existing practices that can be studied and explained by our governance principles, since most NTOs are organized and governed in about the same way. This problem also precludes the ability to do case studies to investigate the variables we are interested in this study.

Very little variance in the way NTOs are organized and governed has another important implication. When stakeholders responsible for NTO matters are to organize a new NTO or reorganize an existing one, there are few other cases to look for that can provide a better solution than the traditional way. Had there been more variation in practice, there would probably have been more examples for stakeholders for to follow trait (in positive cases) or avoid (in negative cases). Without this kind of variation in existing practices, this could act as a conservative force, perpetuating the current "regime". As mentioned in the introductory section, an important purpose of this thesis is to question current practice and suggest alternative ways to organize and govern NTOs. Therefore, we find it necessary to extend the analysis beyond current practices.

### 5.3 Scenario evaluations: The principles' importance for NTOs' incentives, abilities and working conditions

In this section we will address how the participants evaluated the 14 principles, which were embedded in the scenarios respondents were presented to, in terms of the principles' impact on:

- Market Focus
- Long-Term Perspective
- Operational Freedom

From the scenario evaluation data it was possible to extract each individual *principle's* perceived impact on the said dependent variables. By comparing the mean score of the 14 principles on the items representing any of the three dependent variables one can determine which *budgeting principle, funding source or owner alternative* that is perceived to be best (or worse) for NTOs' Market Focus, Long-Term Perspective, and Operational Freedom. A significantly higher (than another principle's) score of a given principle on items representing any of the three dependent variables would indicate that the principle is evaluated more positive on that aspect. For instance, a given budgeting principle that scores significantly higher on e.g., NTOs' Market Focus than any other

budgeting principle could be interpreted as (on average) better for NTOs' Market Focus than those other budgeting principles. This is also valid for that principle in combination with any of the funding and ownership principles (and vice versa.)

Most of the quantitative analyses presented in this thesis are carried out using ANOVA. ANOVA (Analysis of variance) is used to test whether the scenario evaluations vary systematically with any type of principle. For our purposes this method of analysis is used to determine if differences in mean scores between principles are due to systematic variation in the evaluations of the principles, or simply due to random error. The level of confidence is 95% ( $p < 0.05$ ) unless otherwise noted.

The presentation is organized as shown in Table 5.2. An overview of results and operationalizations of the various constructs are shown in Tables 5.6-5.9. We only discuss principles that receive scores that are substantially higher or lower than the scores obtained for other principles. For ease of distinction the *independent variables* are typed in italics, and the Dependent Variables are typed with capitalization in this chapter.

**Table 5.2**  
**Structure of presentation of scenario evaluations** (numbers in cells refer to text-paragraphs)

Dependent variable	Independent variable (Principles)		
	<i>Budgeting method</i>	<i>Funding source</i>	<i>Ownership/control</i>
5.3.2 Market Focus	5.3.2.1	5.3.2.2	5.3.2.3
5.3.3 Long -Term Perspective	5.3.3.1	5.3.3.2	5.3.3.3
5.3.4 Operational Freedom	5.3.4.1	5.3.4.2	5.3.4.3
5.3.5 Conclusion			

When interpreting the results, a caveat is in order: A “low” score does not imply a negative score on the scale used. It only implies that the principle in question on the average gets a score that is considerably lower than the other principles with which it is compared, and is thus evaluated less positive rather than negative for the aspect in question.

### 5.3.1 The relative impact of the principles

Table 5.3 below shows the relative impact of the three main groupings of principles, which are: *the budget principle* (P1-P8), *funding source* (P9-P11), and *ownership/control* of the organization (P12-P14) on the dimensions we are interested in. Table 5.3 shows the data from the practitioners' sample only.

From the information in Table 5.3 below, it becomes apparent that:

- 1) The budgeting principles have less importance for NTOs' *market focus* than for the ability to plan and operate on a *long-term* basis its *operational freedom*.
- 2) The *budgeting principles* are clearly more important than both the *funding source* and the *ownership/control* of NTOs with respect to all the three evaluative aspects.

The groups were instructed to cognitively “free themselves” from their country-specific context as much as possible when they were to evaluate the scenarios. Despite this instruction, our experience based on the interview sessions is that the importance group members attribute to the various principles will be somewhat influenced by the economic, cultural, and political context prevailing in the respondents’ countries.

**Table 5.3<sup>29</sup>**

**Practitioners’ international sample: The relative impact of the three factors on Market Focus, Long-Term Operation, and Operational Freedom of the NTO**

<i>Factor</i>	<b>Market Focus</b>	<b>Long-Term Perspective</b>	<b>Operational Freedom</b>
<i>Budgeting principle</i>	47%	60%	52%
<i>Funding source</i>	33%	18%	27%
<i>Ownership/control</i>	20%	22%	21%

For instance, respondents from countries that have experienced a decrease in government spending on tourism aspects may evaluate government involvement in financing and political control of the NTO differently from those who have witnessed an increase in government spending.

One condition reduces the across-countries comparability somewhat: The wording of one of the principles (P5) was changed slightly after the interviews in Norway, Sweden and Denmark were completed. In these three countries the principle was formulated such that the respondents were asked to evaluate the effect of *a fixed sum negotiated for a period of 3-5 years*, while the respondents in the other countries were asked to evaluate the effect of *a fixed sum decided each year*. This was done when we discovered that the first alternative (long-term budgeting period) seldom was descriptive of current practice, whereas the last alternative (short-term budgeting period) was far more applicable.

Table 5.4 below shows the F value and level of significance of each independent variable’s evaluated effect on the dependent variables in our model for the practitioners’ sample. Using this general linear model procedure, we can test the null hypotheses about the effects of factor variables on the means of various groupings of a joint distribution of dependent variables. The test scores from this (multivariate) test can be understood as follows: The test is used to test the 0 hypothesis that there are no differences in means. A high F-value ( $df = 1$ ) and a low significance level ( $p < 0.05$ ) indicate that the 0 hypothesis should be rejected. In other words, the independent variable produces in fact significant systematic variations in the dependent variables. In our case, it means that inclusion of a

<sup>29</sup> The information in Table 5.3 was derived from running the data from the practitioners’ scenario evaluations in conjoint analysis software. The percentage scores in the table represent the proportion of “utility” attributed to each category of principles in terms of their impact on the dependent variables. A relatively higher percentage score of a given category means that this category of principles has more impact on a given dependent variable than the categories. Note: The theory experts’ sample size was too small to make a corresponding analysis of that group’s evaluations meaningful.



given principle with a low significance-level score in a given scenario should have a significant impact on how that scenario is evaluated in terms of the effects we are interested in.

**Table 5.4**  
**Practitioners' international sample: Level of significances**

<b><i>Principles</i></b>	<b>Expected effects</b>	<b>F</b>	<b>Sig.</b>
<b><i>Budgeting principle</i></b>	<b>Market Focus</b>	<b>5.909</b>	<b>0.016</b>
	<b>Long-Term Perspective</b>	<b>5.633</b>	<b>0.018</b>
	<b>Operational Freedom</b>	<b>12.462</b>	<b>0.000</b>
<b><i>Funding source</i></b>	<b>Market Focus</b>	<b>36.087</b>	<b>0.000</b>
	<b>Long-Term Perspective</b>	<b>1.316</b>	<b>0.252</b>
	<b>Operational Freedom</b>	<b>7.287</b>	<b>0.007</b>
<b><i>Ownership/control</i></b>	<b>Market Focus</b>	<b>0.000</b>	<b>0.984</b>
	<b>Long-Term Perspective</b>	<b>0.049</b>	<b>0.826</b>
	<b>Operational Freedom</b>	<b>3.608</b>	<b>0.058</b>

From the table we can see that the *budgeting principles* appear are evaluated to have a strong and significant impact on all three dimensions we are interested in. The *funding source* is also considered important for NTOs' Market Focus and Operational Freedom, while it has only a limited expected effect on NTOs' Long-Term Perspective. The least important of the three independent variables appear to be *ownership/control* when analyzed as composite group. The respondents only expect it to have a significant impact on NTO's Operational Freedom, while it has little bearing on NTO's Market Focus and Long-Term Perspective. If we, however, split the analysis of the practitioners' group into three sub-groups representing respondents from the NTO, the NTA and the industry, the ownership variable seems to have a stronger effect than for all respondents combined. When analyzed in sub-groups the F values and significance levels improve, and the impact of the *ownership* variable is then significant for both Market Focus and Operational Freedom for all three sub-groups: **NTA**: Market Focus, sig.= 0.000; Operational Freedom, sig.= 0.020; **NTO**: Market Focus, sig.= 0.060; Operational Freedom, sig.= 0.07; and **industry**: Market Focus, sig.= 0.016; Operational Freedom, sig.= 0.036. This should indicate that some of the unexplained variance in how *ownership* is evaluated to affect Market Focus and Operational Freedom could to a large extent be explained from variance between the evaluations of the three sub-groups. The impact of *ownership*, however, is not significant for either sub-group for impact on Long-Term Perspective.

Table 5.5 below shows the same set of data for the theory experts' sample. The only significant effects we can identify are the *budgeting principles*' evaluated impact on NTOs' Market Focus, and a somewhat less pronounced effect on Operational Freedom. A small effect could also be traced to the *funding source*'s effect on Operational Freedom. Lack of significant scores for the other variables *may* be partially attributed to the small

sample size. (Some of the *budgeting principles* had only 4 observations). A larger sample, like the practitioners' sample, may have yielded more significant results<sup>30</sup>.

**Table 5.5**  
**Theory experts' sample: Level of significances**

<b><i>Principles</i></b>	<b>Expected effects</b>	<b>F</b>	<b>Sig.</b>
<b><i>Budgeting principle</i></b>	<b>Market Focus</b>	<b>6.597</b>	<b>0.014</b>
	<b>Long-Term Perspective</b>	<b>0.070</b>	<b>0.793</b>
	<b>Operational Freedom</b>	<b>1.882</b>	<b>0.178</b>
<b><i>Funding source</i></b>	<b>Market Focus</b>	<b>0.281</b>	<b>0.599</b>
	<b>Long-Term Perspective</b>	<b>0.415</b>	<b>0.523</b>
	<b>Operational Freedom</b>	<b>1.659</b>	<b>0.205</b>
<b><i>Ownership/control</i></b>	<b>Market Focus</b>	<b>0.579</b>	<b>0.451</b>
	<b>Long-Term Perspective</b>	<b>0.555</b>	<b>0.460</b>
	<b>Operational Freedom</b>	<b>0.715</b>	<b>0.403</b>

In the following sections we will investigate the results from the scenario analysis in more detail, and break the level of analysis down to deal with each of the 14 individual principles. The main results from the scenario analysis is depicted in Figures 5.6 and 5.7 on the preceding two pages, and summarized in Tables 5.8 and 5.9 at the end of this section. From this point on, we will present the results from the theory experts' sample first and then the practitioners' sample where applicable.

### 5.3.2 Effects on market focus

The first dependent factor we will analyze is the Market Focus of the NTO, and look at how the various principles are evaluated to affect this dimension.

Market Focus reflects the organization's ability or tendency to collect, analyze, distribute and act upon market information about the visitors' current and future needs and preferences and about competitors products and actions. A scale of Market Focus was measured<sup>31</sup> as the mean (on a scale from 1-7) of the following items:

- Collect information on customer needs and preferences
- Communicate information about the market to the tourism industry
- Influence the tourism industry to improve their products
- Collect and analyze information about competitors
- Use of market information when designing communication with the market
- Be selective in terms of which products and markets NTO will market

<sup>30</sup> The analysis of the scenario evaluations shows a fairly good match between the theorists and practitioner's evaluations (as reported later in this chapter), therefore it is reason to believe that the experts' sample would go in the same direction (including higher significance levels) as the practitioners sample, had the sample size been increased. The sample size was kept small due to time- and resource restrictions.

<sup>31</sup> The items were factor analyzed and were found to correlate highly with one factor (see Appendix 3).

**Table 5.6**  
**Scenario evaluations: Theory experts' sample**

<b>Effects</b>	<b>High score principles*</b>	<b>Low score principles*</b>
<p><b>Market Focus</b> Scores (1-7 scale) based on the following measures: Will motivate NTO to....:</p> <ul style="list-style-type: none"> <li>• collect information based on customer needs and preferences</li> <li>• communicate information about the market to the tourism industry</li> <li>• influence the tourism industry to improve their products</li> <li>• collect and analyse information about competitors</li> <li>• use market information in communication with the market</li> <li>• be selective of products and markets</li> </ul>	<p><b>Budgeting principle</b></p> <ul style="list-style-type: none"> <li>• P1: Budget based on estimates of the amount of money spent by visitors the previous year (5.64; 1.70)</li> <li>• P2: Budget based on the increase/decrease in the amount of money spent by incoming visitors relative to "comparable" countries (5.36; 1.27)</li> <li>• P7: Budget based on the revenue generated from taxation on visitors and the travelling public (4.64; 1.67)</li> </ul> <p><b>Funding source</b></p> <ul style="list-style-type: none"> <li>• P10: NTO is funded by the travel and tourism industry (5.15; 1.04)</li> </ul> <p><b>Ownership/Control</b></p> <ul style="list-style-type: none"> <li>• (P12: NTO is a non-profit organization owned by and responsible towards the travel and tourism industry (4.86; 1.43) scores highest, but <b>not</b> significantly higher)</li> </ul>	<p><b>Budgeting principle</b></p> <ul style="list-style-type: none"> <li>• P5: Budget based on a fixed sum decided each year (3.32; 1.15)</li> </ul> <p><b>Funding source</b></p> <ul style="list-style-type: none"> <li>• P11: NTO is funded jointly by the travel and tourism industry and the government (4.28; 1.19)</li> <li>• P9: NTO is funded by the government (4.37; 1.35)</li> </ul> <p><b>Ownership/Control</b></p> <ul style="list-style-type: none"> <li>• (P13 Government ownership/control (4.44; 1.16), and P14: Limited Corporation owned by shareholders score (4.45; 1.26 ) lowest, but <b>not</b> significantly lower)</li> </ul>
<p><b>Long-Term Perspective</b> Scores (1-7 scale) based on the following measures: Will give NTO....:</p> <ul style="list-style-type: none"> <li>• long-term perspective in plans and activities</li> <li>• difficulties to pursue long-term goals</li> <li>• (not) enough funds for NTO's budget</li> <li>• improved long-term market performance</li> </ul>	<p><b>Budgeting principle</b></p> <ul style="list-style-type: none"> <li>• P7: Budget based on the revenue generated from taxation on visitors and the travelling public (4.63; 1.11)</li> <li>• P2: Budget based on the increase/decrease in the amount of money spent by incoming visitors relative to "comparable" countries (4.29; 0.58)</li> <li>• P5: Budget based on a fixed sum decided each year (4.26; 1.06)</li> </ul> <p><b>Funding source</b></p> <ul style="list-style-type: none"> <li>• (P9: Government funding scores highest (4.15; 0.81), but <b>not</b> significantly higher)</li> </ul> <p><b>Ownership/Control</b></p> <ul style="list-style-type: none"> <li>• (P14: Limited Corporation ownership scores highest (4.14; 0.73), but <b>not</b> significantly higher)</li> </ul>	<p><b>Budgeting principle</b></p> <ul style="list-style-type: none"> <li>• P4: Budget based on evaluation of the NTO's marketing plans each year (3.62; 0.72)</li> <li>• P6: Budget based on achievement of goals and objectives decided each year (3.88; 0.82)</li> </ul> <p><b>Funding source</b></p> <ul style="list-style-type: none"> <li>• (P10: Funding by the industry (3.92; 0.96) and P 11 joint funding (3.94; 0.46) score lowest, but <b>not</b> significantly lower)</li> </ul> <p><b>Ownership/Control</b></p> <ul style="list-style-type: none"> <li>• (P12: Industry ownership (3.88; 0.89) and P13 government ownership (4.02; 0.71) score lowest, but <b>not</b> significantly lower)</li> </ul>
<p><b>Operational Freedom</b> Scores (1-7 scale) based on the following measures: Will give the NTO....:</p> <ul style="list-style-type: none"> <li>• problems with operations due to too much fluctuations in budget</li> <li>• (not) make the NTO over-prioritize special interest</li> <li>• make the NTO spend too much resources on sale to the industry</li> <li>• freedom to act</li> </ul>	<p><b>Budgeting principle</b></p> <ul style="list-style-type: none"> <li>• P7: Budget based on the revenue generated from taxation on visitors and the travelling public (5.40; 0.93)</li> <li>• P5: Budget based on a fixed sum decided each year (4.75; 0.75)</li> <li>• P8: Budget based on the revenue generated from taxation of travel and tourism industry (4.47; 1.12)</li> </ul> <p><b>Funding source</b></p> <ul style="list-style-type: none"> <li>• P9: NTO is funded by the government (4.61; 0.97)</li> </ul> <p><b>Ownership/Control</b></p> <ul style="list-style-type: none"> <li>• P13: Government ownership/control (4.32; 1.13)</li> <li>• P14: Limited Corporation ownership (4.17; 1.13)</li> </ul>	<p><b>Budgeting principle</b></p> <ul style="list-style-type: none"> <li>• P3: Budget based on sale and participation in specific projects (3.03; 0.52)</li> </ul> <p><b>Funding source</b></p> <ul style="list-style-type: none"> <li>• P10: NTO is funded by the travel and tourism industry (3.35; 1.03)</li> </ul> <p><b>Ownership/Control</b></p> <ul style="list-style-type: none"> <li>• P12: Industry ownership/control (3.36; 1.08)</li> </ul>

\* Mean scores are typed in **boldface**, while standard deviation statistics are in normal type.

**Table 5.7**  
**Scenario evaluations: Practitioners' sample**

<b>Effects</b>	<b>High score principles*</b>	<b>Low score principles*</b>
<p><b>Market Focus</b> Scores (1-7 scale) based on the following measures: Will motivate NTO to...:</p> <ul style="list-style-type: none"> <li>• collect information based on customer needs and preferences</li> <li>• communicate information about the market to the tourism industry</li> <li>• influence the tourism industry to improve their products</li> <li>• collect and analyze information about competitors</li> <li>• use market information in communication with the market</li> <li>• be selective of products and markets</li> </ul>	<p><b>Budgeting principle</b></p> <ul style="list-style-type: none"> <li>• <b>P2: Budget based on the increase/decrease in the amount of money spent by incoming visitors relative to "comparable" countries (5.07; 1.01)</b></li> <li>• <b>P4: Budget based on evaluation of the NTO's marketing plans each year (4.88; 1.22)</b></li> <li>• <b>P1: Budget based on estimates of the amount of money spent by visitors the previous year (4.77; 1.21)</b></li> </ul> <p><b>Funding source</b></p> <ul style="list-style-type: none"> <li>• <b>P10: NTO is funded by the travel and tourism industry (5.20; 1.09)</b></li> <li>• <b>P11: NTO is funded jointly by the travel and tourism industry and the government (4.94; 1.08)</b></li> </ul> <p><b>Ownership/Control</b></p> <ul style="list-style-type: none"> <li>• <b>P12: NTO is a non-profit organization owned by and responsible towards the travel and tourism industry (5.09; 1.13)</b></li> <li>• <b>P14: NTO is a Limited Corporation owned by shareholders (4.79; 1.15)</b></li> </ul>	<p><b>Budgeting principle</b></p> <ul style="list-style-type: none"> <li>• <b>P7: Budget based on the revenue generated from taxation on visitors and the travelling public (3.74; 1.29)</b></li> <li>• <b>P5: Budget based on a fixed sum decided each year (4.01; 1.14)</b></li> </ul> <p><b>Funding source</b></p> <ul style="list-style-type: none"> <li>• <b>P9: NTO is funded by the government (3.96; 1.21)</b></li> </ul> <p><b>Ownership/Control</b></p> <ul style="list-style-type: none"> <li>• <b>P13: NTO is a non-profit organization owned by and responsible towards the government (4.15; 1.28 )</b></li> </ul>
<p><b>Long-Term Perspective</b> Scores (1-7 scale) based on the following measures: Will give NTO...:</p> <ul style="list-style-type: none"> <li>• long-term perspective in plans and activities</li> <li>• difficulties to pursue long-term goals</li> <li>• (not) enough funds for NTO's budget</li> <li>• improved long-term market performance</li> </ul>	<p><b>Budgeting principle</b></p> <ul style="list-style-type: none"> <li>• <b>P5: Budget based on a fixed sum decided each year (4.24; 1.11)</b></li> <li>• <b>P7: Budget based on the revenue generated from taxation on visitors and the travelling public (4.07; 1.61)</b></li> <li>• <b>P4: Budget based on evaluation of the NTO's marketing plans each year (4.00; 1.47)</b></li> </ul> <p><b>Funding source</b></p> <ul style="list-style-type: none"> <li>• <b>P11: NTO is funded jointly by the travel and tourism industry and the government (4.05; 1.23 )</b></li> </ul> <p><b>Ownership/Control</b></p> <ul style="list-style-type: none"> <li>• <b>(P13: Government ownership/control scores highest (3.91; 1.28), but not significantly higher than others)</b></li> </ul>	<p><b>Budgeting principle</b></p> <ul style="list-style-type: none"> <li>• <b>P3: Budget based on sale and participation in specific projects (3.41; 1.18)</b></li> <li>• <b>P1: Budget based on the amount of money spent by incoming visitors the previous year (3.64; 1.12)</b></li> <li>• <b>P2: Budget based on the increase/decrease in the amount of money spent by incoming visitors relative to "comparable" countries (3.75; 1.09 )</b></li> </ul> <p><b>Funding source</b></p> <ul style="list-style-type: none"> <li>• <b>P10: (Funding by the industry scores lowest (3.62; 1.17), but not significantly lower than govt. funding)</b></li> </ul> <p><b>Ownership/Control</b></p> <ul style="list-style-type: none"> <li>• <b>(P14: Limited Corporation scores lowest (3.78; 1.25), but not significantly lower than both others)</b></li> </ul>
<p><b>Operational Freedom</b> Scores (1-7 scale) based on the following measures: Will give the NTO...:</p> <ul style="list-style-type: none"> <li>• problems with operations due to too much fluctuations in budget</li> <li>• (not) make the NTO over-prioritize special interest</li> <li>• make the NTO spend too much resources on sale to the industry</li> <li>• freedom to act</li> </ul>	<p><b>Budgeting principle</b></p> <ul style="list-style-type: none"> <li>• <b>P5: Budget based on a fixed sum decided each year (4.79; 1.25)</b></li> <li>• <b>P7 Budget based on the revenue generated from taxation on visitors and the travelling public (4.41; 0.96)</b></li> <li>• <b>P4: Budget based on evaluation of the NTO's marketing plans each year (3.98; 1.54 )</b></li> </ul> <p><b>Funding source</b></p> <ul style="list-style-type: none"> <li>• <b>P9: NTO is funded by the government (4.13; 1.28)</b></li> </ul> <p><b>Ownership/Control</b></p> <ul style="list-style-type: none"> <li>• <b>P13: Government ownership/control (4.13; 1.33 )</b></li> </ul>	<p><b>Budgeting principle</b></p> <ul style="list-style-type: none"> <li>• <b>P3: Budget based on sale and participation in specific projects (2.88; 1.10)</b></li> <li>• <b>P1: Budget based on the amount of money spent by incoming visitors the previous year (3.45; 1.13 )</b></li> <li>• <b>P2: Budget based on the increase/decrease in the amount of money spent by incoming visitors relative to "comparable" countries (3.50; 1.19)</b></li> </ul> <p><b>Funding source</b></p> <ul style="list-style-type: none"> <li>• <b>P10: NTO is funded by the travel and tourism industry (3.16; 1.19)</b></li> </ul> <p><b>Ownership/Control</b></p> <ul style="list-style-type: none"> <li>• <b>(P14 Limited Corporation scores lowest (3.36; 1.20), but not significantly lower than industry ownership)</b></li> </ul>

\*Principles in **boldface** are significantly higher/lower scored than the majority of others on the p<0.05 level

These items overlap to some extent with the concept of “market orientation”, which will be discussed in more detail in Appendix 7. (We will use the terms “market orientation” and “market focus” interchangeably here.) In the next paragraphs we will discuss how *budgeting, funding source, and ownership* relate to NTOs’ Market Focus.

### 5.3.2.1 Effects of budgeting principle on market focus

The respondent groups perceive the following NTO budgeting principles to have a positive effect on the Market Focus of the organization (numbers shown **in bold type** are the mean scores, while numbers in normal type are the corresponding standard deviations):

*High scores*

#### **Theory experts’ sample:**

- *P1: Budget based on the last available estimates of the amount of money spent by incoming visitors (international tourism receipts) the previous year (**5.64**; 1.70)*
- *P2: Budget based on the increase/decrease in the amount of money spent by incoming tourists (international tourism receipts) relative to “comparable” countries (**5.36**; 1.27)*
- *P7: Budget based on the revenue generated from taxation on visitors and the traveling public (**4.64**; 1.67).*

The three principles ranked highest by the theory experts are all performance-based principles. We can label the two highest-ranked (P1 and P2) as direct performance principles, while the third-ranked (P7) can be termed an indirect performance principle since NTOs’ budgets are then reflected by e.g., a certain percentage of revenues from visitor taxes. Our theory experts’ evaluations are in line with what we have discussed earlier in the theory chapter, indicating that an organization like an NTO probably needs some kind of incentive tied to market performance to adopt a strong Market Focus.

#### **Practitioners’ sample:**

- *P2: Budget based on the increase/decrease in the amount of money spent by incoming visitors (international tourism receipts) relative to “comparable” countries (**5.07**; 1.01)*
- *P4: Budget based on evaluation of the NTO’s marketing plans each year (**4.88**; 1.22)*
- *P1: Budget based on the last available estimates of the amount of money spent by incoming visitors (international tourism receipts) the previous year (**4.77**; 1.21)*

It is notable that, while the principles ranked first and third (P2 and P1) by the practitioners are both performance-based principles, this is not the case for the second-ranked principle P4 (*budgets based on evaluation of the NTO’s marketing plans each year*). The relatively high ranking of this principle is somewhat surprising according to what we could derive from theory. A budgeting procedure based on evaluation of plans and activities could potentially lead the NTO to focus on lobbying- and negotiation processes. This could be in order to maximize budgets and gain plan approval by the

funding stakeholders. Such processes can be counter-productive in terms of a desirable Market Focus. Our practitioner respondents apparently view this matter differently (refer also to the comments made about this particular principle in Section 5.2.2).

#### *Low scores*

##### **Theory experts' sample:**

The theoreticians score P5 (*budget based on a fixed sum decided each year*) (3.32; 1.15) the lowest in terms of its impact on Market Focus. This is also in line with the theory reviewed; a *fixed sum* allocation should provide weak or no incentives for Market Focus. On the contrary, it could give incentives to focus on lobbying activity during the yearly budget negotiation process, given that such real negotiations in fact do occur.

##### **Practitioners' sample:**

Among the practitioners the budgeting principle that received the lowest evaluation (3.74; 1.28) in terms of its impact on market focus was P7 (*budgets based on the revenue generated from taxation on visitors and the traveling public*). It is interesting to note that this principle in fact can be perceived as an indirect performance-based principle since the revenue generated for the NTO would co-vary with the economic value of incoming tourism. Also, a large portion of tax revenues for the government is obtained indirectly (i.e., income taxes of industry employees or sales tax on tourism products and services). To the extent this tax is levied in addition to other taxes (and not made a part of e.g., the already existing sales tax) it may be considered an extra burden that would harm tourism.

In addition, some of the respondents were concerned that the tax revenue would go into the national government general tax fund, and parts of the revenue generated from tourism would be spent on funding of other causes than NTOs' budgets. If the latter were the case, the principle would obviously have little value as an incentive mechanism. So the concern among some respondents that the funds generated through a tax would not be channeled in full back to NTO funding, and at the same time it would increase the tax burden on tourism, may have made the respondents evaluate the principle negatively with regards to the impact on NTO's Market Focus. Despite its character as a performance-based principle, we believe the general negative attitude toward extra taxation is the primary reason for the low score.

It is also interesting that the most common budgeting principle in current practice P5 (*budgets based on a fixed sum negotiated each year*), receives the second lowest score (4.02; 1.13) among the eight budgeting principles. Thus, our practitioner respondents express through their scenario evaluations that today's most commonly used budgeting principle may not be the best for NTOs' Market Focus.

### 5.3.2.2 Effects of funding source on market focus

#### *High scores*

##### **Theory experts' sample:**

The theory experts find P10 (*funding by the industry*) (5.15; 1.09) as the best source for NTOs' budgets in terms of facilitating Market Focus. We have made the argument earlier in the theory chapter that private/industry financiers may put pressure on the NTO to show market results, since private funds may have stronger requirements for return on investment than public funds. It would be very difficult for an NTO predominantly dependent on industry funding to "ignore" the tourism market, because that would probably give mediocre market results eventually. In such a case, the industry could then be expected to reduce their funding for the NTO, and through that "punish" the NTO. An NTO funded solely by the government may not be held accountable in the same way, and could be able to maintain or increase funding - even with weak market results.

**Practitioners' sample:**

From the practitioners' evaluations it was not possible to identify a single funding source principle that could be labeled significantly "best" in terms of its impact on Market Focus. P10 (*industry funding*) (5.19; 1.09) and P11 (*joint funding*) (4.93; 1.08) are evaluated about equally attractive, with P10 slightly better than P11.

*Low scores*

**Theory experts' sample:**

From the theoreticians' evaluations it was not possible to identify a single source alternative that could be termed "worst". Both P10 (*government funding*) and P11 (*joint funding*) score about equally, with the government alternative scoring slightly higher of the two.

**Practitioners' sample:**

However, one principle appears to be considered *worse* than others by the practitioners: P9 (*Government funding*) (3.96; 1.21) as the sole funding source, is the one that has the weakest positive impact on Market Focus.

### 5.3.2.3 Effects of ownership on market focus

*High scores*

**Theory experts' sample:**

Among the theory experts P12 (*NTO is a non-profit organization owned by and responsible towards the travel and tourism industry*) scored the highest (4.86, 1.25) as positive for Market Focus. The corporate governance theory discussed earlier tend to suggest private ownership as positive because it argues that government-owned organizations involved in business (e.g., state owned enterprises, SOEs) are less efficient than private firms. This is also supported by the discussion in the public choice theory section, which discusses the inefficiency of bureaucracies, and the World Bank-study discussed in Section 2.4.2 under social economics theory. However, there is still some disagreement in the theory discussed about this matter; and our theory experts are apparently not univocal about this matter in their evaluations of the ownership alternatives.

**Practitioners' sample:**

From the practitioners side P12 (*industry ownership*) (5.09; 1.13), and P14 (*NTO is a limited corporation owned by shareholders*) (4.79; 1.15) received positive scores in terms of their impact on NTOs' Market Focus. Thus, respondents seem to believe that an industry-led NTO or a commercial type of NTO organization will be more motivated and able to focus on the market than a government-controlled NTO. However, there is no absolute distinction in the data between these two ownership alternatives, yet *industry ownership* is evaluated significantly better than the others on the  $p < 0.10$ -level.

The analysis shows that *industry ownership* is considered the most positive for NTOs' Market Focus, while *government ownership* is evaluated less positive. The respondents may view industry owners as more market-focused than public sector owners, and they probably reason it will influence the focus of the organization in the same direction as its owners.

*Low scores***Theory experts' sample:**

Both P13 (*government ownership*) (4.44; 1.16), and P14 (*limited corporation*) (4.44; 1.26) score equally among the theoreticians. These scores are, however, only slightly lower than the highest scoring principle, which is P12.

**Practitioners' sample:**

The practitioner respondents are somewhat less positive (4.14; 1.28) with respect to how P13 *government ownership* may influence the Market Focus of NTOs.

This finding also is consistent with our analyses of the ranking of *scenarios*: Scenarios that contain *government funding* and *government ownership* get rather consistently the lowest score in terms of positive effect on NTOs' Market Focus. Scenarios where *government funding* is combined with *government ownership* score definitely lowest on average (3.74; 1.20) e.g., compared to *industry funding* combined with *industry ownership* (5.12; 1.15).

What becomes apparent is that the most common combination of funding source and ownership, namely NTOs funded and owned by the government, is not at all evaluated positive in terms of NTOs' Market Focus. Among all 22 scenarios evaluated, the scenario that scored lowest overall on Market Focus (3.35; 0.86) was a scenario containing a *fixed sum* allocation as budgeting principle (P5), and with NTO *funded by the government* (P9) and *owned/controlled by the government* (P13). This is in fact the most common scenario in current practice according to the respondents' assessments. The highest scoring scenario (5.46; 0.67) was one with *industry funding* (P10) and NTO organized as a *limited company* (P14), combined with *project based* budgeting (P3), i.e., one of the most commercial of the alternative scenarios. Furthermore, 13 of the 14 countries rank *industry ownership* better than *government ownership* as positive for the organizations' Market Focus. Obviously, in this case there is a clear difference in how things are done in



practice and what is considered ideal. We discuss this theory-practice gap later in Section 5.3.6.2.

On the Market Focus-dimension in general, we found a great amount of concordance in the evaluations between the expert and practitioner groups. We will also revert to the issue of between-group concordance in more detail in Section 5.3.6.1.

**Differences in evaluations between various practitioner respondent-types:**

Using a t-test for differences in means, we found that variations in evaluations between NTO, NTA and industry respondents were not significant with regards to most of the eight budgeting principles' effect on NTOs' Market Focus. The exception is, however, that industry representatives are more positive to the *tax alternatives* P7 and P8 than the other practitioner respondents.

One could of course speculate that industry respondents would be more in favor of performance-based principles, since this type of incentive mechanisms are more common in the private sector, whereas activity-based budgeting is the norm in the public sector. According to the practitioners' respondents, this notion only applies to the two tax-based principles P7 (*visitor tax*) and P8 (*industry tax*). The industry representatives are more positive to *taxation* for enhancing NTOs' Market Focus than the NTA representatives (P7: NTA (mean score **3.80**) vs. Industry (mean score **5.11**); sig. = 0.041 & P8: NTA (mean score **3.87**) vs. Industry (mean score **5.18**); sig. = 0.029). This is also the case for the NTO vs. industry representatives (P7: NTO (mean score **3.45**) vs. Industry (mean score **5.11**); sig. = 0.005 & P8: NTA (mean score **4.37**) vs. Industry; sig. = 0.014). The NTO representatives are also more skeptical to budgeting through *projects* than the industry (P3: NTO (mean score **4.35**) vs. Industry (mean score **5.35**); sig. = 0.013).

Other than that, is not so surprising that we find few differences in evaluations between the respondent categories on this issue. It should not really be any other strong reasons why there would be differences in how people from different respondent categories evaluate the various *budgeting principles*. Few differences can be found with respect to *funding source* as well. However, there is reason to believe our categorization of respondents representing NTO, NTA, and industry respectively has more relevance in terms of the ownership-dimension, since the NTO and industry represent in reality different ownership/control groups.

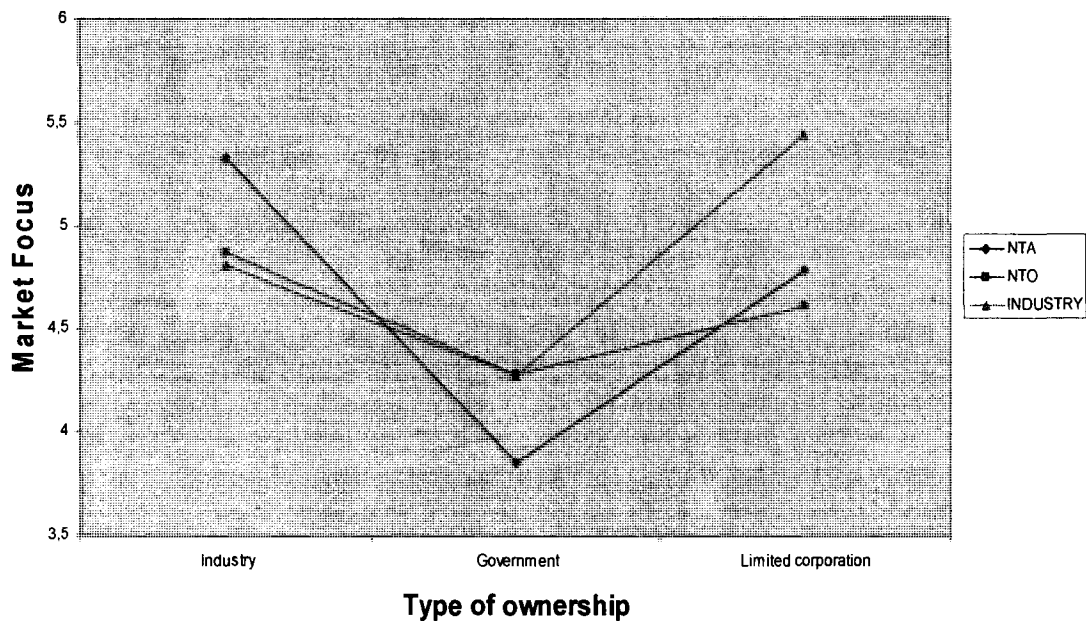
Further analysis shows that there are significant differences in the way industry, NTO, and NTA representatives view ownership. Not surprisingly, industry representatives give systematically higher Market Focus-ratings to the *limited corporation* alternative than the two other groups of respondents do (NTA (mean score **4.78**) vs. Industry (mean score **5.44**); sig. = 0.056) and (NTO (mean score **4.64**) vs. Industry: sig. = 0.010) as shown in Figure 5.1. This indicates that business people have greater faith in a commercial type of NTO-organization to be market-focused than a non-profit one, even if it is industry-led.

NTA respondents (government), surprisingly, appear to be somewhat more convinced that industry ownership would benefit Market Focus than the two other groups (e.g., NTA (mean score **5.33**) vs. NTO (mean score **4.87**); sig. = 0.079). This may indicate that

NTAs consider that NTOs, as NTOs are usually government-controlled as of today, need stronger industry representation/control in order to become more market-focused. It may also indicate that NTAs in general are not entirely satisfied with NTOs' current focus.

Figure 5.1

### Differences between NTA, NTO, and Industry in evaluations of the effect of Ownership on Market Focus



#### 5.3.3 Effects on long-term perspective

A scale of Long-Term Perspective was measured<sup>32</sup> as the mean (on a scale from 1-7) of the following measures:

- Long-term perspective in plans and activities
- Problems with planning due to insufficient funds for the budgets
- Difficulties to pursue long-term goals
- Lead to improved long-term performance

The second and third measures were re-scaled (inverted). In the following paragraphs we will discuss how *budgeting*, *funding source* and *ownership/control* relate to Long-Term Perspective.

<sup>32</sup> The items were factor analyzed and were found to correlate highly with one factor (see Appendix 3)

### 5.3.3.1 Effects of budgeting principles on long-term perspective

Long-Term Perspective implies that plans and activities are carried out with long-term objectives in mind. It also implies that there should not be too much short-term budget squeezes that long-term objectives should not be too difficult to pursue. Long-Term Perspective thus both reflect the attitude toward and the ability to plan ahead.

#### *High scores*

##### **Theory experts' sample:**

The two highest scoring budgeting principles in terms of Long-Term Perspective were both performance-based principles. Assuming that NTOs are in fact able to influence their market performance from one year to another, and with a market performance-based budgeting principle in place, that would give NTOs some control of their future income flows. Again, this would assume the ability to transfer funds from one budget year to another. Like many commercial corporations NTOs could then generate reserves during good years to set aside for use in more difficult future periods. Generated reserve funds from periods of high market performance could also allow NTOs to engage in projects and activities of a more long-term character, which could extend NTOs' planning horizons in time. The budgeting principles with the highest scores were:

- *P7: Budget based on the revenue generated from taxation on visitors and the traveling public (4.63; 1.10)*
- *P2: Budget based on the increase/decrease in the amount of money spent by incoming tourists (international tourism receipts) relative to "comparable" countries (4.29; 0.58)*
- *P5: Budgets based on a fixed sum decided each year (4.26; 1.06)*

The third ranked alternative is P5, and different in principle than P7 and P2. Budgets based on a "fixed-sum-negotiated-each-year"-principle would provide a steady base of income (given that the budget would not be fluctuating considerably from one year to another). Reasonable certainty of the budget size in the future could also allow NTOs to get into long-term engagements and plan activities for several years ahead.

From a theoretical standpoint, a combination of the two types of principles would be ideal. We will discuss this in more detail in the recommendations chapter (Chapter 6). According to the theory experts' ranking of budgeting principles, the experts' data seem to support this idea.

##### **Practitioners' sample:**

Except for P4, none of the budgeting principles positively related to Market Focus by the practitioners were found to have the same impact on Long-Term Perspective. The three budgeting principles found to have the most positive impact on Long-Term Perspective were the following:

- *P5: Budget based on a fixed sum decided each year (4.42; 1.11)*

- *P7: Budget based on the revenue generated from taxation on visitors and the traveling public (4.07; 1.11)*
- *P4: Budget based on evaluation of the NTO's marketing plans each year (4.00; 1.47)*

We can identify two principles that contribute to Long-Term Perspective and at the same time “make sense” from a theoretical standpoint, as well as from the comments made in the focus groups. One is P5 (*fixed sum negotiated each year*). The other principle with a high positive impact is P7 (*taxation of visitors*). The fact that the “fixed-sum-negotiated-each-year”-principle (P5) is evaluated to affect Long-Term Perspective positively probably reflects what many of our respondents underscored: that the yearly negotiations were of a formal nature, and that the amount fixed tended to be quite invariant from year to year. Consequently, the budget size is fairly predictable from one year to another, which could make long-term planning relatively easy. The fact that P7 also contributes positively probably reflects the assumption that taxes, once they are introduced, rarely disappear - and thus perceived to remain a fairly stable source of income.

Why P4 *Budgets based on evaluation of the NTO's marketing plans each year* ranked as high as number three is a bit more difficult to explain. In fact, this principle is ranked the lowest among our theory experts (see below). However, in cases where the NTO is granted autonomy to financially commit to long-term plans, and can relatively easily get approval for long-term plans in the budgeting committee, *budgeting based on marketing plans* can in some instances be beneficial for NTOs' Long-Term Perspective.

#### *Low scores*

#### **Theory experts' sample:**

The two lowest scoring alternatives among our theory experts' evaluations are both typically behavior-based type of principles:

- *P4: Budget based on evaluation of the NTO's marketing plans each year (3.62; 0.72)*
- *P6: Budget based on achievement of goals and objectives decided each year (3.88; 0.81)*

In theory, a budgeting process where NTO managements will have to gain approval of plans from one year to another and face the risk of having plans disapproved by the financing stakeholders, would not ease the long-term planning scheme. Marketing plans and goals subject to approval and change every single year could preclude the ability and incentives for NTOs to adopt a Long-Term Perspective. A negotiating process regarding the financing of NTOs' marketing plans and activities, involving (several) governing stakeholders and NTOs', could require considerable lobbying effort on the part of NTOs in order to secure their interests. Furthermore, it would require competence and insight in NTO matters on the part of the stakeholders in order to effectively evaluate NTOs' marketing plans, and set sane long-term goals and short-term objectives for NTOs. For such a budgeting principle to be beneficial for Long-Term Perspective one would have to

assume that NTOs have the ability and motivation to develop long-term plans and gain budget approval.

#### **Practitioners' sample:**

Budgets based on *sale of specific projects* are considered by our practitioner respondents as an unstable source of funding, as they expressed it in the focus groups. This is also the principle that gets the least positive evaluation with respect to Long-Term Perspective:

- *P3: Budget based on sale and participation in specific projects (3.41; 1.18)*
- *P1: Budget based on the amount of money spent by incoming visitors the previous year (3.64; 1.13)*
- *P2: Budgets based on the increase/decrease in the amount of money spent by incoming tourists relative to "comparable" countries (3.75; 1.09)*

Budgeting principles that are subject to changes from year to year as a consequence of changes in number of visitors and their travel expenditures are believed to be an obstacle to long-term planning and operation. On this aspect there seem to be some disagreement between the theoreticians and the practitioners. The theory experts score performance-based principles (P1 and P2) high, while the practitioners do the opposite and score the same principles among the lowest. The practitioners' skepticism to performance-based budgeting can also reflect the inability for most NTOs to transfer budget funds from one year to another under current practice.

### **5.3.3.2 Effects of funding source on long-term perspective**

#### *High and low scores*

#### **Theory experts' sample:**

Among our theory experts' evaluations it was not possible to distinguish between the *funding source*-principles with respect on their impact on Long-Term Perspective. *Government funding (4.15; 0.81)* scored only slightly better than *Joint funding (3.94; 0.46)*, and *industry funding (3.92; 0.96)*. In theory, one can argue that the industry's ability and willingness to fund NTOs could change as a result of the general profitability of the industry. One could then argue that government sources would provide a more stable source of income, since the government is more able to handle fluctuations in revenues rather than a coalition of businesses dependent on one single industry's performance. However, governments sometimes make seemingly arbitrarily cuts in NTOs' budgets. These cuts can come as a result of changes in political power or priorities of political character, rather than strategically from an economical or business perspective. So one could argue both ways, both the industry and the government could in theory be unstable as a source of income. The results of evaluations may reflect this dilemma, since they show that both the theorists and practitioners have difficulties to identify a "best" or "worst" source of income related to Long-Term Perspective.

*Joint funding* seems to be the better alternative from a theoretical point of view, leaving the NTO with two sources to depend on rather than one only. However, this alternative still fails to score significantly better than the two others, at least with our theory experts.

**Practitioners' sample:**

In our practitioners' sample *joint funding* (4.05; 1.23) scored slightly better than *government funding* (3.86; 1.28) with respect to its relationship to Long-Term Perspective.

*Industry funding* (3.62; 1.17) scored significantly lower than the *combined funding* alternative. It should be noted that our practitioner respondents expressed through some of the itemized data and comments in the focus groups that they are concerned that industry funding alone would not provide the NTO with enough funds, and that will make it more difficult for the NTO to initiate long-term planning and engagements. *Combined funding*, with contributions from at least two different sources, could reduce such a problem.

Overall based on the evaluation of both respondent groups, we cannot conclude that funding source could be expected to have a strong impact on Long-Term Perspective. In other words, it does not matter that much where the money comes from in regards to NTOs' propensity to engage in long-term planning and activities. However, in both groups there is a (weak) tendency to disregard the industry as a source for funding the NTO seen in relation to a long-term perspective. *Industry funding* is ranked lowest of the three alternatives by both groups.

### 5.3.3.3 Effects of ownership on long-term perspective

#### *High and low scores*

**Theory experts' sample:**

There are only small and non-significant differences in how the different ownership alternatives are evaluated by the theory experts. NTO organized as a commercial *limited corporation* scores the highest (4.14; 0.73), but *government ownership* (4.02; 0.71), and *industry ownership* (3.88; 0.89) score just a little lower. As in the case with funding source related to its impact on Long-Term Perspective, one could argue both ways theoretically with respect to ownership/organizational control of NTOs. On one hand, industry ownership may pressure the NTO to focus on short-term market results on the expense of a more long-term based strategy, since the industry is probably more dependent on short-term income from tourism sales. In other words, the industry would need market results fast, and may not want to wait for market performance in e.g., five years ahead in time. One could probably expect the government to be able to commit to more long-term engagements than the industry. For instance, a commercial type NTO could be under pressure from shareowners to produce short-term results. On the other hand, potentially constantly changing political power coalitions and their priorities within the government bureaucracy can change how a government-controlled NTO is governed, and that could hamper the NTO's ability to plan and operate on a long-term basis. From a theoretical perspective it can thus be somewhat difficult to judge whether *industry, government, or commercial ownership* is preferable in terms of the NTO's Long-Term Perspective. The evaluations seem to reflect that, since no single one of the ownership alternatives seem to be evaluated as significantly better than the other two.

**Practitioners' sample:**

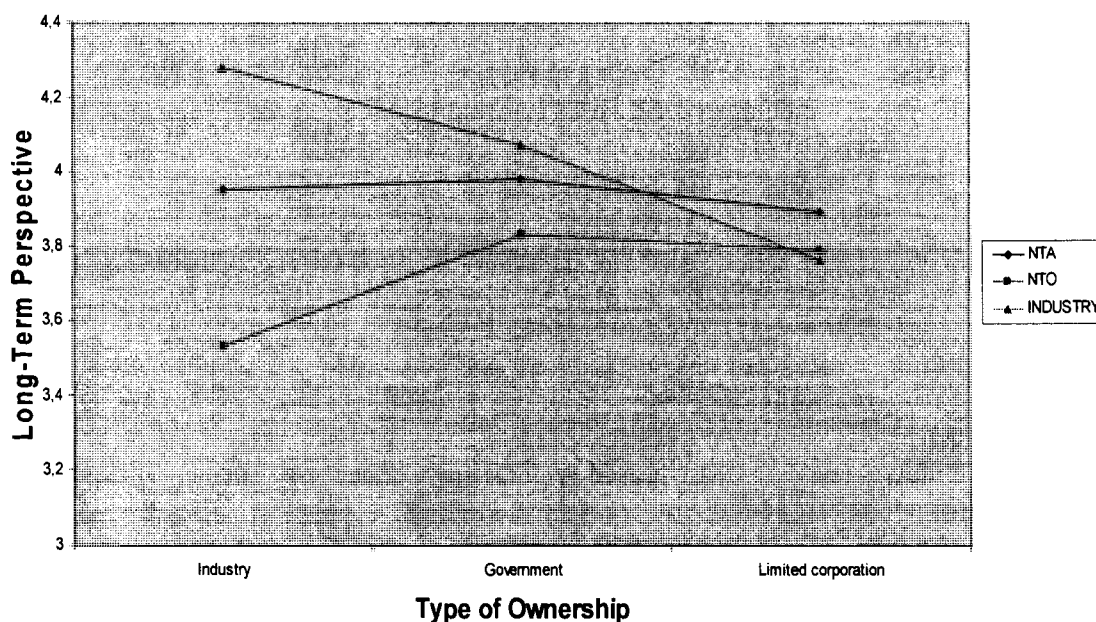
Also the practitioner respondents seen as an overall sample seem to believe that *ownership/organizational control* has little bearing on the NTO's willingness or ability to plan ahead and operate on a long-term basis. *Government ownership* scores the highest (3.91; 1.28), while *industry ownership* (3.85; 1.15) and *limited corporation* (3.79; 1.25) score marginally lower.

**Differences in evaluations between various practitioner respondent-types:**

Some differences can be found in between the sub-groups' evaluations of the effect of P8 (*taxation on the industry*) on Long-Term Perspective (NTO (mean score 3.44) vs. Industry (mean score 4.67); sig. = 0.050). This is somewhat surprising, since P8 would constitute an extra tax-burden on the industry. The different practitioner respondent-types also differ on one aspect in their view on the effect of *ownership* on Long-Term Perspective, as shown in Figure 5.2:

**Figure 5.2**

**Differences between NTA, NTO and Industry in evaluation of the effect of Ownership on Long-Term Perspective**



Participants from the industry view *industry ownership* as more positive for Long-Term Perspective than NTO representatives (NTO (mean score 3.53) vs. Industry (mean score 4.28); sig. = 0.050).

For instance, one could speculate that NTOs have had experiences with industry engagements that have been of a more short-term character than desirable. This idea is in line with the findings of a 1999 European Tourism Committee (European joint organization of NTOs) survey we will discuss later in this section (5.3.5).

### 5.3.4 Effects on operational freedom

Operational Freedom refers to the degree to which the NTO can make independent decisions without consideration of political issues and pressures from special interests. A scale of Operational Freedom was constructed<sup>33</sup> as the mean (on a scale from 1-7) of the following items:

- Will (not) make the NTO over-prioritize special interest
- Will (not) make the NTO spend too much resources on sale of services to the industry
- Will not make the budget fluctuate so much that it restricts NTO's ability to operate
- Will give the freedom to make its own decisions

The scale is thus intended to reflect the degree to which the respondents believe that a certain principle will reduce undue interference from groups and considerations external to the organization. It also considers NTO's incentives for prioritizing special interests, and creating a budget situation limiting the NTOs freedom to act.

#### 5.3.4.1 Budgeting principles' effects on operational freedom

##### *High scores*

##### **Theory experts' sample:**

Our theory experts are in general positive to the two types of taxation as means for funding the NTO. P7 and P8 are both indirectly tied to performance, since the NTOs' income would depend on the level of tourism generated taxes. These taxes are again dependent on the level of tourism traffic.

- *P7: Budget based on the revenue generated from taxation on visitors and the traveling public (5.40; 0.94)*
- *P5: Budget based on a fixed sum decided each year (4.75; 0.75)*
- *P8: Budget based on the revenue generated from taxation on the travel and tourism industry (4.47; 1.12)*

In theory, budgets based on taxes should provide the NTO a fairly high degree of desirable independence from its governing stakeholders. In terms of financing there is little incentive for NTOs to lobby stakeholders to secure funding under a tax-based budgeting principle. It would also give NTOs desirable autonomy, since stakeholders cannot pressure the NTO to focus on special interests through the budgeting process. We had also expected that performance-based budgeting principles would be evaluated to be positive for Operational Freedom, because it would give stakeholders less need to monitor NTOs' activities and intervene in NTOs' operation as discussed in Section 2.5.4. So the evaluation given by the theorists is therefore not surprising; given that type of theoretical of reasoning.

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<sup>33</sup> The items were factor analyzed and were found to load highly on one factor (see Appendix 3).



P5 (*a fixed sum decided each year*) should also give some budgetary room for autonomy as well, given that the budgeting process does not involve extensive negotiations as a part of the yearly budget determination.

**Practitioners' sample:**

According to our analyses of the practitioners' sample, there are two budgeting principles clearly identifiable with a strong positive impact on Operational Freedom. The most positive principles are: *budgets based on a fixed sum*, and *taxation of visitors*. Thus, on this aspect the theorists' and practitioners' evaluations concur to some extent, *performance-based-* and *fixed sum budgeting* seems attractive to both groups.

- P5: *Budgets based on a fixed sum decided each year (4.79; 1.26)*
- P7: *Budgets based on the revenue generated from taxation on visitors and the traveling public (4.41; 0.96)*

*Low scores*

**Theory experts' sample & Practitioners' sample:**

The less positive impact of P3 (*sale of specific projects*) is more pronounced. According to both groups of respondents, the budgeting principle which distinguishes itself as the least positive for NTOs' Operational Freedom is P3 (*budgets based on sales of projects*) (theory experts: **3.03**; 0.52) (practitioners: **2.88**; 1.10). From a theoretical viewpoint, this is not surprising either. An NTO solely dependent on sale of projects to secure funding may be forced to sell or accept to do projects that are not according to their overall marketing strategy. Sale of projects can force the NTO to over-focus on sponsors' special interest.

### 5.3.4.2 Funding source's effects on operational freedom

*High and low scores*

**Theory experts' sample:**

The evaluations done by the theory experts show that *funding by the government (4.61; 0.97)* seems to provide the best conditions for NTOs' Operational Freedom. *Joint funding (4.02; 1.10)* scores second best, while *industry funding (3.35; 1.02)* is evaluated to be the least positive.

In theory, one could argue that government funding would give NTOs more desirable independence than if the funding coalition was made up by industry actors. The reason is that the government could be a more "passive and neutral" financier than the industry, providing the NTOs with more autonomy. Strong and dominating members of an industry funding coalition (e.g., a major airline company, or a casino chain) could pressure NTOs to focus on their special interests on the expense of the industry and stakeholders in general in return for money contributed to NTOs' budgets (e.g., refer to the WHO-case discussed in Section 2.5.1)

**Practitioners' sample:**

Also on this issue the practitioners are in agreement with the theory experts. The practitioners express that *government funding* (4.12; 1.28) is the most positive alternative with regards to NTOs' Operational Freedom. This alternative is considered better than the two other ones. *Joint funding* (3.73; 1.26) scores second best. *Industry funding* (3.35; 1.02) is viewed as the least positive on this aspect, and significantly worse than the two other alternative sources.

### 5.3.4.3 Ownership's effects on operational freedom

#### *High and low scores*

##### **Theory experts' sample:**

With regards to *ownership* the picture is similar. The theorists view *government ownership* (4.32; 1.13) as slightly better NTOs' Operational Freedom than ownership through a *limited corporation* (4.17; 1.12). The least positively evaluated alternative is *ownership by the industry* (3.36; 1.08). Why *government ownership* is evaluated more positively than *industry ownership* could be explained by the notion that dominating industry representatives in NTO boards may put pressure on NTOs to act as the industry wants or to focus on special interests, which may not be in accordance to NTOs' marketing strategy (refer also to the ETC-study later in this section).

##### **Practitioners' sample:**

*Government ownership* (4.12; 1.33) is evaluated by the practitioners to have the most positive impact on Operational Freedom as well, and is considered better than the two other alternative ownership arrangements. Both the NTO under *industry ownership* (3.59; 1.24) or organized as a *limited corporation* (3.36; 1.20) are perceived to be less positive for NTOs' Operational Freedom. From studying the itemized data it appears that the *limited corporation*-alternative scores low particularly because the respondents believe a profit-maximizing version of an NTO will be too much engaged in selling its services and over-prioritizing of special interest groups among the share owners. Some respondents were concerned that a commercial NTO organized as a limited corporation would be forced by its (presumably) profit-maximizing owners to act to maximize (short-term) profits on the expense of the interests of the whole national tourism industry.

Opposite of the case with Market Focus, the analysis of the practitioners' scenario scores reveals that scenarios containing *industry funding* combined with *industry ownership* (3.39; 1.13) are considered inferior to scenarios with *government funding* combined with *government ownership* (4.33; 1.31) in terms of perceived positive effect for Operational Freedom. So aspect the current regime is considered better than the other alternatives by our practitioners. The theory experts agree with the practitioners in this matter, and they favor *government* to the two others when considering the combinations of funding source and ownership.

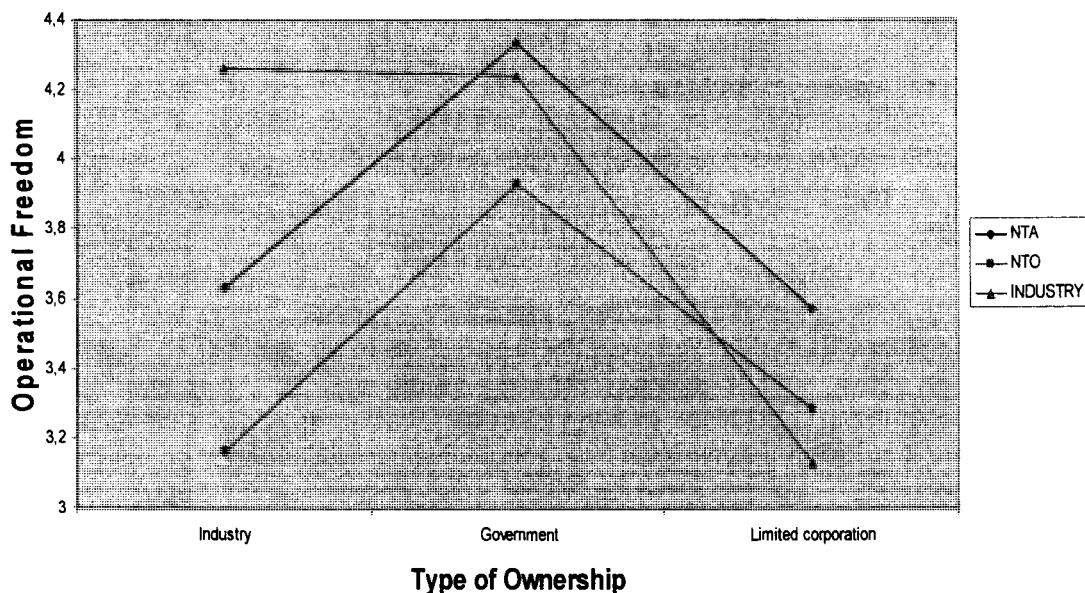
##### **Differences in evaluations between various practitioner respondent-types:**

Considering differences between the three respondent types among the practitioners, we find that the industry representatives are more positive to *taxation on the industry* in terms of NTOs' Operational Freedom (NTO (mean score 3.22) vs. Industry (mean score

4.27); sig. = 0.032). Interestingly, the NTO representatives are more skeptical to *government funding* than the NTA representatives (NTO (mean score **2.86**, NB! a very low score) vs. NTA (mean score **3.39**); sig. = 0.032). It may be so that the NTO representatives have experienced financing difficulties in dealing with the government perceived to have curbed NTOs' Operational Freedom. We can also see from the chart in Figure 5.3 that the industry representatives are far more positive to an *industry-led* organization than the NTO (NTO (mean score **3.16**) vs. Industry (mean score **4.26**); sig. = 0.027), and partially the NTA representatives (NTA (mean score **3.63**) vs. Industry: sig. = 0.19).

Figure 5.3

### Differences in evaluations between NTA, NTO and Industry about the effect of Ownership on Operational Freedom



The industry respondents themselves give systematically higher scores to the industry ownership alternative with respect to Operational Freedom, while the NTO- and NTA-representatives (predominantly government employees) have more faith in government/public ownership of NTOs. This is not really surprising either.

Another finding from the itemized data<sup>34</sup> is that the practitioner respondents believe that *industry funding* (5.05; 1.72), or *combined funding* (4.60; 1.61) is significantly better than pure *government funding* (2.94; 1.67) in terms of increasing the commitment and interest

<sup>34</sup> In this case we refer to one of the items (# 14) deleted from further analysis after the factor analysis, i. e., that the item was not included in any of the three dependent variables (see also Appendix 3 for details of the factor analysis).

of the travel and tourism industry in the work of the NTO. We see the same pattern in terms of ownership: *Industry ownership/control* scores significantly higher (5.03; 1.67) than *government ownership/control* (3.26; 1.77). *Limited corporation ownership/control* (4.20; 1.84) is regarded as second best in that respect, and also better than *government ownership*. So one can conclude that industry participation in funding and ownership is needed to make the travel and tourism industry seriously committed and interested in NTOs' operation and activities. This is also a question of NTOs' legitimacy in the eyes of the industry. The industry would probably have far less interest in NTOs when they are operating as a government entity, than if the industry can participate in the funding of NTOs and influence their activities through e.g., monetary contributions and board representation.

The itemized data also show an identical pattern on another item<sup>35</sup>. This item probed if the scenario in question would cause a negative reaction from the travel and tourism industry. *Government funding and ownership* scored far less favorable than *industry funding and ownership* on this item. It indicates that the pure government ownership and funding would be perceived as the least positive alternative by the travel and tourism industry in general. This is also in line with what we found when analyzing differences in evaluations between different practitioners' respondent sub-groups (NTO, NTA and Industry) as shown in Figures 5.2 and 5.3.

### 5.3.5 Conclusions from scenario evaluations

Overall, the theory experts' evaluations concur well with what could be expected from a theoretical standpoint as outlined in Chapters 2 and 3. In other words, there is in general a high level of agreement between the conclusions from the theory review and the corresponding conclusions derived from the theorists' scenario evaluations. We believe this is positive for the sake of our study, since the results from the experts' evaluations can then contribute to validate the findings from the theory chapter and vice versa. Furthermore, it indicates that we have been reasonably successful in the process of "quantifying theory"; and then converted it into a format such that the theoretical manifestations can be compared directly with the empirical data from our practitioners' evaluations. These evaluations are the extensions of the practitioners' *espoused theories*, as explained in Chapter 1.

With regards to the practitioners' evaluations, the results for the individual national groups are more clear-cut than the ones obtained for all groups in the whole sample combined. This finding reflects the fact that although we instructed our respondents to free themselves as much as possible from the context of their own NTO, the setting and experience with the national NTOs provide a contextual frame for responding to the various scenarios. This leads to considerable heterogeneity in the way respondents from different countries perceive a given principle (see also Section 5.3.6.1 for statistical details). The perceptual differences between members of different national samples probably imply that the pursuit of one system that is optimal for all countries may be futile. In the same manner, there are some differences in how representatives from the

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<sup>35</sup> This item (# 11) was also removed after the factor analysis.

NTO, NTA and the industry view the effects of the various *ownership* alternatives. This fact also contributes to the heterogeneity in how the various principles are evaluated. For instance, most of the differences stem from variations in how the *ownership/control* variable is evaluated by the three respondent sub-groups. It may partially explain why this variable has low F-values and low significance levels, as shown in Table 5.4 in Section 5.1.

The between-subject heterogeneity in the practitioner's sample, both with respect to national origin and organizational background, will contribute to a central tendency in the data. That is making it somewhat harder to significantly differentiate between how the various principles are evaluated in the practitioners' sample. We will go into more detail about these challenges in Chapter 7 (Section 7.2).

However, some of the findings appear to be generalizable, and we will discuss the conclusions that seem to be generally valid in the following paragraphs.

#### *The value of performance-based budgeting principles*

Based on the practitioners' evaluations, two of the performance-based principles get positive evaluations both in terms of their impact on Market Focus as well as their effect on Operational Freedom. The two most positively evaluated performance-based principles imply that NTOs' budgets should be linked to the direct economic value of incoming tourism. The two principles differ with respect to whether they emphasize relative performance (P2) or absolute performance (P1). Foremost, these two performance-based principles provide an incentive for a stronger Market Focus since the budgets of NTOs will depend on what NTOs achieve in the marketplace, and not only on the goodwill and discretion of the financing stakeholders. Conversely, the behavior-based principles will not provide such incentives, and are thus evaluated less positive in that respect. This finding is supported by the results from the theory experts' corresponding scenario evaluations, as well as recommendations from the theory review.

In terms of taxes as a financing alternative, generally, taxes go into a general revenue fund neither channeled back to the industry, nor is it directly identified with the industry at the time of collection. Some practitioner respondents may be concerned, as mentioned in some focus groups, that the revenue from a tourism-tax that is supposed to be dedicated to finance NTOs will not be fully used for that purpose, and for the most part used to finance other government expenses. If this would be the situation, taxes would not provide a strong incentive for NTOs' Market Focus, since the tax revenue would have little impact on NTOs' budgets. This may be one of the reasons why the practitioner respondents are less convinced of the virtue of performance-based principles linked to tax revenues than the theory experts, who are less concerned with political obstacles in their evaluations in principle. We interpret these findings as evidence that an increased tax burden is considered an evil by the practitioners, regardless of the potential incentive effect on NTOs. Our theory experts, however, are not sharing this idea, and evaluate tax positively in concordance with a theoretical argument that taxes should have incentive value as an indirect performance-based principle.

It is also interesting that the positive impact ascribed to performance-based principles as far as their impact on Market Focus and Operational Freedom is concerned, does not apply to Long -Term Perspective. In fact, both P1 and P2 receive low scores in the practitioners' sample in terms of their impact on Long-Term Perspective.

We believe there are several reasons for this skepticism: One concern may be that the budgetary mechanism is believed to result in fluctuating budgets. It is understandable that if NTOs' managements perceive that the future budget situation is very unpredictable due to potentially heavily fluctuating future budgets, it will be hard to commit the NTO to long-term engagements. This may very well be the outcome of applying a principle that links revenues to market performance. However, to the extent that such fluctuations are considered undesirable, a performance-based mechanism should motivate the organization to counteract these fluctuations. This motivating effect is the very reason why this type of principle is suggested as an alternative to existing practice. The theory experts support this idea through their scenario evaluations; they mean that performance-based principles in fact can be beneficial NTOs' for Long-Term Perspective.

If NTOs were allowed to transfer some of the economic resources attained in prosperous years to reserve-funds accounts for use when market conditions are more difficult, it would probably promote long-term thinking on the part of NTOs. A potential practical problem is that, should NTOs be funded by government sponsors, it is not sure this would be agreed to in practice, as it may be contrary to general public funding policy.

Another objection expressed by some of the practitioner respondents against performance-based principles was that it would be difficult to accurately estimate the value of tourism as a performance measure. We do not believe this constitutes a real problem. The *Tourism Satellite Account*-system adopted by the OECD, WTO, and UN, and already in use in many of our respondent countries, should allow reliable estimates to be used for this purpose.

A third concern expressed by some of our practitioner respondents was that revenues tied to market fluctuations would be "unfair" since the NTO only can be made responsible for a limited part of the changes, and the NTO is not usually directly involved in the commercial "sale". We agree that increases in NTO revenues that follow from market changes may not necessarily be "fair" in the sense that they will accurately reflect the level of effort or dexterity (or lack thereof) of the NTO. However, "fairness" is not what characterizes the marketplace for most commercial organizations either. Service operations as well as manufacturing companies will in general be rewarded or punished in the marketplace by events for which they may not be entirely responsible. For instance, an oil company has only limited- to no control over the fluctuating spot-market price of crude oil, fluctuations which may impact the company's profits significantly. The best a company can do is to exploit favorable events and to counter harmful ones and to maximize the value of benign conditions, while at the same time limiting negative consequences.

One argument in favor of using some type of performance-based principle is that the entire budget may not necessarily be made contingent on performance. The application of

a performance-based budgeting principle does not preclude that some part of the budget amount is held fixed. For example, fixed cost of the NTO's operation would be covered by the fixed portion of the budget, while variable cost would be tied to performance measures (see Section 2.4.5.3 for details).

#### *The consequences of revenues based on sale of projects*

The *sale of projects* is the second-most common budgetary mechanism in current practice. Many NTOs base at least some part of their budgets on project sales. We encountered very different reactions to the idea that part of NTOs' revenues can be based on the sale of projects to the private industry. Some of the respondents were opposed to the idea that e.g., government funding should be made provisional on income generated from sale of projects. A matching principle that makes it mandatory for NTOs to generate sales revenues can easily lead to sub-optimal solutions if the projects are initiated for pecuniary reasons and not as an implementation of a general market strategy. Budget principles based on the sale of projects would also make the budget situation unpredictable, which could inhibit long-term planning. Furthermore, project financiers could demand decision power on NTOs' activities in return for project funds, which is not positive for NTOs' Operational Freedom. It requires a strong professional organization and a proactive role to ascertain that projects sold to partners in the industry in fact satisfy the requirements posed by NTOs' long-term strategies.

#### *Arbitrarily determined budgets and behavior-based principles*

In many countries it appears that NTOs' budgets are neither performance-based nor formally tied to the execution of formal marketing plans or set objectives that have been approved by the funding stakeholders and/or owner entity in advance. In most countries the budgets are formally determined each year, but are not subject to considerable variations from one year to another. In one country, Denmark, the budget period is three years. A system in which budgets do not vary considerably, and are not based on activity/behavior control mechanisms, allows Long-Term Perspective and Operational Freedom, but inherently provides no incentives to promote Market Focus. This may be why many practitioner respondents evaluate fixed budgets as positive on those two first dimensions. However, if budgets are cut arbitrarily from one year to another, for instance as a result of changing political coalitions or priorities, this will neither be good for NTOs' Long-Term Perspective and Operational Freedom. The NTOs will have little control of their future budgets, and cannot easily plan ahead. Lobbying activity and justification efforts will probably be necessary to secure sufficient long-term funding.

#### *Do source of revenue and ownership matter?*

With respect to the effect on Market Focus, *industry funding* scores better than *funding from government* sources. In fact this finding is in concordance with the results of the separate data collection reported in Appendix 7. The higher proportion of industry funding, the more market-focused the NTO is evaluated to be; and the higher proportion of government funding, the less market-focused the NTO is evaluated to be.

This type of industry-based funding may have both advantages and disadvantages: In a ETC (European Travel Commission) survey the respondents expressed that funding from the private industry may affect NTOs' Operational Freedom<sup>36</sup>. As many as 50% of member NTOs surveyed agreed (41% disagreed) that they were under pressure from the private sector to do as the private sector wishes as a result of private sector contribution to NTOs' funding. Another 59% agree (27% disagree) that a reduction in public funding will weaken the strategic freedom to act.

At the same time, 55% of member countries surveyed in the ETC study agreed that closer cooperation with the private sector has resulted in a substantial increase in their NTO budgets. A majority of 45% agree that the cost of efforts to obtain greater funding from the private sector is in a sensible relationship to income produced (32% disagree).

It is also possible that our NTO respondents may have experienced the same as most of the ETC respondents: In the ETC survey 90% (!) of respondents agree (5% disagree) that greater cooperation with the private sector has resulted in greater independence in the relationship with the government. Thus, *combined funding* seems to be the best alternative judging from the ETC survey. Our respondents agree with that, but more with respect to the positive impact of *combined funding* on Market Focus than on Operational Freedom.

In general, the respondents appear to be skeptical to the government both as single source of income and as the only "owner". Both pure *government funding* and *government ownership* are clearly perceived to be less positive for NTOs' Market Focus, while pure *industry funding and ownership* is considered more positive. It is interesting that the first listed set-up is quite similar to the current regime in most countries. With respect to the current system, our respondents consider it to be less than optimal for achieving an NTO that is market-focused. On the other hand, the results from the scenario evaluations are not that clear with respect to *funding* and *ownership*-effects on NTOs' Long-Term Operation. In terms of the impact of *funding source and ownership* on NTOs' Operational Freedom, *government funding and ownership* is evaluated positively, while industry funding and ownership is considered to be less positive. The commercial type of NTO in the form of a *limited corporation* is evaluated to be positive for Market Focus, but at the same time less positive for Long-Term Operation and Operational Freedom. Overall, the *limited corporation*-option comes out quite weak as our respondents evaluate it.

Our industry respondents are more positive to the *limited corporation*, *industry funding*, and *industry ownership* alternatives than their counterparts in the NTOs and NTAs, reflecting influence from the industry representatives' private/commercial background.

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<sup>36</sup> ETC Member Survey, spring 1999 (22 of 29 European member NTOs participated).



**Table 5.8**  
**Theory experts' sample: Summary of scenario evaluation results**

<b>Estimated Effects</b>	<b>Principles</b>	<b>Most positive</b>	<b>Least positive</b>	<b>Differences between theory experts' (Table 5.8) &amp; practitioners' evaluations (Tbl. 5.9)</b>
<b>Market Focus</b>	<b>Budgeting Principle</b>	<b>Estimates of amount of money spent by visitors</b> (Significantly higher than 1 out of 7 other principles)	<b>Fixed sum</b> (Significantly lower than 2 out of 7 other principles)	Theory experts give higher scores to <i>industry taxation</i> (P7) and lower scores to <i>budgeting based on evaluation of marketing plans</i> (P4) than practitioners reps.
	<b>Funding Source</b>	<b>(Industry)</b> (Only significantly higher than <i>joint funding</i> on p<0.10 level)	<b>(Joint funding)</b> (Only significantly lower than <i>industry funding</i> on p<0.10 level)	Government funding is considered somewhat less positive by the practitioners than by the theory experts.
	<b>Ownership/control</b>	<b>(Industry)</b> (Scores higher, but not significantly better than the two other principles)	<b>(Government)</b> (Scores lowest but not significantly lower than both others)	No significant differences.
<b>Long -Term Perspective</b>	<b>Budgeting Principle</b>	<b>Taxation of visitors</b> (Only significantly better than 1 out of 7 other principles on p<0.15 level)	<b>Evaluation of marketing plans</b> (Only significantly worse than 1 out of 7 other principles on p<0.15 level)	Theory experts are far more favorable to <i>performance-based principles</i> , and less favorable to <i>evaluation of marketing plans</i> (P4) than the practitioners.
	<b>Funding Source</b>	<b>(Government)</b> (Scores highest, but not significantly better than two other principles)	<b>(Industry)</b> (Scores lowest, but not significantly lower than two other principles)	No significant differences.
	<b>Ownership/control</b>	<b>(Limited corp.)</b> (Scores highest, but not significantly better than the two other principles)	<b>(Industry)</b> (Scores lowest, but not significantly lower than the two other principles)	Theory experts slightly more favorable to <i>limited corporation</i> , and less favorable to <i>govt. funding</i> than the practitioners.
<b>Operational Freedom</b>	<b>Budgeting Principle</b>	<b>Taxation of visitors</b> (Significantly higher than 3 out of 7 other principles)	<b>Specific projects</b> (Significantly lower than 3 out of 7 other principles)	Practitioners are more skeptical to <i>performance-based principles</i> than the theory experts.
	<b>Funding Source</b>	<b>Government</b> (Significantly higher than <i>industry funding</i> )	<b>Industry</b> (Significantly lower than <i>government funding</i> )	No significant differences.
	<b>Ownership/control</b>	<b>Government</b> (Significantly higher than <i>industry funding</i> )	<b>Industry</b> (Significantly lower than <i>government funding</i> )	Theory experts are more favorable to <i>limited corporation</i> than the practitioners.

**Table 5.9**  
**Practitioners' international sample: Summary of scenario evaluation results**

<b>Estimated Effects</b>	<b>Principles</b>	<b>Most positive</b>	<b>Least positive</b>	<b>Differences in evaluations of NTA, NTO and Industry reps.</b>
<b>Market Focus</b>	<b>Budgeting Principle</b>	<i>Amount of money spent by visitors relative to comparable countries</i> (Significantly higher than 3 out of 7 other principles)	<i>Taxation on visitors</i> (Significantly lower than 6 out of 7 other principles)  <i>(Fixed sum)</i>	Industry representatives give systematically higher scores to both <i>industry taxation</i> (P7) and <i>visitor taxation</i> (P8) than NTA and NTO representatives.
	<b>Funding Source</b>	(no clear "best" altern.) (Both <i>industry</i> and <i>joint funding</i> score about equally)	<b>Government funding</b> (Significantly lower than both others)	No significant differences.
	<b>Ownership/control</b>	<b>(Industry)</b> (Industry scores significantly higher than Limited Co. on p<0.10 level)	<b>Government</b> (Significantly lower than both others)	Industry representatives give systematically higher scores to <i>limited corporation control</i> .
<b>Long -Term Perspective</b>	<b>Budgeting Principle</b>	<b>Fixed Sum</b> (Significantly higher than 6 out of 7 other principles)	<b>Specific projects</b> (Significantly lower than 5 out of 7 other principles)	No significant differences.
	<b>Funding Source</b>	<b>Joint funding</b> (Significantly better than industry funding)	<b>(Industry)</b> ( <i>Industry funding</i> scores somewhat weaker than <i>gov. fund.</i> )	No significant differences.
	<b>Ownership/control</b>	(no clear "best" alternative) (All owner alternatives score about equally)	(no clear "worst" alternative) (All owner alternatives score about equally)	NTO representatives are more skeptical of the <i>industry</i> as owner than the others.
<b>Operational Freedom</b>	<b>Budgeting Principle</b>	<b>Fixed Sum</b> (Significantly better than 6 out of 7 other principles)	<b>Specific Projects</b> (Significantly worse than 7 out of 7 other principles.)	No significant differences.
	<b>Funding Source</b>	<b>Government</b> (Significantly higher than both others)	<b>Industry</b> (Significantly lower than both others)	No significant differences.
	<b>Ownership/control</b>	<b>Government</b> (Significantly higher than both others)	(no clear "worst" alternative) ( <i>Industry ownership</i> and <i>limited corporation</i> score about equally)	Industry representatives give systematically higher scores to <i>industry ownership</i> than NTO representatives.

In conclusion, a well-balanced combination of industry and government both as “owners” and sources of income appears to be more acceptable. This is also in line with our theory discussion in Section 2.4.1. However, NTOs’ operation and performance is also dependent on an industry that is able to be market-focused, have a long-term perspective, quality-minded and otherwise professional. As one of the Canadian group members expressed it: “As long as the client [user/buyer/beneficiary of NTO’s services] is professional it does not matter whether it [NTO] is a private firm or a state agency.”

### 5.3.6 Gap-analysis

As outlined in the research design section and illustrated in Figure 1.2 in Chapter 1, we have stated an interest in investigating any potential mismatches between theory and practice in the NTO context. We have already concluded that the findings from the theory review match the corresponding findings from the theory experts’ evaluations quite well. We can then assume that the theoreticians’ evaluations represent theoretical side of the study to a large extent, as illustrated in the upper left section of Figure 1.2 in Chapter 1.

#### 5.3.6.1 Gap-analysis # 1: Do the evaluations done by theorists match the evaluations done by practitioners?

It is then interesting to analyze whether there is high level of agreement between the espoused theories of the theory experts with no stake in the subject matter, and practitioners with experience with practical NTO administration and governance with a stake in NTO matters. If there is a great amount of disagreement between the two groups, that could imply either: a) that the theoreticians are not well informed about the NTO context; or b) that current theory is under-developed to deal with that context; or c) that the practitioners are not well acquainted with the theoretical implications of NTO governance, or d) that our measures and/or theory work may not be as accurate as we want it to be. In other words referring to a), b), and c): Either the theoreticians or the practitioners could be “wrong” to some extent in their ideas about NTO-related matters. Then there would be a need for either a) to readjust existing theory and/or develop new theory for dealing with research problems similar to the NTO context; or b) to inform or educate NTO practitioners more about the theoretical implications of NTO governance. Conversely, if there is to be a great amount of agreement between the two respondent groups - that would indicate that there is theoretical-theoretical and practical-theoretical agreement as well, and that would indicate that our measures are adequate. If so, that would strengthen the theoretical side of the “equation”: i.e., that both a) judgments by theory experts, b) practitioners’ espoused theories, and c) theory reviewed about how NTOs should be governed – all come to more or less the same conclusions.

We will now compare the results consisting of the sample of scenario evaluations done by theory experts with the corresponding ones done by the practitioners in more detail. To check for differences or similarities, we will apply three different statistical tests:

*T-test for differences in means*

First we will start with presenting the results of a t-test for differences in mean scores. In our case, however, the sample size represents a problem for this test, since we have a relatively small sample of evaluations by our theory experts. Only two sets of the 22 different scenarios were evaluated by the theory-expert group. For instance, this left us with only two “individuals” (see Section 4.3.1 for details) and 4-6 cases for each of the 8 budgeting principles. Therefore, we decided to group the budgeting principles into sub-groups of two or more in order to yield more cases in each sub-group than for the individual principles<sup>37</sup>. We grouped the two types of *direct performance budgeting principles* (P1 and P2), the four *behavior-based principles* (P3-P6), and the two *indirect performance budgeting principles* (P7 and P8).

With respect to the principles' evaluated effect on Market Focus, we only found anything close to significant differences ( $t=1.929$ ,  $sig. = 0.071$ ) between the two respondent groups with regards to P11 *joint funding* as the funding arrangement. The practitioners (mean score **4.94**) view this source combination as more positive than the experts (mean score **4.29**).

In terms of the evaluations of the various principles' effects on Long-Term Perspective, we found no significant differences between the two groups judged by this test.

On the Operational Freedom-dimension, there were some differences between the two groups. With respect to *taxation* (P7 and P8) as budgeting principles, the theory respondents (mean score **4.98**) are more positive than the practitioners (mean score **4.09**) ( $t = -2.174$ ,  $sig. = 0.040$ ). The theory experts also are more positive (mean score **4.17**) to *limited corporation* as the ownership constellation than their practitioner counterparts (mean score **3.36**) ( $t = -3.188$ ,  $sig. = 0.05$ ) as well.

Those are the only differences we can identify between the two groups using a t-test.

#### *Non-parametric test for rank concordance*

We wanted to employ an additional test to test for differences between the two respondent groups. Kendall's non-parametric test for *rank concordance*, which tests the ordinal concordance between the ranking of  $m$  objects (principles or scenarios) by  $n$

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<sup>37</sup> This grouping procedure may not appear obvious without an explanation: P1 and P2 (both direct performance-based principles) are relatively similar in nature, e.g., with regards to the incentives they are expected to provide, and could therefore be grouped together. So are the two *tax-based principles* P7 and P8 (both direct performance-based principles). More problematic are the four behavior-based principles: P3, P4, P6, (and P5). It should be noted that P5 is not strictly speaking behavior-based, since it constitutes transfer of a fixed sum each year, relatively regardless of NTO's behavior. Furthermore, the three others are quite different in nature. Except the behavior-based nature of P3, P4, and P6, the only real feature these four principles have in common, are that they are not performance-based and should give few incentives for e.g., Market Focus. However, the t-test applied showed that there were, in general, few differences between the two groups evaluations' using the grouping procedure as mentioned. Had there been major differences, it may have been necessary to look at the grouping procedure again and regrouped e.g. the behavior-based principles in another fashion. Given the small and relatively insignificant differences between the groups' evaluations', we are thus comfortable with the grouping of budgeting principles into three different groups.

judges (here “individuals” = country groups and theory expert group). In our case the test checks for concordance in how the principles/scenarios are ranked by the two respondent groups, to find out whether the two groups rank the principles differently. This test statistic, Kendall’s coefficient of concordance (W), ranges from 1.00 (perfect concordance) to 0.00 (no concordance). First we ran the test with both respondent groups together in a joint sample where we had included the data for all the individual countries and the expert group. In that manner the rank test was run on the rank-order of all individual countries plus the expert group. We then ran the test excluding the expert group, and examined the difference in test scores between the two trials. If the test statistic W increased drastically after excluding the experts, it would signal that the expert evaluations differ considerably from the practitioners’ sample. For example, employed with respect to all the 8 budgeting principles’ effect on Market Focus, the concordance appears to be fair (W= 0.288, Chi sq. = 30.25), while significant (sig. = 0.000) in the first trial including the expert group. The second trial excluding the expert group, the test statistics had changed only slightly (W= 0.292, Chi sq. = 28.60), while still significant (sig. = 0.000). That should indicate that the exclusion of the experts does not raise the numeric value of W much, which it should have done if the expert group sample rank-order score was very much different from the other individual countries. In other words, that means that the principles are ranked more or less similarly across the two groups, and that the evaluations are concurring. This test also supports the notion that there are only minor differences between the two groups.

It is also worth to mention that some disagreement was observed with regards to the various *funding sources*’ impact on Market Focus. The W statistic increased from 0.618 (sig. = 0.000) to 0.679 (sig. = 0.00) when we excluded the expert group. This difference probably stems from the experts being somewhat more positive to *government funding* than the practitioners, and less positive to *combined funding*.

Some disagreement can also be observed with regards to the *budget principles*’ impact on Long-Term Focus. The W statistic increased from 0.108 (sig. = 0.124) to 0.117 (sig. = 0.118) when excluding the expert group. So there are some disagreements between the two groups about the impact of the various *budgeting principles* on Long-Term Perspective; however, they are only small differences. This minor disagreement is based on the fact that the expert group scores some of the performance-based principles higher than the practitioner group on this dimension.

We also ran the same test using the ranking of the 22 *scenarios* instead of the 14 *principles*. In addition to serve as a validation of the preceding test, we also avoid the problem with few degrees of freedom (2) when running tests for *funding source* (3 *source principles* = 2 *df*) and *ownership* (3 *owner principles* = 2 *df*). Running the test for all 22 scenarios (21 *df*) including the expert group with respect to Market Focus, revealed a fair degree of concordance with a W score of 0.191 (Chi sq. = 60.075), while significant (sig. = 0.000). Excluding the experts and running the same trial revealed just minor differences with a W score of 0.193 (Chi sq. = 56.739), and still clearly significant (sig. = 0.000). Again we can conclude that there are only minute differences between the scenario evaluations of the practitioners and the theory experts.

With respect to Long-Term Perspective, this test revealed a weak level of concordance among the countries when running the trial including the experts. The W score was 0.070 (Chi sq. = 21.900) and far from significant (sig. = 0.405). Again excluding the expert group, the W score increased only slightly to 0.076 (Chi sq. = 22.429), while still far from significant (sig. = 0.375). Judging from these two trials we can conclude that there is a significant degree of differences with respect to how the respondents in each country rank (i.e., score) the scenarios. However, these differences do not stem from differences in the ranking of scenarios between the practitioner and expert groups, rather from differences in rankings within the practitioners' group (i.e., between countries).

In terms of Operational Freedom the W score was 0.274 (Chi sq. = 86.251), and again significant (sig. = 0.000) in the first trial with the theory experts included. With the second trial excluding the expert group, the W score decreased to 0.268 (Chi sq. = 78.776), and still significant (sig. = 0.000). Again we can conclude that there is a fair degree of concordance, both between the two groups and in-between the countries in the practitioners' group.

From the Kendal test of rank-concordance we can then conclude that there is a significant degree of concordance between the rank-order of the scenario evaluations of the two groups.

### *Cluster analysis*

We then proceed to a third and final test to probe the degree of agreement between the theory experts and practitioners. This procedure attempts to identify relatively homogeneous groups of cases based on selected characteristics, using an algorithm that can handle large numbers of cases. By including the expert group as one "individual" or case along with the cases representing the 14 countries in the practitioners' sample, we wanted to check if the expert group deviated from the other cases. For instance, if the expert group was classified in one of the "deviant" clusters with few members, one could conclude that the expert group differs from the majority of the other cases. We ran the test for 2, 3 and 4 clusters for all the 3 dependent variables. Cluster analysis data are reported in Appendix 3.

In terms of Market Focus the expert group was clustered with the majority cluster of 10 cases, while the evaluations of Sweden and Luxembourg were clustered in the deviant cluster of only two members in the 4-cluster trial. This indicates that the expert group is not different from the majority of other cases in the practitioners' sample.

Continuing with Long-Term Perspective, the expert group was again clustered with the majority-cluster of 7 cases. Slovakia and Canada were clustered in the deviant cluster of two members in the 4-cluster trial. Also on this dimension, the expert group is in agreement with the majority group of evaluations done by the individual country groups or cases.

With respect to Operational Freedom, the expert group was actually clustered in the deviant group along with Norway in the 4-cluster trial. The majority cluster contained 8

cases in the final trial. There was also another deviant cluster of two members, but this cluster was clustered with the majority cluster in the 3- and 2-cluster trials. So the cluster containing the expert group could be considered “most deviant”. This analysis shows that the expert group in some disagreement with the majority of country groups’ evaluations on this particular dimension. Seen in connection with the t-test reported earlier in this section, the differences here seem to stem from differences in perceptions about *taxation* as budgeting principles (P7 and P8) and a *limited corporation* as an ownership constellation, about which the theoreticians are more positive to both of those than the practitioners.

Based on the cluster analysis altogether, we find a great amount of agreement between a) the majority of the practitioners’ individual country groups, and b) the theory expert group, on two out of the three dimensions

Judging from these three tests we have run: the parametric t-test of differences in means, the non-parametric tests rank concordance and cluster analysis; we can conclude that there is a high degree of agreement between the evaluations of the practitioners and the evaluations of the theory experts. There are some differences, as commented on, but these are definitely fewer than the similarities in the evaluations made by the participants in these two separate samples.

We have concluded earlier that the theory reviewed is on most aspects in fairly high agreement with the results from the evaluations made by the theory experts. Now we have taken the gap-analysis one step further; and we have found that the practitioners agree with the theory experts, as it is expressed through the scenario evaluations. We can then put down the following “research equation” to illustrate the conclusions so far:

**Theory reviewed  $\approx$  Theory experts’ scenario evaluations  $\approx$  Practitioners’ scenario evaluations**

Referring to Figure 1.2 in Chapter 1 depicting the research design, we can then state the following: There is no clear mismatch between the theory reviewed, the theory experts’ espoused theories, and the practitioners’ espoused theories. In other words, the three separate pieces of “theory manifestations” support each other, aid to validate another, and thereby strengthen the theory-side of this study, as we consider it. We will now go on to add the “last piece of the puzzle”, and ask the following: Does current practice concur with prescriptive theory; do the practitioners in our sample and their colleagues in the respective countries actually do as our respondents say (i.e., express through the scenario evaluations) NTO governance should be done?

Our final question can be added to our illustrative “research equation”:

**Theory reviewed  $\approx$  Theory experts’ scenario evaluations  $\approx$  Practitioners’ scenario evaluations = current practices?**

We will attempt to answer this question in the following section.

### 5.3.6.2 Gap-analysis # 2: Do the practitioners' evaluations (espoused theories) match current practice (theories-in-use)?

*Does the map (theory and scenario evaluations) match the terrain (principle descriptions of current practices)?*

Following the discussion in the preceding section, it is then very interesting to compare the theory-side of the study with how things really are done in practice; to see if practice runs contrary to theory literature and espoused theory.

To investigate this issue it would intuitively be tempting to try to run a correlation analysis between the descriptive scores for current practice (Table 5.1) and the practitioners' scenario evaluations (Table 5.7) since the data are readily available and measurement scales used are the same. However, as we have pointed out already, there is too little variation in how the principles are applied in current practice to make such a direct statistical comparison meaningful. Furthermore the scores in Table 5.1 are measures of the degree of any given principles' use in current practice, whereas the scores in Table 5.7 are measures of the evaluated effect of the principles on the three dependent variables. Thus, the scores are not statistically directly comparable. Instead we have decided to do the gap-analysis graphically<sup>38</sup>. Any match or mismatch between the degree use of principles, and the recommendations expressed through the scenario evaluations, will become visually apparent when we plot the two data sources in the same chart, as depicted in Figures 5.4 - 5.6 below.

There is in fact a mismatch in some instances between which principles are actually practiced in NTO governance, and what the practitioner respondents express should be done ideally in terms of governance principles. This becomes apparent as there is a difference in what the respondents describe as the current situation in terms of the proposed principles, and how the same principles are evaluated through the scenario evaluations. In the graphical gap-analysis below, we have investigated the nature of this mismatch. We will not go through all the possible combinations of variables in detail, but concentrate on the most important findings.

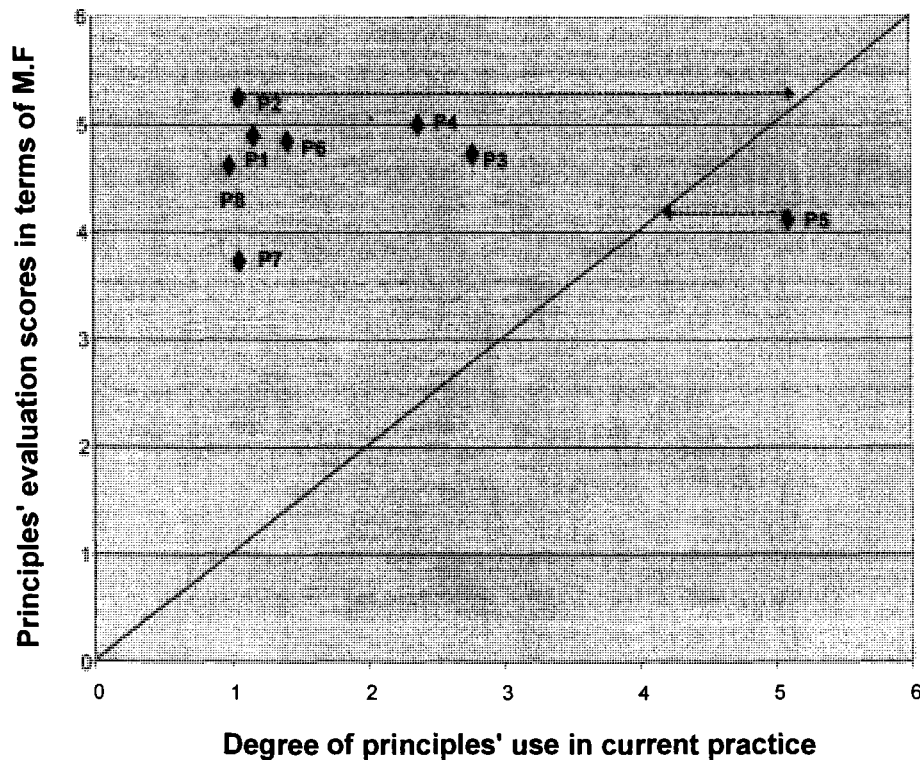
Figure 5.4 illustrates this mismatch. The diagonal line across the chart shows the ideal position of a given principle. For instance, any given principle that receives a low score in the scenario evaluation on an important aspect should ideally be used only to a lesser degree in practice, and conversely, a principle that scores high should be used to a higher degree.

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<sup>38</sup> For this gap analysis we have chosen to use a visual comparison between the two sets of data. In Gap analysis #1 we had two sets of data (theorists and practitioners) that were directly comparable for which we could run regular statistical analysis for to check for differences in the two sets. For the purpose of Gap analysis #2, this was not possible, since the scores for the descriptions of current practices illustrates to which degree any given principle is in use, whereas the scenario evaluations illustrate the expected effect of the principles on the three independent variables. Thus the data sets are not on the same format and therefore not statistically directly comparable. This is why we chose to use a visual comparison of the two data sets in Gap analysis #2.



**Figure 5.4**  
**Current budgeting practices vs. evaluations**  
**of principles' effect on Market Focus**



The principle that is the most “off the line”, as illustrated by the dotted arrow going right, is P2 (*relative performance*), since it scores high on positive effect on Market Focus, but is virtually nonexistent in current practice. Similarly, P5 (*fixed sum*) is evaluated below average in positive effect on Market Focus, while it is very common in current practice. In other words, P2 is not used as often as it should, while P5 is used too often - according to our respondents as judged by their scenario evaluations.

Use of principles in existing practice and the corresponding scenario evaluation scores are a lot more in congruence with respect to Long-Term Perspective, and will thus not be discussed in more detail here.

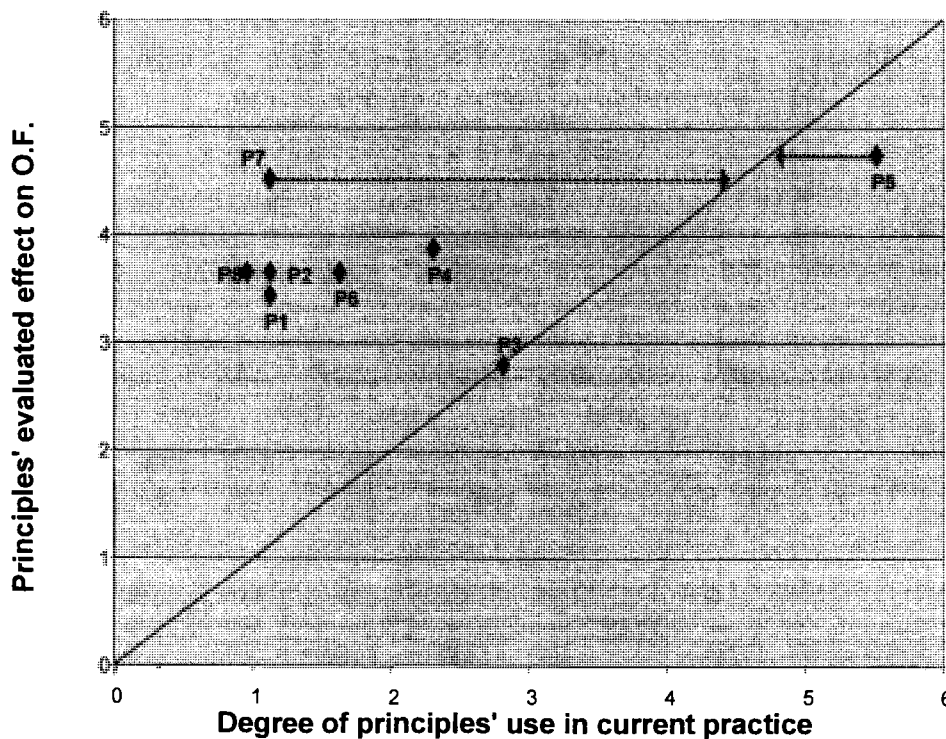
However, Figure 5.5 illustrates a similar mismatch as shown in Figure 5.4, but then in terms of Operational Freedom. The performance-based principles (P1, P2, P7 and P8) on the left side of the chart all score about average in terms of positive effect on Operational Freedom, whereas the same principles are virtually never used in practice. For instance, P3 (*project based*) is used more often than the performance-based principles, despite its evaluation score ranking it as the weakest of all the eight budgeting principles. P5 (*fixed sum*) scores quite high on Operational Freedom, but is still used more often than it “deserves” relative to, for instance, P7 (the *visitor tax* principle).

In terms of the eight budgeting principles we can summarize the findings as follows: We can see from the principle descriptions made by the focus groups that direct performance-based budgeting is not widely used (P1: score = 1.18, and P2: score = 1.07). However, our respondents rate these budgeting principles highly both on Market Focus and Operational Freedom. The principles are rated highly relative to the more traditional behavior-based budgeting principles such as *fixed sum-based* or *project-based*, which are both more commonly used (P5: score = 5.45, and P3: score = 2.77). This is an interesting finding, and important for the conclusions of this study.

NTA representatives and NTO executives, who made up the bulk of the scenario groups, *do in fact not "practice what they preach"*. On two out of the three factors we have included as important for successful NTO operation, our respondents favor performance-based budgeting as opposed to behavior-based budgeting, as it appears in the results of the scenario analysis. But performance based-systems are almost never used in practice. So our respondents clearly mean that performance-based budgeting is better overall, but those involved in NTO governance do not seem to put that idea into practice.

Figure 5.5

**Current budgeting practices vs. evaluations of principles' effect on Operational Freedom**



*Given the benefits of performance-based budgeting principles, why aren't they used?*

So why is not performance-based budgeting more widely used? We can only “guesstimate” why this is the case. Probably are the reasons more political or traditionally influenced than straightforward economical. In the following we suggest some plausible possible explanations:

1. A simple explanation is that NTOs' governing stakeholders are locked into a traditional way of thinking, and the idea of performance-based budgeting may not even have been on the agenda in most NTAs or any other stakeholder coalitions. One may simply not be aware of that performance-based budgeting is a realistic NTO set-up option. They may not be aware of the problems associated with the current traditional behavior-based budgeting system, and the potential benefits of performance-based budgeting. This is a straight-forward plausible explanation, but we hope this study can help overcome any disability to see new solutions on the part of the stakeholders.
2. As we have pointed out earlier in the theory chapter (Section 2.4.3), an obvious practical problem with performance-based systems is their complexity. They depend on governments' access to all relevant data needed for the set-up, implementation and execution of a performance-based system. This means that some resources will have to be consumed by the governments to design and follow up such systems and for the NTOs to understand, familiarize themselves with, and adapt to the new system.
3. There is of course a “switching cost” associated with breaking up established routines and to develop and follow up new practices. Performance-based budgeting may not be in line with current public budgeting processes for many governments, and such changes may involve labor-intensive and bargain-laden effort involving coordination of several ministries or departments, e.g., department of tourism, treasury, labor, interior, etc. A bureaucracy will of course need both strong internal and external incentives to embark on such a (possibly controversial) change process.
4. The flexibility for NTAs under e.g., a “fixed sum budget decided each year”-system can be used to cut NTOs' budgets arbitrarily when the general budgeting situation calls for budget cuts in the general national budget, and that flexibility will then be lost under a performance-based system. The NTAs, other departments or parts of the bureaucracy may not want or cannot agree upon giving up budget flexibility.
5. This is also related to the issue of budget liability uncertainty on the part of the government or other funding stakeholders. Budget liability uncertainty can be challenging for some governments, because it makes the government liable to come up with extra budget funds if the NTO achieves significant increases in tourism traffic. The government will not know for sure how much it will have to pay out next year, which may be problematic in the public budgeting process (ref. section 2.4.2). The government and other sponsors may not wish to cope with this kind of unpredictability.

6. Since many NTOs worldwide still are government bureaus or entities, NTO governance regimes based on government control and funding of NTOs may not give as strong incentives for a change of system compared to the incentives for private organizations. Private principal-organizations have stronger incentives to try to reduce any agent inefficiency, e.g., through performance-based contracting, when strong competition forces organizational inventions and change in order for the organization to survive. Performance-based contracting is in fact more common in the private sector than in the public sector (ref. the World Bank-study discussed in Section 2.4.2).
7. The set up of NTOs and other similar organizations may be subject to a kind of international “mimicking”. When any given country decides to organize an NTO, it may look at how this is done in neighboring or familiar countries. Since performance-budgeting systems still are relatively uncommon, one can probably not expect that governors of new NTOs are innovative and implement these kinds of new systems “out of the blue”. Any (hypothetical) governors of new NTOs will probably resort to a cross-nations kind of “group thinking” with respect to NTO set-up. Then the prevailing traditional system perpetuates to the governance system of new NTOs. The parties involved may not want to spend the resources and put forward the needed effort to invent and implement a new system, unless the parties perceive that the benefits outweigh the costs of changing the current regime.
8. There has been little empirical research on the subject matter. We know of no other study that involves the set-up of an NTO governance system. To this date, there is still little solid empirical evidence that performance-based budgets actually improve NTOs’ or similar organizations’ performance in reality. Of course there are some costs involved with implementing such systems, and when there are costs there are risks. Governments or other stakeholder coalitions may be resistant to be the first-mover actors and go ahead to set up such a new system when the effects have not been solidly proven. Thus, they may not want to take on the risk to be the first-movers on testing out a not-yet-proven system.
9. Furthermore, there could be a strategic imperative to resist performance-measurement (ref. Section 2.3.4). It may reveal inefficiency, which obviously can be embarrassing for the NTOs themselves, but also for the public sponsors (i.e., NTA) which is supposed to be (at least to some degree) responsible towards its constituents for the NTO agencies’ (mis-)behaviors. In fact, this potential embarrassment can cause implementation and use of performance-measurement being resisted to both by NTOs themselves and sponsors i.e., the government or any other sponsoring stakeholder.
10. There is also the issue of cost of transfer of risk (ref. Section 2.2.4.3). Performance-budgeting is likely to increase NTO managements’ perceptions of risk, since tourism traffic fluctuations, and thereby the budget outcome somewhat depend on factors beyond their control. Then the managements may demand a risk-premium, for instance higher relative base budgets, for them to accept an implementation of performance-based budgeting. If NTO managements are threatening to refuse to comply with performance-based budgeting unless there is an addition of a risk-

premium, this could make the implementation of the system appear to be more costly than beneficial from NTAs' viewpoint.

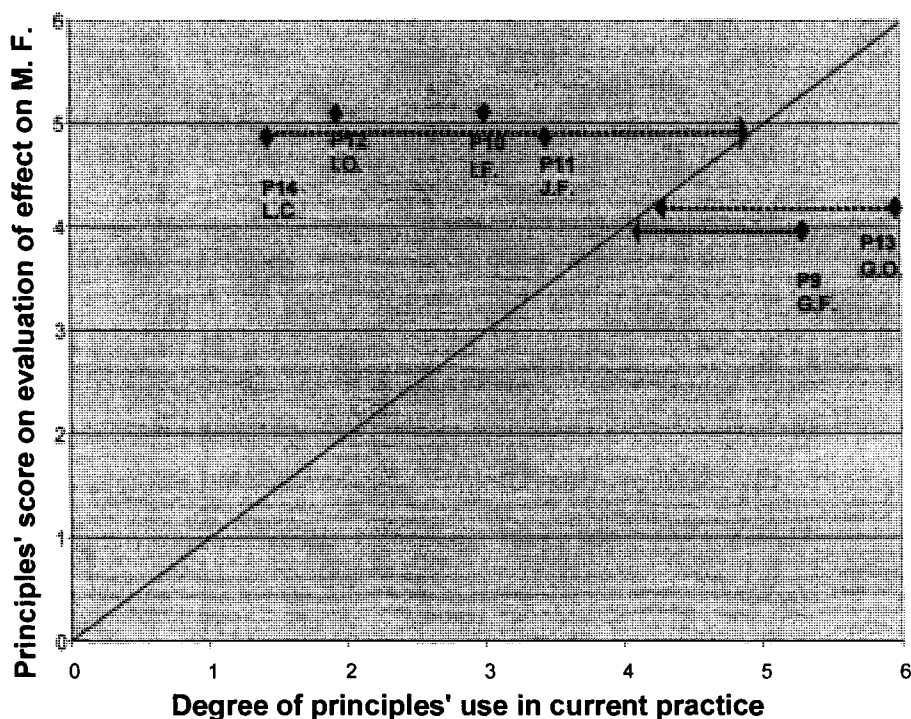
11. Finally, and this may be one of the most important reasons, the NTOs' managements may be able to convince NTAs and other stakeholders that it is unreasonable that the NTOs should be held accountable for factors that influences fluctuations in tourism traffic that could be somewhat beyond NTOs' control. NTOs' managements may then be able to negotiate soft NTO targets instead of hard performance targets (ref. 2.4.2).

The eleven reasons listed above may explain why performance-based budgeting systems are not commonly used despite their many advantages and positive evaluations.

In the same way as with the *budgeting principles*, there is a mismatch in terms of evaluation scores versus the current level of use of some of the various *funding* and *ownership* principles.

In Figure 5.6 we have plotted both the scores for the funding and ownership principles in the same chart. From the chart display we can notice that *government funding* (P9) and *government ownership* (P13) are by far the most common principles in practice. But these principles score significantly lower on the evaluated effect on Market Focus than *industry funding* and *industry ownership*.

**Figure 5.6**  
**Current funding and ownership practices vs. evaluations of principles' effect on Market Focus**

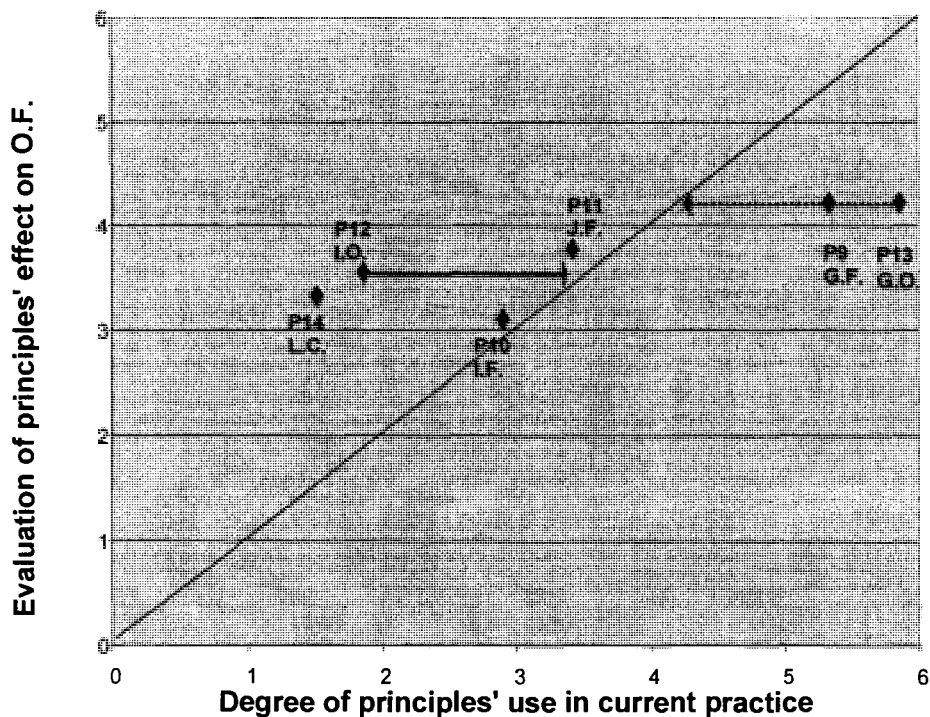


It is also noteworthy that the respondents express through the scenario evaluations that *limited corporation ownership* should be used more often than it is, considering its perceived positive effect on Market Focus.

Again, we can see from the principle descriptions made in the focus groups that *industry-owned/controlled* (P12: score = 1.70 and P14: score 1.43) and *industry-financed* (P10: score = 2.34) NTOs are not common in current practice. However, our respondents rate *industry ownership* and *funding* significantly better than *government ownership* and *government funding* on Market Focus. In other words, *government ownership* and *government funding* are not considered as beneficial for NTOs' Market Focus as the alternative principles; still these are the most common arrangements. Reducing government funding and ownership/control and increasing private ownership/control, could be beneficial for NTOs propensity for Market Focus. This is yet another interesting finding.

In Figure 5.7 below we can see a more "correct" pattern in terms of the Operational Freedom-dimension, principles that score high on evaluations are also used most frequently (P 9 and P13), with P 10 (industry funding) being the most "in line", i.e., moderately positively evaluated and moderately used.

**Figure 5.7**  
**Current funding and ownership practices vs. evaluation of principles' effect on Operational Freedom**



*Government funding* and *government ownership/control* is widely used, while these are also the principles that receive the most favorable evaluations. So in that case there is no serious mismatch, except that *industry ownership* could have been used more frequently than it is relative to *government ownership*.

With respect to Long-Term Perspective, there is little variation among the principles with respect to how they are evaluated. According to the evaluations, it does not matter that much which *funding-* or *ownership* principle is used in that regard.

*Given the value of private ownership and funding principles on Market Focus, why aren't they used?*

So why are not *private/industry ownership* and *private/industry funding* used more widely? Again, there are probably several reasons why, as listed below:

1. Obvious reasons can be the same factors like tradition; mimicking; costs and perceived risks associated with change of existing practices; political resistance to change; potential shift in power, status and resource-allocation etc. as noted in connection with the budgeting principles earlier.
2. The NTAs and (other stakeholder coalitions) do not appreciate the value of Market Focus, or think that this should be an important goal for NTO-governance. The NTAs and NTOs themselves may not be aware of (i.e., what we propose to be) the cause-and-effect relationship between Market Focus and organizational performance. Some of our respondents may not even be familiar with the concept of Market Focus/market orientation, (especially those from countries with a transition economy e.g., the Czech Republic and Slovakia), even though we attempted to explain this concept thoroughly in the focus group sessions.
3. There seemed to be a consensus among the group members and across groups that *government operation* is less efficient than *private operation*, which is in line with the theory-discussion in Section 2.4.1. However, as we pointed out there, the governments may have other motives than cost-efficiency (e.g., through Market Focus) and profit-maximization related to NTOs' operation. Our respondents, and others who form NTO governance in the individual countries worldwide, could have been concerned that *private sector funding* and *private sector ownership/control* would cause NTOs to undervalue important societal goals, and that private operation therefore is not appropriate.
4. Another plausible explanation may be the notion that *private funding* (and operation) simply would not work in practice due to the *common/collective good problem* discussed in Section 2.4.4. The common good nature of NTO operation makes it difficult to find one particular private actor or group who would be willing to accept the responsibility to fund and operate the NTO. One concern is that NTOs would be under-funded, another is that private actors may not want or be able to spend the resources to obtain the information needed to influence or participate in strategic planning, negotiate budgets, monitor activities and performance, and enforce reward

and punishment schemes. Several focus groups pointed to the case with the failed attempt by the Swedish NTA to privatize the funding and operation of its NTO. This was mainly explained by the difficulties to rise sufficient private sector funding. However, the Swedish NTO case should not be taken as all-time solid evidence that all privatization attempts are destined to fail. For instance, as noted in Section 2.4.4, local-level and private-sector LTOs do exist and seem to function adequately. Some of these also receive some public funding. So private funding and operation could be possible, but government participation, i.e., public-private joint funding, might be needed to make such a system work in practice.

5. Private actors may not have the needed confidence in an organization like the NTO, which can help explain why so few private sector NTOs exist. The private sector actors may not have confidence in that the national-level generic type of marketing activities performed by NTOs are sufficiently efficient and effective in terms of attracting visitors. These actors may want to prioritize local-level, trade-specific, or individual business-type of marketing activity. Our respondents, particularly the industry representatives, may have been considering this when they made their scenario evaluations.

As in the case with performance-based principles, there are many obstacles to stronger private presence in NTO funding and operation. However, there are several merits by introducing private influence. A good example is the Canadian Tourism Commission, which participated in our study. The CTC is funded approximately 50% by the private sector, and 50% by the public sector, which is the highest proportion of private sector funding in our international sample. The CTC also has stronger-than-usual private representation in its board of directors. Not surprisingly to us, the CTC appeared to be the most market-focused, long-term oriented and autonomous NTO among the 15 NTOs we came across in our study. The CTC is also one of the most successful NTOs in terms of performance. The CTC has managed to improve its performance significantly after it was reformed from being a public bureau (around 1990) to its current semi-private/public form. We will investigate the case of the CTC in comparison to other NTOs in our sample in more detail in Appendix 7.

### 5.3.6.2 Conclusions from the gap analysis

From Gap analysis #1 it becomes clear that there are only minor differences in how the theory experts and practitioners evaluate the 14 proposed principles. Conversely, we have seen that there appears to be a mismatch on several counts between a) what the stakeholders think are the best principles, as well as what literature and theory experts prescribe, and b) the actual principles in use under current practices. This is shown graphically and commented on in Gap-analysis #2.

We can then answer our final question in our illustrative “research equation”

**Theory reviewed  $\approx$  Theory experts’ scenario evaluations  $\approx$  Practitioners’ scenario evaluations  $\neq$  current practice!!!**



As we have pointed out earlier, the theories-in-use are not only a result of the discretionary choice of the practitioners in our sample alone. The decisions made and practices implemented are also influenced by people not included in our sample. Furthermore, current practices are the outcome of political processes, bureaucratic regulations and existing legislation, as well as tradition and culture, etc. So the current practices implemented may not be based on efficiency, effectiveness, and business concerns alone, but are the result of political decisions as well.

Apart from that, some of the reasons we have listed why there is a mismatch between theory and practice, as it relates to NTO governance, are probably more legitimate than others. For instance, some of these reasons point to: unwarranted bureaucratic or other stakeholders' "laziness", propensity to "let things slide", traditional ways of acting, and bilateral resistance to change. Others could involve: loss or change of power, status, and resources. Common for all these reasons are that they are counter-productive seen from societal perspective, and should not be allowed to hamper progressive change in NTO governance. However, some of the other reasons are somewhat more justifiable; they do point to real practical problems, and are thus harder to overcome even if the willingness to change is present. Anyway, all the reasons listed, and any other that may be plausible, are real obstacles to implementation of NTO output-enhancing performance-based budgeting systems and increased industry/private sector presence. For a change in regime to occur, one probably needs consensus among several stakeholder parties about this course of action. A change also depends on the real initiative from motivated, dedicated, powerful, and resourceful individuals or groups to bring such changes about. Not all NTAs or other stakeholder coalitions have such individuals or groups in their staffs and needed resources within their administrations, and the result may be that the old system prevails indefinitely.

As mentioned in the discussion from the introductory chapter in Section 1.4, an important purpose of this study is to elicit how the stakeholders think and reason when they make decisions about NTO matters, and if this reasoning is actually congruent with what ends up as implemented principles in current practices. In fact, this research process can be described in terms of Argyris and Schon's (1974) notion of *discovery of espoused and theory-in-use*. In line with Argyris and Schon's arguments as presented in Section 1.4.2, we want to contribute through this study so that both the espoused theories and the theories-in-use of NTOs' governing stakeholders and their underlying assumptions are discovered, made explicit, and put under public scrutiny. We believe that in this way NTO governance matters could be made subject to healthy public debate, and eventually, so that any inefficient or obsolete practices are abandoned.

## 5.4 Summary of empirical findings

The most important empirical findings from this study are as follows.

1. Existing practices, i.e., how NTOs are set up and governed today, are quite similar from one country to another. In other words, there is little variance in which ones of the proposed 14 principles that constitutes the best descriptions of these

practices across the countries in our sample. Existing or current practices can be termed the extensions of the *theories-in-use* of those involved in NTO government in our sample countries, as explained earlier. These practices are summarized in Table 5.1. The principles describing existing practices the best (as expressed by our respondents), are the following: 1) Budgets are based on *a fixed sum decided each (fiscal) year*. 2) Some countries base parts of the NTO's budget on the *sale of specific projects*. 3) The NTOs are (for the most part) *funded/financed by the government*. 4) In some instances the NTOs are *funded/financed jointly by the government and the industry*. 5) The NTOs are *owned or controlled by the government* and thus responsible towards the government (usually a ministry). 6) In some cases, industry representatives are allowed to join the NTOs' boards, and some NTOs are therefore perceived to be *partially "controlled" by the industry*.

2. The scenario evaluations represent the theory experts' and the practitioners' anticipations about how the various principles, as they are combined into different scenarios, will affect NTOs' incentives and working conditions. This can be considered the respondents' *espoused theories*. Their "theories" as to how the principles will affect NTOs' behavior are expressed in how they assess the likely consequences (in terms of NTOs' Market Focus, Long-Term Perspective and Operational Freedom) of each scenario.
  - a. From Tables 5.3, 5.4 and 5.5 we can see that the *budgeting principle* is the one independent variable that has the strongest impact on any one of the three dependent variables. On the other hand, *ownership/control* is the independent variable perceived to have the least impact on any of the dependent variables.
  - b. The analysis of the various principles derived from the scenario evaluations are summarized in Tables 5.6 - 5.9. Both theoreticians and practitioners seem to agree that performance-based principles (i.e., P1 and P2) are preferable in order to increase and maintain NTOs' Market Focus. Furthermore, both *industry funding* and *industry ownership/control* are perceived significantly better than *government funding* and *ownership/control* on this dimension.
  - c. However, a governing principle deemed beneficial for one dimension of performance does not necessarily have the same positive impact on other dimensions. For instance, *behavior-based budgeting* principles (e.g., P5) are perceived better than *performance-based* principles on the Long Term-Perspective and Operational Freedom- dimensions by our practitioner respondents. Moreover, *government funding* and *government ownership/control* are perceived more positive than the industry equivalent on the Long Term-Perspective and Operational Freedom- dimensions by both respondent groups.

- d. Considering the practitioners' sample only, there are some differences in how the various types of respondents (i.e., NTO, NTA, and industry representatives) evaluate the principles. Industry representatives are more favorable to *taxation* as a budgeting principle than the other respondents with regards to enhancing NTOs' Market Focus (e.g., P7: NTA (mean score **3.80**) vs. Industry (mean score **5.11**); sig. = 0.041 & P8: NTA (mean score **3.87**) vs. Industry (mean score **5.18**); sig. = 0.029). This applies to P8 (*industry tax*) for the two other dependent variables as well. The industry representatives also give higher Market Focus-ratings to the *limited corporation* alternative than do the two other types of respondents (NTA (mean score **4.78**) vs. Industry (mean score **5.44**); sig. = 0.056) and (NTO (mean score **4.64**) vs. Industry: sig. = 0.010). Moreover, participants from the industry also regard *industry ownership/control* as more beneficial than e.g., the NTO representatives for NTOs' Long-Term Perspective (NTO (mean score **3.53**) vs. Industry (mean score **4.28**); sig. = 0.050). Lastly, industry representatives are far more positive to an *industry-led* organization than the NTO (NTO (mean score **3.16**) vs. Industry (mean score **4.26**); sig. = 0.027) and somewhat more than the NTA representatives (NTA (mean score **3.63**) vs. Industry: sig. = 0.19) with respect to NTOs' Operational Freedom.
  
  - e. The scenario analysis reveals that there are some differences between the theory experts and practitioner groups. For instance, the theoreticians appear to be more favorably inclined to *taxation* (P7 and P 8) as budgeting principles than the practitioners, as well as more positive to a *limited corporation* as an owner with regards to Operational Freedom. The theory experts are in general more favorable to *performance-based budgeting principles* (P1, P2, and P7), and less favorable to *behavior based-budgeting* (e.g., P4) than the practitioners in terms of both Long-Term Perspective and Operational Freedom. On the last two dimensions, the theory experts are more favorable to NTO ownership/control by a *limited corporation* than their practitioner counterparts.
3. Despite these differences between the two groups' evaluations, the statistical tests in Gap-analysis #1 reveal that these differences are still small and relatively insignificant:
- a. The pair wise t-tests for differences in means only reveal significant differences in terms of the evaluations of the various principles' effects on the Operational Freedom-dimension. With respect to *taxation* (P7 and P 8) as budgeting principles, the theory respondents (mean score **4.98**) are more positive than the practitioners (mean score **4.09**) ( $t = -2.174$ , sig. = 0.040). The theory experts are more positive (mean score **4.17**) to *limited corporation* as owner than their practitioner counterparts (mean score **3.36**) ( $t = -3.188$ , sig. = 0.050) as well.

- b. Kendall's test of rank order concordance revealed some disagreement with regards to the various *funding sources*' impact on Market Focus. The W statistic increased from 0.618 (sig. = 0.000) including the theory experts, to 0.679 (sig = 0.00) when we excluded the theory expert group. This difference probably stems from the experts being somewhat more positive to *government funding* than the practitioners, and less positive to *joint funding*. Some disagreement was also observed with regards to the *budget principles*' impact on Long-Term Perspective. The W statistic is increased from 0.108 (sig. = 0.124) to 0.117 (sig = 0.118), when excluding the theory expert group. This is mainly due to differences in evaluations with regards to the two *tax principles* (P7 and P8).
- c. Our final test, cluster analysis, only revealed differences with respect to the Operational Freedom-dimension. The theory expert group was clustered in the "odd" group in the 4 cluster trial on this one dimension. This analysis shows that the theory expert group is in some disagreement with the majority of the individual country groups' evaluations on this dimension. The disagreement seems to stem from differences in perceptions about *taxation* as budgeting principles (P7 and P8) and a *limited corporation* as an owner, where the theorists are more positive to both of those than the practitioners.
- d. Judged by the three test reported in Section 5.3 there is a fairly high degree of statistical agreement between the two respondent groups. However, even though the between-groups variance is fairly low, there is some variance between the individual evaluations within the two groups. In particular this concerns how the principles are expected to influence NTOs' Long-Term Perspective. This becomes apparent from the relatively high standard deviation of the mean scores as depicted in Table 5.7 and the rank order test of Kendall's W. For the practitioners<sup>39</sup> the W score is 0.19 for Market Focus, and W = 0.08 (no significant concordance) for Long-Term Perspective, while W = 0.26 for Operational Freedom in terms of how the scenarios are ranked. This is interesting, since it indicates that different respondents view things differently, particularly with regards to Long-Term Perspective. (Scores close to 1.00 would indicate strong agreement across countries.) Regarding the practitioners' group we have already pointed out the possibility that differences are stemming from the respondents professional background. Further variance may be due to differences in cultural background and varying exposure to the various governance regimes (e.g., as in transition economies in Eastern Europe vs. industrialized countries in Western Europe).
- e. Judged by the lower standard deviation scores (e.g., compare Tables 5.6 and 5.7) the theory experts appear in general more in agreement within the

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<sup>39</sup> The sample size with only two sets of scenarios is too small to calculate the theory experts rank concordance separately, and scores for this group is thus not reported here.

group than the practitioners are across countries. Notwithstanding, the theoreticians also represent different areas of theory, and as we have seen in the theory review, the various areas of theory may yield somewhat conflicting recommendations. This can account for some of the observed variance within the theory experts' group.

4. Gap-analysis # 2 represents a visual/graphical analysis of the differences between the results from the scenario evaluations and the existing or current practices. The *theories-in-use*, in terms of to what degree the various principles are used in NTO governance today, do not appear to match the *espoused theories* derived from the practitioners' scenario evaluations on several aspects, as depicted in Figures 5.5, 5.6 (& 5.7). This is one of the most important and interesting findings of this study. For instance, *performance-based budgets* as well as *industry funding* and *industry ownership/control* are considered positive for NTOs' Market Focus, while seldom used in existing practice. Moreover, *project based budgeting* is the second-most used budgeting principle, despite its very low scores on both the Long-Term Perspective and Operational Freedom dimensions. This fact should call for some changes, or at least revisions, of existing practices (see also Chapter 6 for details).
5. There are also a few differences between the theory- and context-based propositions/recommendations in Chapter 3, and the practitioners' espoused theories. Specifically, this applies to the practitioners' skepticism towards *visitor tax-based budgeting* (P7). In general, the practitioners' are more skeptical to the *performance-based budgeting principles* in terms of both Long-Term Perspective and Operational Freedom than the propositions/recommendations suggest. Not surprisingly, these propositions are more in line with theory experts' evaluations, since the professional background of the theory experts build (among other aspects) on the very same theory literature the recommendations are derived from.
6. Finally, it is noteworthy that these recommendations or prepositions appear to concur very well with the espoused theories of the theory experts extracted from the scenario evaluations, and quite well with the espoused theories of the practitioners. What distinguishes itself from these three "manifestations of theory", are the existing practices, i.e., the practitioners' and their colleagues' theories-in-use in their respective countries. So there is at least a partial mismatch between theory and practice in our case. This is particularly valid with regards to theory and practice in terms of fostering a desirable Market Focus of NTOs.

## **6.0 Conclusions and Recommendations**

Our findings and conclusions can be summarized as follows:

### **6.1 Conclusions**

We believe that it is advantageous for NTOs to have:

- a Market Focus as the dominating organizational orientation,
- a Long-Term Perspective in planning and engagements, and
- Operational Freedom to determine and implement marketing strategies.

We furthermore believe that the degree to which NTOs have a Market Focus, a Long-Term Perspective, and enjoy Operational Freedom with incentives to determine and implement its marketing strategies, at least to some degree is influenced by:

- the procedures used for determining the budgets/revenues for the NTO,
- its source of revenue, and
- who “owns” or controls the organization.

Our respondents from the international sample appear in general to concur with the conclusions above - although this conclusion should be modified somewhat:

The practitioner respondents revealed, both in focus group discussion and in the scenario evaluations, that:

- performance-based principles promote Market Focus and Operational Freedom, but
- these principles may at the same time discourage a Long-Term Perspective.

They also expressed concern that a performance-based principle may produce revenues that would be very volatile. However, the theory experts do not seem to agree with the practitioners on this issue. Theory experts evaluate performance-based principles to score high also on Long-Term Perspective, which can be argued for from a theoretical perspective as well.

Furthermore, our practitioner respondents distinguished fairly strongly between alternative performance measures and were quite skeptical to the idea of tying the budgets to *tax revenues*. The theory experts – on the other hand – are also far less skeptical to tax revenues as a budgeting principle. Our separate data analyses (ref. Appendix 7) also suggest that it may be unimportant whether performance-based budgets are linked to tax revenues, tourist receipts or some other measure of value creation, since

- the correlation between alternative performance measures is high.

We believe that the skepticism to any tax-based budget procedure to some extent reflects legal constraints on earmarking tax revenues for designated purposes. We will return to this issue later.

Although some of our practitioner respondents questioned whether the source of income (e.g., the government) had any impact whatsoever on Market Focus, the scenario evaluations reveal some skepticism to *funding by the government*. This is also the case with the evaluations of the theory experts. Furthermore, we found a relatively strong correlation between the amount of NTOs' budget accounted for by the government on one side and the organization's Market Focus and market orientation on the other. This parallel analysis is included in Appendix 7. This finding suggests that

- in fact the importance of government funding may affect NTOs' relationships to their stakeholders.

There were also differences in how the ownership/control variable was viewed by our respondents. *Industry ownership* was perceived positive for NTOs' Market Focus and Operational Freedom, while government ownership was perceived important for NTOs' Long-Term Perspective. Along with the theoretical support, this leads us to conclude that

- *joint funding* and *joint ownership* may be the best solution for NTOs' operations.

In terms of our gap analysis there seems to be a good match between theory recommendations from literature, theory experts' scenario evaluations, and practitioners' scenario evaluations (which also are the practitioners' espoused theories). However, there is an apparent mismatch between these three theory-representations on one side, and current practices (the practitioners' and their colleagues' theories-in-use) on the other side on several aspects. We believe this fact calls for revisions of current practice to make it more coherent with what theory prescribes. This will most likely enhance NTOs' performance.

These are the most important findings of this study.

## 6.2 Recommendations

Our recommendations are the outcome of a synthesis of the theoretical framework, a contextual analysis, and the conclusions based on our empirical findings. The recommendations are listed in below, and we will in the following give a short justification for each:

- **The NTO's budget – or some part of it, should be performance-based**

We believe this recommendation can be justified on several grounds:

1. It will make NTOs share the destiny of the industry they are commissioned to promote in the sense that they will realize that what is good for the overall tourism

industry, will also be in their own interest. We believe this will promote Market Focus of the organization. Hence, we believe it will be in NTOs' own interests to engage in marketing activities like:

- information generation,
  - information dissemination to the industry,
  - competitor awareness and response,
  - selection and positioning of tourist products that are market-oriented, etc.
2. It will reduce the need for the stakeholders to constantly monitor and approve NTOs' plans and activities. Thus NTOs may put less emphasis on lobbying and legitimizing its existence and activities, and put more emphasis on the market effects of its actions. At the same time, the NTO will probably be allowed to enjoy more Operational Freedom to base their decisions on their own professional judgment, i.e., under the restrictions of marked-performance put on the NTOs' through the performance-based principle.
  3. A performance-based principle will reward both the NTOs and the tourism industry for their value creation. In many countries the tourism industry is the only export industry that has to pay sales/value added tax. Whether a performance-based principle somehow is linked to e.g., value added tax or tourism receipts, performance-based revenues will allow the tourism industry to get a "fair share" of its contributions to the country's tax revenue.
  4. Performance-based procedures can be designed so that the disposable revenues for NTOs will reflect fluctuations in the size of the market they serve and their customer base. This may be desirable, since it is more costly to sustain a large customer base than a small one due to the costs associated with retaining "old customers". This is also somewhat analogous to extra credit/bonuses for new accounts created in a sales compensation scheme for an individual salesperson or team within a company.
  5. Our respondents appear in general to be favorably disposed to the idea of performance-based budgets (see Tables 5.6 and 5.7).
- **The NTO's budget should have a fixed component with a time horizon of more than one year (e.g., three years)**
1. A fixed portion will reduce fluctuations due to a performance-based principle, which may be particularly important in a transition period. The fixed amount could then gradually be reduced (see Appendix 7 for an illustration).



2. A time-horizon of more than one year (e.g., three years as in Denmark) will promote Long-Term Perspective and may reduce the need for NTOs to engage in political processes every year in order to acquire economic resources<sup>40</sup>.
  3. A fixed portion with a time horizon of more than one year will alleviate the concern expressed by some of our practitioner respondents that performance-based principles alone may demote Long-Term Perspective and/or Operational Freedom (see Tables 5.7 and 5.9).
  4. The fixed portion of the budget could be included to cover the more programmable, routine kind of tasks (see Section 2.1.5.6 for an explanation of which tasks these are). These programmable tasks are also somewhat easier to price or cost-assess, and can be cost-assessed for a longer time period than the less programmable tasks, since they change less from year to year.
  5. The fixed portion could also be designated to cover fixed cost of NTOs' operation, e.g., office rent, energy, base salaries etc. However, NTOs could be allowed to choose from a variable "budget-menu" which combination of fixed/performance-based they would like to operate under (see Section 2.4.5.5. for details and Appendix 7 for an illustration).
- **The NTO should be allowed to transfer funds from one budget year to another**
    1. Such a principle would encourage Long-Term Perspective, and reduce the need to spend all available resources within one budget year. Excess funds accruing in prosperous years could then be saved to counter adverse conditions other years. A related issue is when to set aside funds and why (e.g., see Table 2.6).
    2. Such a procedure would also alleviate the concern expressed by some of our practitioner respondents that performance-based principles alone may demote Long-Term Perspective (see Tables 5.7 and 5.9).
  - **The NTO should be *allowed to*, but *not required to*, sell projects to the tourism industry**
    1. A matching-principle may force the NTO to sell projects that may not necessarily be compatible with its long-term strategies. Many countries (e.g., Denmark and Canada) experience that projects initiated by the NTO itself may both serve their partners' interests and help the NTO pursue its long-term goals.
    2. We believe the initiation and sale of projects on a *voluntary basis*, and not as an implementation of a matching-principle, could alleviate the concern expressed by our

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<sup>40</sup> E.g., CTC's (Canada's NTO's) budget is multi-year (the government planning process forecasts fixed appropriation).

international respondents that sale and participation of projects may discourage Long-Term Perspective and reduce Operational Freedom (see Tables 5.7 and 5.9)

- **The NTA should take steps to involve the tourism industry more in both funding and ownership of the NTO**

Although our empirical investigation reported in Appendix 7 suggests that *funding source* may have an impact on NTOs' focus, we do not give absolute recommendations with respect to the *source of funding* (either *government* or *industry*). The reason why we do not is that we believe procedures such as the following will reduce the importance of the source: a) A fixed sum portion of the budget granted for more than one year b) combined with a relative performance-based portion of the budget - will allow NTOs to fully turn their attention to the market regardless of where the funding comes from. A system that allows transfer of funds from one year to another may have the same effect, as will the abolition of a matching principle.

We do not offer absolute recommendation with respect to *ownership* either, except that we believe that more industry/private sector participation in NTOs' ownership/control could be beneficial. To the extent that implementation of our recommendations above will encourage more Market Focus and stronger market orientation, it may imply a transfer of "ownership" from some of NTOs' currently controlling stakeholders *to the market*.

Rather than recommending either government- or industry/commercial funding and ownership, we encourage the NTAs to involve the industry and private sector more than they are as of today. Private-public sector partnership in funding and ownership/control seems to be the best alternative. The reasons for this recommendation are as follows:

1. Both respondent groups agree that pure *government funding and ownership* is not beneficial for NTO's Market Focus. *Industry* presence seems to be necessary to promote this very important dimension. At the same time, the practitioners value the government as the best funding source and owner in terms of Operational Freedom. Joint funding also seems to be the best alternative to promote Long-Term Perspective.
2. *Government funding and ownership* may lend itself to a more bureaucratic way of operating NTOs. For instance, it may result in an organization laden with "bureaucrats in business", rather than led by professionals with marketing and industry experience. It can in some instances lead to an NTO organization where decisions are made politically rather than professionally; an organization that is rule-based and inflexible - characteristic of some government bureaus and agencies; as well as an organization where budget-maximization, political career-building, and government-lobbying effort becomes more important than efficiency and market performance.
3. Strengthening *industry/private sector* presence in NTO funding and control may increase professionalism in the organization, as well as improve NTOs'

legitimacy in relation to the industry it is set to promote, and increase the industry's interest and commitment in NTOs' operation, activities and performance.

- **The government should still be involved in NTO funding and ownership, but share this role with the industry/private sector.**
1. On the other hand, *government* participation in *funding* and *ownership* may be needed to provide a stable source of income (e.g., in a combined funding scheme), to deal with needed financing due to the common goods-problem of generic tourism marketing, and to secure that societal concerns (ref. Figure 3.5) are taken into consideration in NTOs' activities and strategies.
  2. Government presence in funding and control may also be beneficial to avoid that NTOs over-prioritize special interest in the private industry; and to avoid that NTOs become too product-oriented or sales-oriented rather than market-oriented.
  3. Finally, a final reason for *joint funding* and *ownership* is fairness. The industry, the government, and the taxpayers all benefit from sustainable tourism, as we have pointed out in the introductory chapter and illustrated in Figure 3.3 in Chapter 3. It is then a matter of fairness that all beneficiaries that have a stake in NTO matters should contribute to NTOs' funding as well as being represented in NTOs' governing bodies.

**Table 6.1**  
**Management implications**

**Recommendations: Our ideal "scenario"**

- *The NTO's budget – or some part of it, should be performance-based*
- *The NTO's budget should have a fixed component with a time horizon of more than one year (e.g., three years)*
- *The NTO should be allowed to transfer funds from one year to another*
- *The NTO should be allowed to, but not required to, sell projects to the tourism industry*
- *The NTA should take steps to involve the tourism industry more in NTO funding and ownership/control*
- *The government should still be involved in NTO funding and ownership, but share this role with the industry/private sector.*

## **7.0 Contributions, limitations, and suggestions for further research**

### **7.1 The thesis' contributions to practitioners' management implications and to academic research**

In the following section we will discuss the thesis' contribution on three main areas of academic research and for practitioners, namely: practical, theoretical, and methodical.

#### **7.1.1 Contributions to the development of policies in tourism administration**

We believe this study has value both within its specific research context, which is *travel and tourism*, as well as beyond that. We consider it to have some value for both for academics as well as for practitioners, which adds to the thesis' *practical usefulness*-dimension. We believe that the study have some strengths related to *external validity*, which has been an important consideration for this work.

##### **7.1.1.1 Contributions to the development governing principles for NTOs and governing stakeholders' policies**

The unit of analysis of this study, NTOs, has so far not been subject to much academic research. As we pointed out in Sections 1.1 and 3.1 the governing-process of NTOs, and thereby the efficiency and effectiveness of these organizations, certainly has a facet of public interest also beyond the tourism industry itself.

Furthermore, since most NTOs are (at least partially) government-controlled and funded, knowledge about sound NTO-governance principles is obviously important to the process of developing sane *government policies*. Misgovernment of the NTO may in turn lead to: waste of both public and private resources, loss of market opportunities, loss of tax revenue and foreign currency; and in general have a negative impact on the tourism industry and parts of the society in any given country involved with incoming international tourism. In this thesis we offer recommendations for the governance of NTOs. We believe these can help NTOs' stakeholders to foster organizations more efficient and effective in the marketplace - with positive effects for both the domestic tourism industry and society in general.

##### **7.1.1.2 Contributions to the development governance principles for lower-level/local tourism organizations (LTO)-administration**

Although the unit of analysis of this study is NTOs at the national level, a host of similar organizations often exist on the regional and local level. The budgets of these lower-level organizations combined often surpass the NTOs' budgets by far. It is not uncommon that these organizations are also (at least partially) funded by municipalities or other local-level government bodies, and thus consume taxpayer monies. The research conducted in

this thesis, and the recommendations derived thereof, may very well be applicable for the lower-level organizations as well. The principles we suggest, if/when applied wisely, can help a country in redeveloping its tourism organizational structure, with substantial efficiency and effectiveness gains as the end result.

### **7.1.1.3 Contributions to administrative principles for industry marketing organizations in other sectors and for ideal organizations**

The tourism industry is not the only industry that has this type of central marketing organizations. In many countries one can find central marketing organizations responsible for promoting an industry's products and services to an international or national market on behalf of that industry. Some of these are commercially/privately owned/controlled/funded, while others are government organizations or some combination of private or government entities. Some are commercial organizations dependent on a commercial market as the source of income, while others are non-commercial organizations. For instance, in Norway, there is a Trade Council for helping domestic businesses to export products or establish themselves in foreign markets, as well as a specialized Norwegian Seafood Export Council, which both are examples of similar organizations. For instance, the sub-sectors of the agricultural sector often have their own marketing organizations; in New Zealand there is a marketing organization for the export of kiwi fruits, and another for the export of wool. In the US there are marketing organizations for dairy products, poultry, and meats. These (non-tourism) organizations and NTOs have in fact several properties in common. These properties are, for instance:

- they often (partially) government funded/sponsored and controlled,
- they are seldom directly dependent on market response for their survival and growth, c) they often have several principals/stakeholders with potentially conflicting goals,
- sometimes it is unclear what/who the "market" really is, and
- they promote products and services subject to the common/collective good problem, etc. (See e.g., Section 3.1 for details).

Knowledge gained through this study with its principles and management implications could come to use in the governance of this kind of (non-tourism) organizations as well.

The same can be said about some ideal or charity organizations (e.g., benefiting cancer patients, disabled people, poor people, or the environment) promoting a cause or idea rather than a commercial product. The focus of these organizations sometimes becomes more geared towards administration and fund-raising than actually helping the beneficiaries, which could be analogous to lobbying and justification vs. market-performance in the NTO context. We believe some of the conclusions from this research may be put to use in these cases as well.

### 7.1.2 Theoretical contribution

As pointed out earlier, in order to assess how practical decisions about NTO administration should be made, it is useful to investigate whether different areas of established theory could provide any recommendations as to how these organizations can be set up and governed. From the discussion in the theory framework in Chapter 2 it becomes apparent that more than one area of theory will be needed to gain sufficient knowledge about the research questions we are investigating. The NTO context is complex and in many aspects unique, and we do not think that any known area of theory by itself is capable of providing a sufficient, comprehensive understanding of all the issues in question. Therefore, we have found it necessary to piece together several different areas of theory to try to find a basis for resolving the research problem. This compilation of relevant theory represents a comprehensive theory framework made up of theory areas that, to our knowledge, never been used in combination before.

This *abductive* approach is somewhat untraditional compared to the more common approach in academic research, which is to choose one distinct area of theory and apply that one only. We hold that this “piecing-together-of-relevant-theory-process” is a contribution to theory development on its own. This is because the theories, when put together in a comprehensive framework, gain synergistic value that surpasses the value of a single theory applied in isolation. This is in line with the abductive research approach we have described in Section 1.5, where “theoretical models or constructs from one research area can in this manner work as “heuristic tools” for theory development in another area” (Troye, 1994).

Furthermore, this process also reveals some shortcomings of existing theory, which is also theory-developing in itself. It certainly calls for further research in the areas of theory we discuss in Chapter 2, and that we have commented on after each of the five theory sections.

### 7.1.3 Methodical contribution

We think that the study of NTOs has several aspects of more academic interest. At the same time, we also aim to arrive at distinct recommendations that are useful for practitioners worldwide as well. The NTO context is rather complex with its many stakeholders with different interests and semi-public/private business environment. Furthermore, the cross-cultural perspective of the study, as well as the obstacles caused by too little natural variation in our independent variables, and even non-presence of some of the suggested principles in existing practices, make the study methodically challenging. Consequently, such a situation calls for a particular methodical approach (see Section 4.1 and 4.2 for details).

Another concern in a study like this, involving data collection from respondents that may have incentives to make statements and answer questions strategically, is to find a method to elicit responses that are based on truthfulness and professional judgments rather than private interests. As we have pointed out earlier in Section 4.4.2, we believe

we have found a method that can help mitigate this potential problem, and that can be applied in settings where strategic responding may be of concern.

We have chosen to use a new and quite untraditional scenario-analysis approach to our research problem, which we find to be potentially useful in other research settings as well. Therefore, we believe the methodical approach of this thesis is a contribution to the development of research methods in academic research. We have recently successfully applied the same scenario technique in a similar project involving a government commissioned enquiry. This enquiry investigated the consequences of a possible levy of a tourism-tax versus other financing systems for funding of the NTO, as well as funding of a host of other common tourism goods in Norway (Farstad, Skalpe and Troye, 2001). This project provides some evidence that the method can be used in other settings as well, especially when a situation, involving complex governance- and incentive problems, and many stakeholders with several conflicting concerns, calls for distinct practical recommendations that can lead to solutions that can be implemented in practice.

## 7.2 Limitations

There are several limitations and challenges that should be pointed out and considered in further research in this area.

### *External validity*

The study reported here is quite ambitious in terms of trying to arrive at recommendations that can be applied worldwide and not only for one single country or a small group of homogeneous countries. We have chosen to use a sample of countries that vary considerably with respect to national culture, geography, make-up and nature of the tourism industry, political system/culture, and so forth. Moreover, whenever possible we have also included respondents, not only from the NTO or NTA, but also industry representatives and tourism consultants or researchers. These various respondents may have different views of the issues in question, as well as influence on the decisions to be made in NTO governance. External validity has therefore been a major concern in this study, in order to make the results generalizable across national cases and across stakeholder groups. However, some important tourism countries requested to participate declined to take part in our study, e.g., Germany, Ireland, Italy, Australia, etc. Another limitation of practical nature was that our sample was confined to OECD countries only (as of 1999), which are all industrialized countries with certain economical and political common features. Our sample did not contain countries from e. g., developing countries, or transition economies outside the OECD. Many of these are also important tourism countries e.g., China, Thailand, Singapore, Brazil, Egypt, etc.

### *Internal validity*

As the theory discussion in Chapters 2 and 3 shows, the subject matter of this study can be complex and complicated in certain areas. Some of the respondents may not be familiar with e.g., the concept of Market Focus, or have substantial insight in and

understanding of the proposed cause-and-effect relationships we investigate in this thesis. We were also of course under time-, language-, and capacity-limitations during the data collection sessions, and were not able to explain all the various principles in exhaustive detail, and any possible implications thereof, to every single one of the various respondents. Given the heterogeneous make-up of the respondent groups, and the pragmatic discretion of the contact person in each country to select respondents, we do not know for sure whether every one of the various respondents have been sufficiently qualified to give good estimates of the consequences of the scenarios they were presented to. This could of course have tinted the data with some odd- or non-responses. However, as we have shown in Chapter 5, the practitioners' evaluations seem to make sense from a theoretical point of view, and do concur well with the evaluations of the theory experts. That should indicate that most of the practitioner respondents have in fact made qualified judgments, rather than spurious responses.

A measurement-related concern, however, is that the number of participants and make-up of respondent groups were not exactly the same from one country to another. The number of respondents could vary, e.g., in some countries there were only 3- 4 respondents whereas in others there could be as many as 7-8. In a few countries we were not able to include any industry representatives or researchers. Furthermore, since our contact persons in the participant countries (usually a person from the NTO or NTA in each country) were responsible for recruiting respondents in their country, some contact persons *could* have deliberately excluded some potentially important respondents from the national respondent group of e.g., political reasons. These were all conditions beyond our control, which may have influenced the measurement reliability from one country to another.

It was also quite difficult to keep the oral presentation of e.g., the research problem and related issues, the principle descriptions, and the respondent instructions, exactly identical from one country to another. In some sessions we had, for instance, an access to an overhead projector, whereas in other sessions groups were too small to make a full presentation practical. This *could* have influenced the way the respondents evaluated the scenarios. However, we have no strong indications from the data that supports such suspicions.

Furthermore, there may be other variables than the ones we have investigated here which could have an important impact on NTOs' market performance. In Figure 1.1 in Chapter 1 we have listed some of those possible factors, and there may be others that could be interesting to investigate closer to gain more knowledge about the issues important for NTO governance.

### *Construct validity*

The governance principles we have used as our independent variables are developed entirely by us. These principles are first and foremost based on real world observations of current practice and alternative principles derived from the theory review. Of course, our list of 14 principles may not be exhaustive in terms of any such principles that may already exist or be feasible. It is conceivable that other already existing, or potential and



promising principles for *budgeting*, *funding source*, or *ownership* could be added to the list and used in future research.

We have introduced several new measures in this study. For the Market Focus-dimension, our measures are for the most part adopted from already existing empirical research material in this area. The operationalizations and measures for Long-Term Perspective and Operational Freedom are, however, developed entirely by us. They may need to be validated, and possibly refined or modified, in future studies in similar contexts. For instance, there might exist areas of research where scales to probe Long-Term Perspective and Operational Freedom or similar constructs are developed, and those can contribute to refine our measures.

#### *Statistical conclusion validity*

We have pointed out earlier that the practitioner respondents vary quite a lot in professional and cultural background, and this has resulted in some heterogeneity in how a given scenario or principle has been evaluated from one respondent to another. On some aspects, our concern for external validity and practicality - has maybe been emphasized at the expense of internal validity and statistical power. The amount of heterogeneity in the data could possibly have been reduced by conducting the study as several samples in one single country, or in a small group of similar countries close in culture and ways governing NTOs. Alternatively, one could have limited the empirical work to include only academic experts, and left out the practitioners. That would probably have made the data more homogeneous, and probably increased the statistical conclusion validity on some aspects. However, one could then question whether these results would have been sufficiently valid for the real-world international setting we are interested in.

Due to practical reasons and limitations on economic and time resources, we had to settle with 14 countries and one expert group session. Given the anticipated and actual heterogeneity in respondent composition and hence the data collected, the optimal number of countries, expert groups, and respondents is probably higher than we managed to include in our samples. An increase in sample size may have yielded more statistically valid results than we were able to obtain given our resource restrictions.

### **7.3 Suggested areas of further research on government of NTOs**

We must remind the reader that although we consider this thesis complete in its present form, our research on NTOs and other similar organizations or context is still a work under progress. Further work on the subject matter could, e.g., concentrate on the following:

#### *Suggestions to improve the external validity of the results*

- Include more countries, for instance outside the OECD, in future studies of similar nature. This may improve the external validity even more.

- Re-apply or validate the research method in other settings. We believe the research method and the data collection procedures can be put to use in other settings as well. Any such projects may also serve to validate the methodical work completed in this thesis.
- Gain more knowledge of the issues at hand by applying the method developed here on lower-level tourism organizations or even similar organizations in other industries. That may help validate the results from the study reported here.

*Suggestions to improve the internal validity of the results*

- Standardize the respondent groups. One could with merit make efforts to balance and heterogenize the respondent groups in future extensions of this study or similar studies. This can be done by standardizing the number of respondents in each group, and to include the exact same make-up of respondent sub-types of NTA, NTO, industry, and researcher/consultant respondents. One could also introduce a respondent qualification procedure to secure that all respondents have a certain standard level of understanding of the concepts and issues relevant for the study.
- Redevelop, modify, and validate measures and scales used in this study. As mentioned in Section 7.2, some of the variables and their corresponding measures are new as they are developed by us, and these variables and measures may need some refinements or adjustments.
- Consider introducing other variables than may have an impact on NTOs' performance. As pointed out in the preceding section, there may be other variables (for instance those depicted in the white box on the left/center in Figure 1.1), which can be investigated with merit. Likewise, there may be other than the dependent variables we have investigated that could be included in future models.

*Suggestions to improve the construct validity of the results*

- Develop the theory framework further. Hopefully, an even more comprehensive theory framework can be constructed by including additional existing theoretical and empirical research, possibly by using contributions from e.g., organizational psychology, negotiations, and game-theory literature, etc.
- Develop and refine operationalizations and measures for testing both the *funding source's* and *organizational control's* effect on NTOs' Long-Term Perspective and Operational Freedom empirically (ref. variables not used in Appendix 7). This means that measures for probing *organizational control* (independent variable), and Long-Term Perspective and Operational Freedom (dependent variables) will have to be developed if good measures cannot be found in current literature. The reason for this suggested conceptual extension is twofold: 1) The scenario evaluations offered few clear directions on these issues. 2) This will

empirically compliment the data on Market Focus, and possibly add to the empirical support our theory regarding the relationships between our dependent and independent variables.

*Suggestions to improve the statistical conclusion validity of the results*

- Increase the sample of cases (respondent groups). This could increase statistical conclusion validity or otherwise strengthen the empirical support. In future extensions of this study one can probably merit from more observations from practitioners and (especially) from theory experts; possibly by including several international theory expert groups.
- Investigate empirically the impact of the independent variables *funding source* and *organizational control* on the dependent variables Long-Term Perspective and Operational Freedom. Among other issues, we have made some empirical findings of the relationship between the *funding source* and the organizations' Market Focus in this thesis, as reported in Appendix 7. To strengthen the statistical validity of these findings one may also in this case need to increase the sample size somewhat.

*Other suggestions to increase the practical applicability of the results*

- Arrange for a comprehensive evaluation of the proposed scenario, as outlined in Table 6.1 in our recommendations-section, by theory experts and practitioners. It would be fruitful to have the recommended scenario re-evaluated in detail by a group of theory experts and relevant practitioners to see if our recommended scenario needs to be developed further to be readily implementable in practice.
- Investigate the practical and technical aspects of the implementation of performance-based principles as outlined in Section 7.4.
- Extend the research on the *common goods problem* in tourism in general and in the NTO context. Both theoretical and empirical research is needed to find ways to motivate the private sector to participate in *funding* and *ownership* of NTOs (and similar organizations), and find solutions to make this politically attractive and possible.

## 7.4 Further work on performance-based principles

Apparently, performance-based budgeting principles are not very common in the NTO context and similar contexts. Thus little research has been done on the technicalities and practical issues of implementation of such principles. We have attempted to start this process in our simulations shown in Appendix 7. However, a number of issues still remain to be investigated in more detail:

- What basic principle of performance-based revenues should be chosen?
- What kind of performance measures should be used?
- What relative size of the fixed portion versus variable portion in a fixed/variable amount-model should be used?
- If a relative performance principle is chosen, what should be the exact criteria for selection of countries to be included in the reference group for P2 –type models (Ref. Appendix 7)?
- What should be the source of the performance-based portion of the budget, i.e., what should be the “logistics” of payment to the NTO (e.g., how should the funds be collected/transferred from the funding source(s))?
- What are the legal and administrative obstacles to an implementation of performance based principles?

Of course, some of these issues should be a matter of discussion internally in the NTOs or between the NTOs and the government or industry partners if such budgeting principles were to be considered for implementation. We do not have sufficient insight in internal conditions to be able to offer specific recommendations on these issues as of today. In any event, these questions will have to be looked at more closely before any country is advised to implement any of the principles as described and suggested above.

## 7.5 Conclusions on contributions, limitations, and suggestions

It is our opinion that this study has some contributions to research both on NTO governance and in general with regards to: theory development, methodical development, management applications, etc. However, there are some limitations and challenges that should be considered when studying the results and/or applying them, e.g., with respect to external, internal, construct, and statistical validity. Our suggestions to develop, improve, specify, or amend the work of and findings from this study are listed in Section 7.5.

We realize that it is probably not possible to develop universal recommendations on NTO governance that are both practically implementable and politically acceptable in *every* single country. However, the OECD-project “Market Orientation of National Tourism Organizations”, which this thesis is partially based on, has sparked some international interest about the issues at hand. The issues at hand have until now been an area of limited research and discussion in most tourism administrations. With the results from the current study, possibly along other studies that offer further development of relevant theory and empirical results, we hope to offer an instrument for NTO governance that will be accepted and implemented by administrations open to and willing to change to a modern, efficient, and effective NTO governance-system.

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### **APPENDIX1: Studies on the effects of market orientation**

Some selected empirical studies on the effects of market orientation<sup>41</sup>

<b>Authors (year)</b>	<b>Theoretical prediction</b>	<b>Empirical support</b>	<b>Sample</b>
Narver & Slater (1990)	Market Orientation has positive effect on Return On Assets	Partial support	84 SBUs * of a forest corporation
Narver, Jacobson & Slater (1993)	Market Orientation has positive effect on Relative Sales Growth	Significant	35 SBUs of a forest corporation
Jaworski & Kholi (1993)	Market Orientation has positive effect on Business Performance	Significant	452 companies and SBUs
Desphandè, Farley & Webster (1993)	Customer Orientation (as reported by customers) has positive effect on Business Performance	Significant	82 Japanese firms
Ruekert (1992)	Market Orientation has positive effect on Long Run Financial Performance	Significant	5 SBUs of a large U.S. firm
Pelham (1993)	Market Orientation has positive effect on Marketing/Sales Effectiveness	Significant	160 industrial (business-to-business) firms
Wood & Bhulan (1993)	Market Orientation has positive effect on Performance	Significant	24 not-for-profit hospitals
Pleshko (1993)	Market Orientation has positive effect on Business Performance	Significant	141 public and private firms
Balakrishnan (1992)	Degree of Market, Research and Manufacturing Orientation has positive effect on Bus Performance	Significant	139 manuf. co. of machine tools /manufacturing machinery
Selnes, Jaworski & Kholi (1998)	Market Orientation has positive effect on Performance	Significant	237 SBUs of Scandinavian companies
Sandvik (1998)	Market Orientation has positive effect on Performance	Significant	372 Norwegian hotels

\* SBUs= Strategic Business Units

<sup>41</sup> Adapted from "The effects of market orientation", doctoral dissertation by Kåre Sandvik, Norwegian School of Economics and Business Administration (1998)

**APPENDIX 2: Conceivable control principles for NTOs derived from application of theory**

**Appendix 2 (a)**

<b>Control principle</b>	<b>Type of control</b>	<b>Requirements</b>	<b>Purpose/benefits</b>	<b>Potential negative consequences</b>
<b>Behavior-based budget control</b>				
Stakeholders decide on plans and activities and budget accordingly each period  (Monitoring structure #1)	Behavioral –based control	-Competent stakeholders -Agreement among stakeholders and between stakeholders and agent on plans and activities -Monitoring of activities	-Assures that agent acts in the interests of stakeholders -Low agent risk	-Curbs agent's operational freedom. - Negotiation, monitoring and maladaptation cost -No outcome focus incentive for agent -Possible budget maximizing efforts
Fixed sum ("salary") is allocated each period  (Monitoring structure #1)	Behavioral –based control	-Competent agent -Reporting procedures (auditing by stakeholders)	-Moderate to high agent operational freedom -Efficient in large complex organizations with many line items, several outputs and stakeholders -Predictability of budget amount = long term planning facilitated -Low agent risk	-No financial residual claim = possible shirking -No outcome focus incentive for agent -Negotiation, monitoring and maladaptation cost -No outcome-focus incentive for agent -Legitimizing efforts -Incentive for budget maximizing
Specific project budgeting according to activities/services to be performed in a given project  (Monitoring structure #1)	Behavioral –based control  (Long run: Somewhat outcome-based)	-Competent stakeholders -Agreement between stakeholders and agent (and possibly among several project stakeholders) on project content and resources -Monitoring of project activities and outcome	-Stakeholder commitment (legitimacy) -Increases availability of additional financial resources -Moderate agent risk	-Project selling effort (i.e., budget maximizing) -Low agent operational freedom -Client lobbying -Possibly focus on special interests -Often short-term project span = long term planning may suffer -Low predictability of budget amount = long term planning hampered

**Appendix 2 (b) (continued)**

<b>Control principle</b>	<b>Type of control</b>	<b>Requirements</b>	<b>Purpose/benefits</b>	<b>Potential negative consequences</b>
<b>Outcome-based budget control</b>				
<p>Absolute market performance (“straight commission” pay) compensation paid in terms of budgets each period.</p> <p>Indirect market performance (% of tourism taxes received) compensation paid in terms of budgets each period.</p>	Outcome-based control	<ul style="list-style-type: none"> <li>-Measurability of outcome (relevant statistics)</li> <li>-Competent agent</li> <li>-Agreement among stakeholders and agent on measurement criteria</li> <li>-Some ability of agent to influence outcome</li> </ul>	<ul style="list-style-type: none"> <li>-Agent and stakeholders have stake in the same outcome</li> <li>-Curbs opportunistic behavior</li> <li>-Agent focus is concentrated on outcome mediating activities</li> <li>-Low negotiation, monitoring and mal-adaptation cost</li> <li>-No incentive for budget maximizing efforts</li> <li>-No incentive for lobbying or focus on special interests</li> </ul>	<ul style="list-style-type: none"> <li>-High agent risk</li> <li>-Low predictability of budget amount = long term planning hampered (unless budget transfer to next period is allowed)</li> <li>-Possible resistance from both stakeholders and agent (potential embarrassment)</li> <li>-Exposure to agent-uncontrollable elements affecting outcome</li> <li>-Non-market related tasks may be ignored (e.g., sustainable tourism, environment, public services)</li> </ul>
Relative market performance (“tournament commission” pay) compensation paid each period	Outcome-based control	<ul style="list-style-type: none"> <li>-Measurability of outcome (relevant statistics)</li> <li>-Competent agent</li> <li>-Agreement among stakeholders and agent on measurement criteria</li> <li>-Some ability of agent to influence outcome</li> <li>-“Comparable” reference group members (i.e., reference group members have the same/similar working conditions)</li> </ul>	<ul style="list-style-type: none"> <li>-Agent and stakeholders have stake in the same outcome</li> <li>-Curbs opportunistic behavior</li> <li>-Agent focus is concentrated on outcome mediating activities</li> <li>-Low negotiation, monitoring and mal-adaptation cost</li> <li>-No incentive for budget maximizing efforts</li> <li>-No incentive for lobbying or focus on special interests</li> <li>-Reduces the impact of chance events on budget</li> </ul>	<ul style="list-style-type: none"> <li>-High agent risk</li> <li>-Low/moderate predictability of budget amount = long term planning hampered (unless budget transfer to next period is allowed)</li> <li>-Possible resistance from both stakeholders and agent (potential embarrassment)</li> <li>-Exposure to agent uncontrollable elements affecting outcome</li> <li>-Non-market related tasks may be ignored</li> <li>-No incentive to cooperate with members of reference group</li> </ul>
Stakeholders decide on objectives and goals and budgets on the achievement of these goals each period (i.e., MBO)	Hybrid of activity- and performance-based control	<ul style="list-style-type: none"> <li>-Competent stakeholders</li> <li>-Agreement among stakeholders and between stakeholders and agent on objectives and goals and then whether o &amp; g are achieved</li> <li>-Monitoring of goal achievement</li> </ul>	<ul style="list-style-type: none"> <li>-Assures that agent’s and stakeholders’ goals are aligned</li> <li>-Moderate/low agent risk</li> <li>-Focus (goal orientation)</li> </ul>	<ul style="list-style-type: none"> <li>-Curbs agent’s operational freedom.</li> <li>-Negotiation, monitoring and maladaptation cost</li> <li>-Stakeholder disagreement = goal ambiguity = possible inefficiency</li> <li>-Possible budget maximizing efforts</li> </ul>

**Appendix 2 (c) (continued)**

<b>Control principle</b>	<b>Type of control</b>	<b>Requirements</b>	<b>Purpose/benefits</b>	<b>Potential negative consequences</b>
<b>Organizational control (through operational control)</b>				
Organizational control by the industry  (Monitoring structure #2)	Behavioral –based control	-Competent industry stakeholders -Agreement among industry stakeholders on policy and actions	- Monitoring by interest groups -Increased professionalism -Industry stakeholder commitment (legitimacy) -Direct information feedback to the industry	-Non-market related tasks may be ignored -Potential for industry lobbying -Possible focus on special interests -May curb agent’s operational freedom
Organizational control by the government  (Monitoring structure #2)	Behavioral –based control	-Competent government stakeholders -Agreement among various government stakeholders on policy and actions	-Public agency legitimacy -Low special interest focus -Organizational stability /survival (this can also be a negative aspect) -Monitoring by media -Legitimate funding of a common good (NTO)	-Bureaucratic decision process, inefficiency, budget maximization -Potential lack of business professionalism -Lack of industry stakeholder commitment (legitimacy problem) -Potential for gvt. lobbying
Organizational control by shareholders  (Monitoring structure #2)	Outcome –based control  (Behavioral –based control traits if monitoring structure # 1,2 &3 is applied)	-Competent board of directors -Procedures for reporting to shareholders -(Sellable) income producing services	-Financial residual claim (curbs shirking) -Decision flexibility/speed -Agent operational freedom -Agent focus is concentrated on outcome-mediating activ. -Low negotiation, monitoring and mal-adaptation cost -Little incentive for budget maximizing efforts, lobbying, or focus on special interests	-Likely that non-market related tasks will be ignored -Financial risk (the organization may go bankrupt) -Moderate/low predictability of budget amount (i.e., income). -Risk that shareholders could pressure NTO to focus on short-term activities.
<b>Funding source (indirect control through legitimate influence)</b>				
Funding by the industry  (Monitoring structure #3)	Indirect behavioral control (through financial auditing)	-Auditing of agent -Cooperation among industry stakeholders.	-Increased access to resources - -Stakeholder commitment (legitimacy)  -Only moderate predictability of budget amount (possibly not sufficient funding due to “free riding” by some industry stakeholders)	-Non-market related tasks may be ignored - Potential for industry lobbying -Lack of stakeholder consensus may hamper decision making, long term planning and thus increase uncertainty and agent risk
Funding by the government  (Monitoring structure #3)	Indirect behavioral control (through financial auditing)	-Agent monitoring -Budget negotiations and approval by gov. -Procedures for reporting to ministry etc.	-Non-market related tasks may be receive attention -Moderate to high predictability of budget amount -Reduces special interest focus	- Potential for government lobbying -Possible budget maximizing efforts - Bureaucratic financial auditing (time and resource consuming)

## **APPENDIX 3: List of Items, Factor Analysis, Cluster analysis, and Scenario Evaluation Questionnaire**

### **ITEMS USED FOR DATA COLLECTION in SCENARIO EVALUATIONS (Operationalizations of the 3 dependent variables)**

*This scenario (# 1-22)...*

#### **Market Focus**

1. will motivate the NTO to systematically collect and analyze information about the market's current and future needs and preferences
2. will motivate the NTO to communicate information about the market's current and future needs and preferences to the travel and tourism industry
3. will encourage the NTO to influence the travel and tourism industry to develop or improve their products and services based on information about the market's current and future needs and preferences
4. will motivate the NTO to systematically collect and respond to information about key competitors in the market (e.g., their products/services, strengths and weaknesses and strategies)
5. will motivate the NTO to use information about the market's current and future needs and preferences and about competitors in the market in the NTO's communication with the market (e.g., promo. & PR)
6. will cause the NTO to be selective (e.g., about the quality) as to what tourism products and destinations they will market

#### **Long-Term Perspective**

7. will motivate the NTO to adopt a long run perspective in their marketing plans and activities
8. will make it difficult for the NTO to pursue its long term goals
9. will not provide sufficient funds for NTO's budget
10. will lead to long-term market performance for the industry and the NTO

#### **Operational Freedom**

11. will cause the NTO to over-prioritize on activities endorsed and sponsored by special interests (e.g., not for the good of the overall travel and tourism industry)
12. will cause the NTO to spend too much resources on selling its services to the travel and tourism industry to secure NTO's funding
13. will cause the NTO's budget to fluctuate too much and make operation difficult for the NTO
14. will give the NTO freedom to make its own decisions



## Factor analysis

(Practitioners' sample, ref. items in Scenario Evaluation Form)

Rotated Component Matrix

F#	Component				Used/ Deleted
	Market Orientation	Operational Freedom	Long-Term Perspective	N/A (deleted)	
	1	2	3	4	
S01	<b>,815</b>	,122	4,239E-02	-4,764E-03	U
S02	<b>,818</b>	-,116	,114	,249	U
S03	<b>,853</b>	8,665E-02	,118	9,248E-02	U
S04	<b>,839</b>	-3,203E-03	3,164E-02	,183	U
S05	<b>,863</b>	6,414E-03	5,930E-02	-1,543E-03	U
S06	,409	,584	<b>,341</b>	-,221	U
S07	<b>,444</b>	-8,723E-02	6,096E-02	,144	U
S08	-6,115E-02	<b>,794</b>	-7,914E-03	,278	U
S09	-,161	<b>,732</b>	,145	1,258E-02	U
S10	,217	-,153	4,919E-02	<b>,734</b>	D
S11	,171	,258	8,506E-02	<b>,736</b>	D
S12	5,078E-02	,230	<b>,709</b>	4,247E-02	U
S13	-,169	<b>,617</b>	,431	-,130	U
S14	N/A	N/A	N/A	N/A	D
S15	,167	<b>,564</b>	,206	-3,465E-02	U
S16	,373	,362	<b>,497</b>	-,145	U
S17	-1,613E-02	,270	<b>,705</b>	2,225E-02	U
S18	,282	-6,601E-02	,654	,300	D

Extraction Method: Principal Component Analysis.

Rotation Method: Varimax with Kaiser Normalization.

Rotation converged in 6 iterations.

## Cluster analysis

### Market Focus

(Cases in bold type are deviant cases in the 4-cluster trial)

#### Cluster Membership

Case Number	Country	Cluster	Distance
5	NOR	1	5,226
<b>8</b>	<b>SWE</b>	<b>2</b>	<b>4,040</b>
11	ENG	1	3,833
14	CZH	1	4,084
17	SLO	1	4,328
20	AUT	4	3,520
<b>23</b>	<b>LUX</b>	<b>2</b>	<b>4,040</b>
26	SPA	1	4,134
29	POR	4	3,520
32	KOR	1	3,894
35	JAP	1	4,691
38	CAN	1	4,105
41	FIN	1	4,250
44	DAN	3	,000
47	EXPERTS	1	4,315

## Long-Term Perspective

(Cases in **bold** type are deviant cases in the 4-cluster trial)

### Cluster Membership

Case Number	Country	Cluster	Distance
6	NOR	2	4,564
9	SWE	2	4,656
12	ENG	3	5,603
15	CZH	3	5,070
<b>18</b>	<b>SLO</b>	<b>4</b>	<b>3,627</b>
21	AUT	3	4,948
24	LUX	1	4,157
27	SPA	3	4,234
30	POR	1	4,600
33	KOR	3	4,480
36	JAP	1	3,521
<b>39</b>	<b>CAN</b>	<b>4</b>	<b>3,627</b>
42	FIN	2	4,392
45	DAN	3	4,294
48	EXPERTS	3	3,308

## Operational Freedom

(Cases in **bold** type are deviant cases in the 4-cluster trial)

### Cluster Membership

Case Number	Country	Cluster	Distance
<b>7</b>	<b>NOR</b>	<b>1</b>	<b>3,338</b>
10	SVE	2	4,071
13	ENG	3	3,873
16	CZH	4	4,626
19	SLO	4	4,297
22	AUT	4	5,940
25	LUX	4	3,254
28	SPA	4	2,172
31	POR	2	3,427
34	KOR	4	2,783
37	JAP	4	3,936
40	CAN	2	3,322
43	FIN	4	5,509
46	DAN	3	3,873
<b>49</b>	<b>EXPERTS</b>	<b>1</b>	<b>3,338</b>

## Scenario evaluation questionnaire

(Questionnaire used for the practitioners' sample. A slightly modified questionnaire was used for the theory experts' sample, i.e., questions 11 and 14 removed in the scenario evaluation form.)

### **Introduction**

*The main purpose of National Tourism Organizations (NTO) is to market a country as a tourist destination. The objective of this project is to evaluate how such organizations can be organized and financed in order to enhance their performance and strengthen their role as a promoter of tourism. In the following you will be asked to evaluate alternative scenarios for financing and organizing the of NTOs in terms of the likelihood that each scenario will affect the NTOs' effectiveness and efficiency, improve the NTOs' working conditions - and a number of other practical implications.*

*More specifically, our goal is to identify arrangements that may improve NTOs' performance with respect to their ability to*

- *increase the number of foreign tourists in the long and short run*
- *increase the economic value of tourism in the long run and the short run*
- *increase the attractiveness of the country as a destination in international markets*
- *etc.*

*By "scenarios" we refer to the several combinations of various principles for funding and organizing the NTO we have identified to be applicable. Each principle is explained on the following page. It is important that you read the explanations of the various principles carefully.*

*First, you will also be asked to evaluate to which degree the listed principles are in effect in your country, using the SIMILARITY EVALUATION FORM. Second, you are asked to proceed to evaluate the scenarios assigned to you, using one SCENARIO EVALUATION FORM for each scenario.*

*Please indicate your evaluation on each item by circling the number that best corresponds to your opinion.*

**Thank you in advance!**

<b>Principle</b>	<b>Explanation/comments</b>
1. NTO's budget one year is based on last available estimates of the <b>amount of money</b> spent by incoming visitors and/or estimated <b>number</b> of incoming visitors the previous year	1. This can be based on a certain percentage (e.g., 0.05%) of the estimated money spent by incoming visitors. This principle is analogous to the percentage-of-sale rule used in companies to determine advertising budgets. A substitute for (or a supplement to) visitor expenditure measures can be the number of incoming visitors (or number of bed nights, port arrivals etc) the previous year
2. NTO's budget one year is tied to the <b>increase/decrease</b> in the amount of money spent by incoming visitors (or the number of visitors in NTO's country) <b>relative to</b> "comparable" countries the previous year	2. This can be based on an amount per percentage point increase or decrease in estimates of amount of money spent by incoming visitors or in the number incoming of visitors. It will only lead to decreases (increases) in the NTO's budget to the extent that economic value of tourism in the country or number of incoming visitors falls behind what was achieved in "comparable" countries.
3. NTO's budget is based on sale and participation in <b>specific projects</b>	3. This budget allocation depends on the NTO's sale of projects to the industry or the government. These projects can both be initiated by the industry (e.g., hotel chains, regions, resort areas), the NTA (government body dealing with tourism), and the NTO itself.
4. NTO's budget is negotiable and funded based on <b>overall evaluation of the NTO's marketing plans</b> each year	4. This principle involves negotiations between the NTO and the NTA and/or the industry. The budget is determined for one year at the time (or any other time period agreed upon) based on assessments of needs and plans for NTO's activities.
5. NTO's budget is based on a <b>fixed sum</b> decided each year	5. This principle is similar to principle 4 - but is not directly linked to the NTO's marketing plans.
6. NTO's budget is tied to the <b>achievement of a number of goals</b> that are agreed upon each year	6. This principle involves setting a set of prioritized goals (e.g., overall increase in visitor traffic, increases for certain types of visitors, increases in desired visitor traffic in prioritized regions or in industry segments etc.)
7. NTO's budget is based on the revenue generated from <b>taxation on visitors and the traveling public</b>	7. This principle channels government revenue (portions of it or in full) generated from taxation on consumers of travel and tourism products and services to the funding of NTO's budget. (Such taxes and fees can be hotel tax, flight seat fees, arrival/departure tax, port fees etc.)
8. The NTO's budget is based on the revenue generated from <b>fees and taxes paid by the travel and tourism industry</b>	8. This principle channels government (portions of it or in full) revenue generated from payments received from operators of travel and tourism businesses to the funding of NTO's budget. (Such taxes and fees can be mandatory marketing fees, casino taxes, aviation taxes or operating permit-dues etc.)
9. NTO is funded by <b>the government</b>	9. The NTO's budget is funded by the government- including local governments/municipalities/provinces.
10. NTO is funded by <b>the travel and tourism industry</b>	10. The NTO's budget is funded by the industry, including contributions from public sector & enterprises.
11. NTO is funded jointly by <b>the industry and the government</b>	11. Both the industry and the government contribute significantly to the NTO's budget.
12. NTO is a <b>non-profit</b> organization owned by and responsible toward <b>the travel and tourism industry</b>	12. This implies that the travel and tourism industry is the "owner" or principal.
13. NTO is a <b>non-profit org.</b> Owned by and responsible toward <b>the governm.</b>	13. This implies that the government is the "owner" or principal.
14. NTO is a <b>limited corporation</b> owned by <b>shareholders</b> within and outside the travel and tourism industry	14. This implies that the NTO is run similar to a regular enterprise in the private sector that is only responsible to the shareholders.

(Used for the practitioners' sample only)

SIMILARITY EVALUATION FORM		Please, indicate the degree to which the principles are descriptive of the situation in your country		
Principle		Does NOT describe the situation	Describes the situation	Don't know
NTO's budget one year is based on last available estimates of the <b>amount of money</b> spent by incoming visitors (and/or estimated <b>number of incoming visitors</b> ) the previous year		1 2 3 4 5	6 7	8
NTO's budget one year is tied to the <b>increase/decrease</b> in the amount of money spent by incoming visitors (or number of visitors in NTO's country) <b>relative to "comparable" countries</b> the previous year		1 2 3 4 5	6 7	8
NTO's budget is based on sale and participation in <b>specific projects</b>		1 2 3 4 5	6 7	8
NTO's budget is negotiable and funded based on <b>overall evaluation of the NTO's marketing plans</b> each year		1 2 3 4 5	6 7	8
NTO's budget is based on a <b>fixed sum</b> decided each year		1 2 3 4 5	6 7	8
NTO's budget is tied to the <b>achievement of a number of goals</b> that are agreed upon each year		1 2 3 4 5	6 7	8
NTO's budget is based on the revenue generated from <b>taxation on visitors and the traveling public</b>		1 2 3 4 5	6 7	8
NTO's budget is based on the revenue generated from <b>fees and taxes paid by the travel and tourism industry</b>		1 2 3 4 5	6 7	8
NTO is funded by the government		1 2 3 4 5	6 7	8
NTO is funded by the travel and tourism industry		1 2 3 4 5	6 7	8
NTO is funded jointly by the travel and tourism industry and the government		1 2 3 4 5	6 7	8
NTO is a non-profit organization owned by and responsible toward the hospitality industry		1 2 3 4 5	6 7	8
NTO is a non-profit organization owned by and responsible toward the government		1 2 3 4 5	6 7	8
NTO is an limited corporation owned by shareholders within or outside the travel and tourism industry		1 2 3 4 5	6 7	8

**SCENARIO EVALUATION FORM**

**This scenario...**

**Respondent initials.....**

**Scenario # .....(1-22)**

1) will motivate the NTO to systematically **collect and analyze information** about the market's current and future needs and preferences

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

2) will motivate the NTO to **communicate information** about the market's current and future needs and preferences **to the travel and tourism industry**

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

3) will encourage the NTO to **influence the travel and tourism industry** to develop or improve their products and services **based on information** about the market's current and future needs and preferences

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

4) will motivate the NTO to systematically **collect and respond to information about key competitors in the market** (e.g., their products/services, strengths and weaknesses and strategies)

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

5) will motivate the NTO to **use information** about the market's current and future needs and preferences and about competitors in the market **in the NTO's communication with the market** (e.g., promotion & PR)

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

6) will motivate the NTO to adopt a **long-run perspective** in their marketing plans and activities

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

7) will cause the NTO to be **selective** (e.g., about the quality) as to what tourism products and destinations they will market

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

8) will cause the NTO to **over-prioritize** on activities endorsed and sponsored by **special interests** (e.g., not for the good of the overall travel and tourism industry)

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

9) will cause the NTO to **spend too much resources on selling its services** to the travel and tourism industry to secure NTO's funding

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

10) will cause the NTO to **spend too much resources on "lobbying"** the government to secure NTO's funding

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

11) will cause a **negative reaction** (e.g., from the t & t industry or the visitors)

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

12) will **not provide sufficient funds** for NTO's budget

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

13) will cause the NTO's **budget to fluctuate too much** and make long-term planning difficult for the NTO

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

14) will increase **the commitment of the travel and tourism industry as a whole** to the work of the NTO

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

15) will give the NTO **freedom to make its own decisions**

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

16) will lead to **improved long-term international market performance** for the t & t industry in NTO's country

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

17) will make it **difficult for the NTO to pursue its long-term goals**

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

18) will create a system that is **not resource-efficient** (e.g., costs more than it pays)

Strongly disagree 1 2 3 4 5 6 7  
Strongly agree 8  
Don't know

Any other potential positive or negative consequences?

Positive.....

.....

Negative.....

.....

.....

.....

.....

(For more comments, please use backside of form)

## **APPENDIX 4: Sample of scenarios**

**4 out of 22 different scenarios are shown here**

**(Scenarios are representing the operationalizations of the independent variables)**

### **Scenario 1**

- *NTO's budget is negotiable and funded based on overall evaluation of the NTO's marketing plans each year*
- *NTO is funded by the travel and tourism industry*
- *NTO is an unlimited corporation owned by shareholders within or outside the t & t industry*

8/10/00

OECD



1

### **Scenario 2**

- *NTO's budget one year is tied to the increase/decrease in the amount of money spent by incoming visitors (or the number of visitors in NTO's country) relative to "comparable" countries the previous year*
- *NTO is funded jointly by the industry and the government*
- *NTO is a non-profit organization owned by and responsible toward the travel and tourism industry*

8/10/00

OECD



2

## Scenario 8

- *NTO's budget is based on the revenue generated from **taxation on visitors and the travelling public***
- *NTO is funded by the **government***
- *NTO is a non-profit organization owned by and responsible toward **the government***

8/10/00

OECD



3

## Scenario 10

- *NTO's budget is based on a **fixed sum** decided each year*
- *NTO is funded jointly by the **industry and the government***
- *NTO is a non-profit organization owned by and responsible toward the **travel and tourism industry***

8/10/00

OECD



4



## **Appendix 5: What determines organizational focus and market orientation of the NTO?**

We have emphasized earlier that we are not interested in testing of theory in this particular study. The main reason is because in the context we are working with, this is not practically possible, as explained in Chapter 4, Section 4.2. However, it is still interesting to investigate if there is any empirical relationship between any of our variables that could support our assumptions, such as that the funding source will have an impact on the organization's focus as theorized in Figure 2.3 in Chapter 2.

Ideally we would want to investigate any empirical relationship between the three independent and the three dependent variables. The reasons why we have chosen to concentrate on only the relationship between the independent variable *funding source* and the dependent variable Market Orientation (Market Focus) are as follows:

1. There is too little statistical variation in the two other independent variables *budgeting principle* and *ownership* in terms of how current practices of NTOs are described by the respondents (Ref. Table 5.1 in Chapter 5).

For instance, there are virtually no countries that have implemented any of the direct or indirect performance-based principles P1, P2 and P7, P8. These are, for instance, the most interesting in terms of impact on Market Orientation. The only ones that are used in current practice are the behavior-based principles like P5 (majority) and P3 and P4 (a few). The latter two are seldom the leading principle, merely used to some limited degree of e.g. project-based funding. Thus it would be meaningless to run a statistical analysis with the *budgeting principle* as an independent factor.

Likewise, there is little variation in how NTOs are owned/controlled. Almost all are for the most part government controlled (P13), a majority 100% government controlled. Only a few NTOs are subject to any significant degree of tourism industry ownership (P12). None are completely organized as a limited company and thus as commercial entity (P 14).

The only one of the independent variables that has sufficient variation to make a meaningful statistical analysis is the *funding source*. There is quite a lot of variation in the ratio of government versus industry funding. Some NTOs are 100% government funded, while a few are about 50%/50% in terms of government and industry funding. Most are somewhere in-between, the average is about 72% government and 28% industry funding.

2. Of practical reasons we had to select one dependent variable only, because we did not want to overload our NTO respondents. In terms of the dependent variables, we think that Market Orientation is the most important.

If we were to measure all three dependent variables, the extra questionnaire would have been too long, and we could risk that we got a low response rate, poor data and to alienate the respondents (ref. also the data collection procedure in Section A7.1.1 below). Of the

three dependent variables, Market Orientation is probably the most important, because it measures the focus of the organization, which we believe is the most important in terms of the NTO's efficiency, effectiveness and market performance. Without market orientation, it does not matter how long-term oriented or operationally autonomous the organization is. We wanted to measure the construct in more detail than only through the scenario evaluations. A separate study and questionnaire was then necessary.

3. Of the three dependent variables we only had access to tested, validated and recognized measures from previous literature for the Market Orientation-construct. We had no pre-developed equivalent measures for the Long-Term Focus and Operational Freedom-constructs available.

This is the reasons why we chose to concentrate on the Market Orientation-dimension only and left out the two others in this separate study.

## A5.1 Results: NTOs' self-evaluation

Thus, in this section we will empirically address two issues:

- How do the NTOs perceive their own orientation to the market?
- To what extent does the organizational focus of the NTO reflect the importance of government and/or the industry as source of income?

### A5.1.1 Procedure

To assess the Organizational Focus and Market Orientation of the NTOs in the sample, we developed a questionnaire for NTO key personnel consisting of two parts:

1. a section addressing Organizational Focus (i.e. prioritization of various stakeholders) of the NTO in the preparation of its strategic plans (see Appendix 6, part A)
2. a section intended to tap NTO's degree of Market Orientation (see Appx. 8, part B)

We asked a representative(s) from NTO staff (e.g. general manager or others with thorough knowledge of the organization) to complete a four page questionnaire dealing with Organizational Focus and Market Orientation of the NTO. The questionnaires and scales are developed in earlier published studies and were modified to fit the NTO context. The questionnaire was handed out to selected NTO representatives in each country at the end of the interview session and then submitted to us by fax after the NTO representatives had completed the questionnaire. 13 of the 14 participating countries completed and returned the questionnaire. Many of the aspects covered in the Organizational Focus and Market Orientation-questionnaire correspond to (but are not identical with) the items used to tap Market Orientation/market focus in the scenario evaluation earlier in this report.

The construct, Organizational Focus, reflects the NTO's attention to and prioritization of

- the market
  - Needs and preferences of end users
  - Increase the long-term potential of T&T products/services

- Priorities and strategies of competitors
- the government,
  - Interests and opinions of national and local governments
- the industry
  - Interests and opinions of biggest T&T companies
  - Interests and opinions of small- and medium sized T&T companies

Market Orientation covers the following dimensions:

- Information Generation  
*Collect information about the market, competitors, and the business environment*
- Information Dissemination  
*Distribute/exchange information within the NTO and the industry*
- Market Orientation Domain-width  
*Make efforts to identify and respond to new markets, new segments, and new competitors*
- Information Responsiveness  
*Change strategies as markets, competitors, and business environment change*

The data representing the distribution of government versus industry/private budget portion were collected from informational material (e.g. annual reports, fiscal budgets etc.) given us by the respondent NTOs/NTAs themselves.

### A5.1.2 NTOs' self-assessment of Organizational Focus and Market Orientation

By *focus* we refer to *market-*, *industry*<sup>42</sup>-, or *government*-orientation as the dominating strategic focus of the NTO in question. Figure A7.1 shows the self-assessment of organizational focus and market orientation for Canada and the other 12 countries in the study. We have picked Canada as an illustrative case because of the Canadian NTO's apparent high degree of market orientation compared to other countries in our sample. Canada has the lowest portion of government funding 50%, while the average cross-sample portion is 72%. As we see, the Canadian respondent perceives the Canadian NTO to have a stronger focus on the market than the 12 other respondents perceive their respective NTOs to have.

While other NTO representatives in the practitioners' sample rate the interests of government and the market as about equally important and more important than industry interests in strategic planning, the Canadian respondent clearly reports emphasis on the market as the dominant focus. Figure A7.1 shows that the Canadian respondent reports stronger focus on the *market* than the other respondents do and *relatively* less focus than the others with respect to both industry and government interests. We believe that this is a quite positive pattern with respect to a proper focus of a NTO (i.e. that the main-focus should be on the market). This is because both the government and the industry would eventually benefit from a market-focused NTO.

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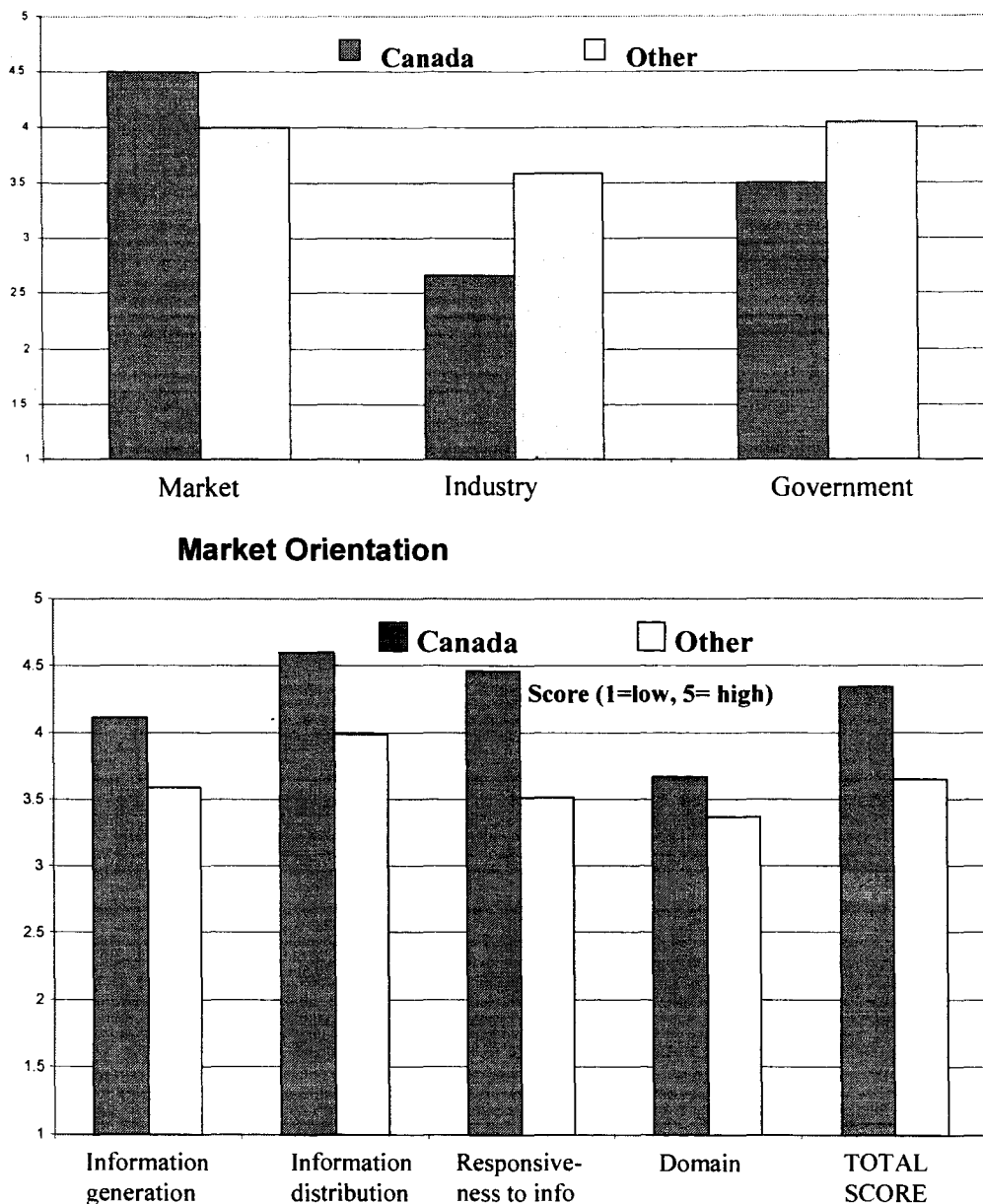
<sup>42</sup> By the term *industry* we refer to non-government business stakeholders with interests in the tourism sector (i.e., tourism (as a demand-based phenomenon) cuts across many traditional industries)).

Compared to the other respondents, the Canadian respondent also perceived the NTO as more market-oriented in terms of all four market orientation-dimensions. Since these scores are based on one observation per country, we should not exaggerate the significance of this finding. Intuitively, however, the findings seem to have face validity.

### A5.1.3 The relationship between importance of government as source of revenue and NTOs' organizational focus and market orientation

Is it so that NTOs that receive a larger percentage of their total budget from the government also have a stronger focus on government and lower scores in terms of market focus and market orientation?

**Figure A5.1**  
**Organizational Focus and Market Orientation of Canada and other countries**



This issue was addressed by correlating the percentage of government funding with the scores on each of the various dimensions of organizational focus and market orientation. The results are shown in Table A5.1a and b.

**Table A5.1a**  
**Correlation between percentage of NTO's budget from government and different foci of the NTO**

	Percentage of budget from government
Market focus	(0.18)
Industry focus	(-0.11)
Government focus	+0.58

( ) = non- significant at  $p < 0.15$  level

**Table A5.1b**  
**Correlation between percentage of NTO's budget from government and dimensions of Market Orientation of the NTO**

	Percentage of budget from government
Information generation	(-0.10)
Information dissemination	-0.48
Information responsiveness	-0.33
Domain Width	(-0.13)
Total index	-0.35

( ) = non- significant at  $p < 0.15$  level

As we see, the amount of government funding appears to be positively related to the organizations' tendency to have a government focus. There is, however, no systematic tendency that the magnitude of government funding is negatively related to market and industry focus.

Unfortunately, since the majority of NTO funding worldwide comes from government sources, it appears that government funding is negatively related to important facets of market orientation. A negative correlation was observed between the percentage of funding from government and the self-assessed tendency to

- disseminate information to the industry ( $r = -0.48$ ,  $p < 0.10$ )
- respond to information ( $r = -0.32$ ,  $p < 0.15$ )

It is also interesting to note that government funding apparently is not related to *information generation*. While both information dissemination and responsiveness are

more involving activities and probably require a strong motivational basis in the organization, it might be easier for an external stakeholder to instruct the NTO to carry out certain information generation activities (e.g. collection of census data, surveys, etc).

The correlation with the overall market orientation index (based on all items across sub-dimensions combined) was fairly high (-0.35) and negative, suggesting that high government involvement may not promote market orientation.

#### A5.1.4 Conclusion: Does source of revenue matter?

Again, a caveat is in order: We must bear in mind that

- the findings are only based on 13 observations,
- and the measures of organizational focus and marketing orientation are only based on one observation per country.

There are, however, at least three reasons why we should have some confidence in the results:

- One reason is methodological: The two sets of measures, budget on one side and evaluations on the other, are collected independently of each other<sup>43</sup>. We can have more trust in the correlations between the two sets of variables than what is warranted if both sets had been based on the same data source.
- A second reason is that some of the correlations are fairly high
- A third reason is that the findings corroborate our initial preposition and also the results of our theory experts' and practitioners' scenario evaluations.

We therefore interpret the findings to imply that the source of income may influence the NTOs approach to the market and their stakeholders. This finding does not imply that the government should not provide the necessary means for the NTO's existence. What the results do imply is that an important consideration for the government is to avoid that the NTO diverts its attention from the most important stakeholder: The tourist market.

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<sup>43</sup> Consequently the correlations are not artificially inflated due to common method variance

## APPENDIX 6: Organizational Focus and Market Orientation Assessment Questionnaire

### 6A: Organizational Focus questionnaire

<b>*Statement</b>	<i>Please indicate to which degree you agree to the claims</i>					
In the preparation of our market/strategic plans, to make sure that none of our owners or sponsors would feel unfairly treated or set aside is among our most important considerations.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
In this organization, we consider the needs and preferences of the end-users of our country's travel and tourism products and services (e.g. visitors/tourists) to be among our most important considerations in the preparation of our market/strategic plans.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
We consider the interests and opinions of the biggest companies of our country's travel and tourism industry to be among our most important considerations in the preparation of our market/strategic plans.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
We consider the interests and opinions of the small or medium sized companies of our country's travel and tourism industry to be among our most important considerations in the preparation of our market/strategic plans.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
To increase the long-term market potential of our country's t & t products and services in general is among our most important considerations in the preparation of our market/strategic plans.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
The interests and opinions of the national and local governments are among our most important considerations in the preparation of our market/strategic plans.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
How we can maximize our financial support from national and local governments is among our most important considerations in the preparation of our market/strategic plans	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
The priorities and strategies of competitors from other countries are among our most important considerations in the preparation of our market/strategic plans.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
Whatever we can do that will generate the greatest amount of visitor/tourism receipts (i. e., sales/traffic) for our country in general will be among our most important considerations in the preparation of our market/strategic plans.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6

Adapted from Jacobsen, Erik W. (1998), "Finansiering og styring av fellesgodeprodusenter: områdeorganisasjoner i reiselivsnæringen som empirisk arena", Doctoral dissertation, Norwegian School of Economics and Business Administration, Norway.

#### **\*NOTE:**

"End-users" is in this questionnaire referring to tourists/visitors (i.e. individuals, groups or organizations) that have traveled, or will (actually or potentially) travel, to your country.

"The industry" or "t & t industry" is in this questionnaire referring to the travel and tourism industry in your country (including companies owned both by the private and public sector).

"Competitors" or "competitor countries" is in this questionnaire referring to organizations or companies from other countries, which promote (or sell) travel and tourism products and services in competition with your organization - or any other organizations and companies from your country.

**Please proceed to answer the questions on the following two pages.**

**6B: Market Orientation questionnaire**

<b>*Statement</b>	<i>Please indicate to which degree you agree to the claims</i>						
In this organization we meet with the (most important) end-users of our country's travel and tourism products and services at least once a year to find out what they will need in the future.	Strongly disagree	1	2	3	4	Strongly agree	Don't know
We arrange for representatives from the travel and tourism industry in our country to meet with end-users to find out how we can serve the end-users better.	Strongly disagree	1	2	3	4	Strongly agree	Don't know
In this organization we plan and conduct market research ourselves.	Strongly disagree	1	2	3	4	Strongly agree	Don't know
We are fast to detect changes in the end-users' product preferences regarding the travel & tourism (t & t) products and services of our country.	Strongly disagree	1	2	3	4	Strongly agree	Don't know
We poll end-users of our country's travel and tourism products and services at least once a year to assess the quality of these products and services.	Strongly disagree	1	2	3	4	Strongly agree	Don't know
We often talk with those that can influence our end-users' purchases (e.g. travel agencies, travel secretaries)	Strongly disagree	1	2	3	4	Strongly agree	Don't know
We collect industry information through informal means (lunch with t & t industry friends, hotel managers, tour-operators, government officials etc.)	Strongly disagree	1	2	3	4	Strongly agree	Don't know
We are slow to detect fundamental shifts in the travel and tourism industry (e.g. new competitors, new technology, regulation)	Strongly disagree	1	2	3	4	Strongly agree	Don't know
We periodically review the likely effect of changes in our business environment (e.g. VAT/taxes, new alliances new patterns of travel) on end-users.	Strongly disagree	1	2	3	4	Strongly agree	Don't know
A lot of informal "hall talk" in our organization concerns competitor countries' tactics or strategies.	Strongly disagree	1	2	3	4	Strongly agree	Don't know
We have meetings with representatives from our country's travel and tourism industry and our government at least once a year to discuss market trends and developments.	Strongly disagree	1	2	3	4	Strongly agree	Don't know
Marketing personnel in our organization spend time discussing end-users' future needs with representatives from our country's travel and tourism industry.	Strongly disagree	1	2	3	4	Strongly agree	Don't know
Our organization regularly exchanges documents (e.g. reports, analyses) that provide information on end-users with the t & t industry.	Strongly disagree	1	2	3	4	Strongly agree	Don't know



<b>*Statement</b>	<i>Please indicate to which degree you agree to the claims</i>					
When we find out that something important happens to a major group of end-users or market, we will tell our contacts in the t & t industry about it right away.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
We make sure that data on end-user satisfaction are disseminated in the t & t industry at all levels on a regular basis.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
There is minimal communication between our organization and the t & t industry.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
There is minimal communication between our organization and the government.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
When we find out something important about the end-users, we are slow to alert the t & t industry.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
When the t & t industry finds out something important about the end-users, the t & t industry is slow to alert us.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
It takes us forever to decide how to respond when our competitors from other countries' change their prices.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
Principles of market segmentation are always taken into consideration when we discuss new product development with the t & t industry.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
For some reason or another, we tend to ignore changes in our end-users' product and service needs.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
We periodically review product and service development efforts with the t & t industry to ensure that they are in line with what the end-users want.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
Our business plans are more driven by resource advances than by market research.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
We periodically get together with representatives from the t & t industry and the government to plan a response to changes taking place in our business environment.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
The products and services we promote depend more on politics or special interests than on real market needs.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
The activities of our organization are well coordinated with the activities of the government and the t & t industry.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6

<b>*Statement</b>	<i>Please indicate to which degree you agree to the claims</i>					
We have no formal routine to alert the t & t industry when we learn about dissatisfaction among end-users concerning the t & t products and services of our country.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
Even if we came up with a great marketing plan, we would probably not be able to implement it in a timely fashion.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
We are quick to respond to changes in our competitor countries' products and services offerings.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
When we find out that end-users are unhappy with the quality of our products or services, we take corrective action immediately.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
When we find out that the end-users would like a modified product or service, the t & t industry would make concerned efforts to make the required modifications.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
The people in this organization frequently discuss how we can discover the end-users' needs.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
We collect information about potential end-user groups/segments not currently being served by the t & t industry of our country.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6
We concentrate all marketing attention toward current end-users and current competitor countries.	Strongly disagree 1	2	3	4	Strongly agree 5	Don't know 6

**Thank you for your effort!**

## **Appendix 7: What if NTOs' budgets were performance-based?: Performance-based budgets simulations**

As the scenario evaluation results discussed earlier in Chapter 5 indicate, the respondents generally viewed some of the performance-based budgeting principles to encourage Market Orientation of NTOs. Notwithstanding, the respondents expressed more skepticism when they evaluated the effect of the performance-based principles on Long-Term Focus.

One reason for this skepticism could be a concern for *timing*: Decisions are made for the present or future, incentives are tied to achievements in the past. Another concern that was expressed by some of the respondents is that the impact of the NTO is small or negligible compared to the effects of a host of other factors over which the NTO has little or no control. Consequently, wise decisions in difficult times may harvest little or no rewards, while unwise decisions when conditions are favorable may lead to few or no negative consequences for the organization.

In this section we will address one objection against performance based budgets. It can be argued that fluctuations in the market demand would lead to unwanted fluctuations in NTO's resources, making long-term planning difficult. Based on data on tourism receipts for Canada and some other countries for the years 1995 to 1998 (see end of this Appendix 7), we have applied two different performance principles in combination with a fixed sum component to calculate the impact on the budget of the CTC<sup>44</sup>. This is done only for illustration and the calculated revenue for the NTO would only correspond to the actual revenue if the budgeting principle itself had no effect on market demand. The potential incentive effect of the performance-based principle is therefore ignored.

### **A7.1 Factors that affect performance-based budgets**

It is obvious that the size of performance based budgets is affected by at least the following three factors:

- the kind of performance on which the budgets are based
- the type of procedure used for linking budget to performance, and
- the degree to which the budget is based on performance alone or in addition contains e.g. a fixed amount

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<sup>44</sup> The actual amount of the Canadian Tourism Commission's (CTC, Canada's NTO) budget for the budget year 1998-1999 is "moved back" to the budget year 1995-1996, which is the base year in our simulations. This is done to see what would have happened if the various models had been implemented with the current budget amount in effect from the base year. The calculations are not adjusted for inflation and currency fluctuations. The principles are conceptually explained in Table 5.1.

*Kind of performance*

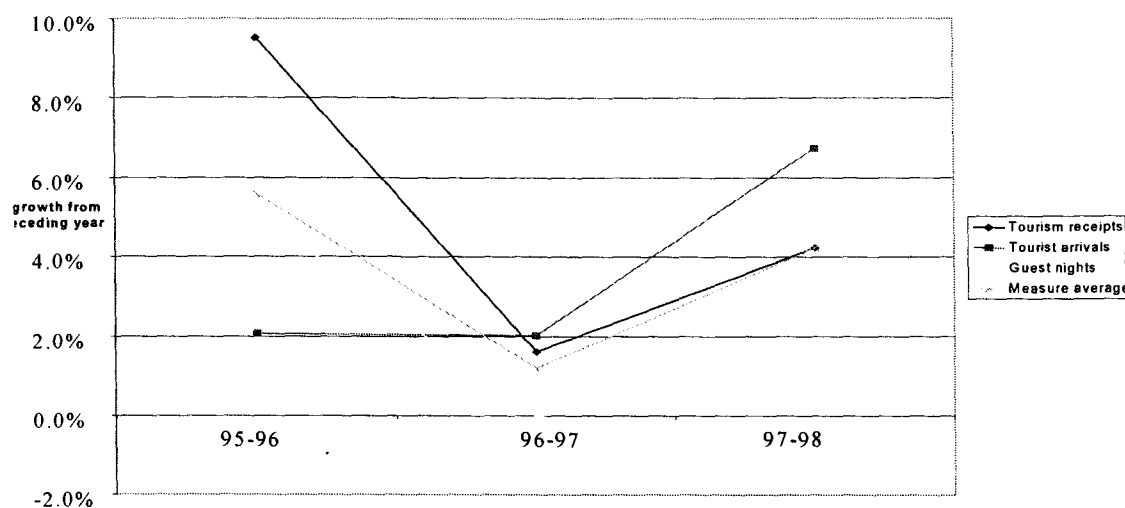
One reason for choosing one performance measure over another is obviously that the preferred measure is closely related to the goals we might have for the NTO. Thus a measure of value creation (e.g. tourism receipts) may be preferable to a performance measure that only reflects number of tourists. However, the more alternative performance variables correlate, the less it matters which is chosen as basis for determining budgets.

**Table 7.1**  
**Correlation between various performance-measures, Canada**

	Tourism receipts	Tourist arrivals	Guest nights
Tourism receipts	1.00		
Tourist arrivals	0.87	1.00	
Guest nights	0.99	0.79	1.00

**Figure A7.1**  
**Pattern of various performance-measures. Canada**

Variations in different tourism performance measures (tourism receipts, arrivals, and nights) Canada

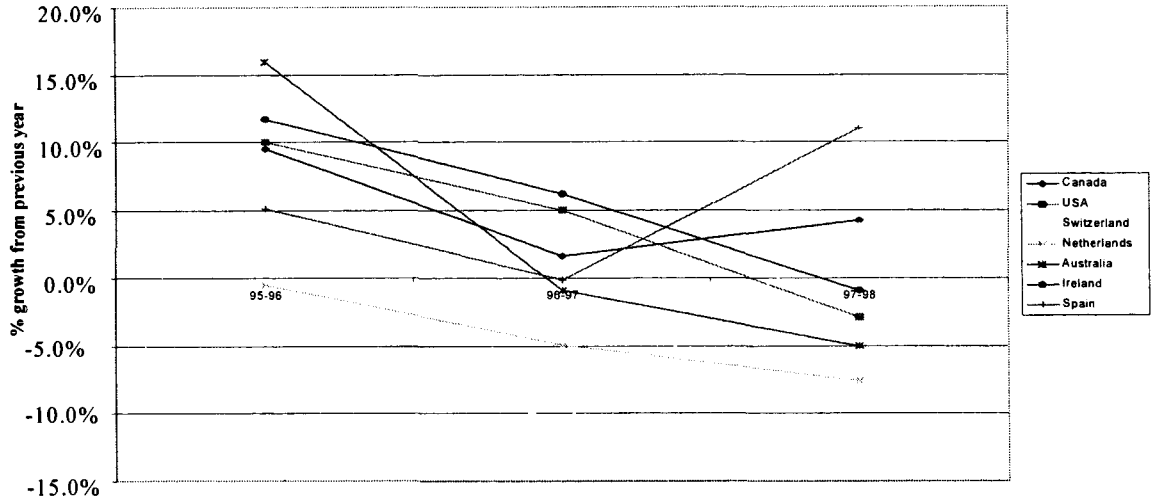


As Figure A7.1 and Table A7.1 show, the pattern of various performance variables is fairly similar. As we see the correlation between *number of guest nights* and *tourist receipts* is as high as 0.99 and the lowest (between guest nights and arrivals) is still as high as 0.79. It is therefore not very important which performance measure is chosen.

Some of the principles reflect relative performance of country X in the sense that the market performance of country X (in this case Canada) is weighted by the market performance of “comparable” countries. To the extent the pattern of performance differs between country X and the other countries in the pool, the performance-based budget can deviate considerably from what would be the case if the performance of these

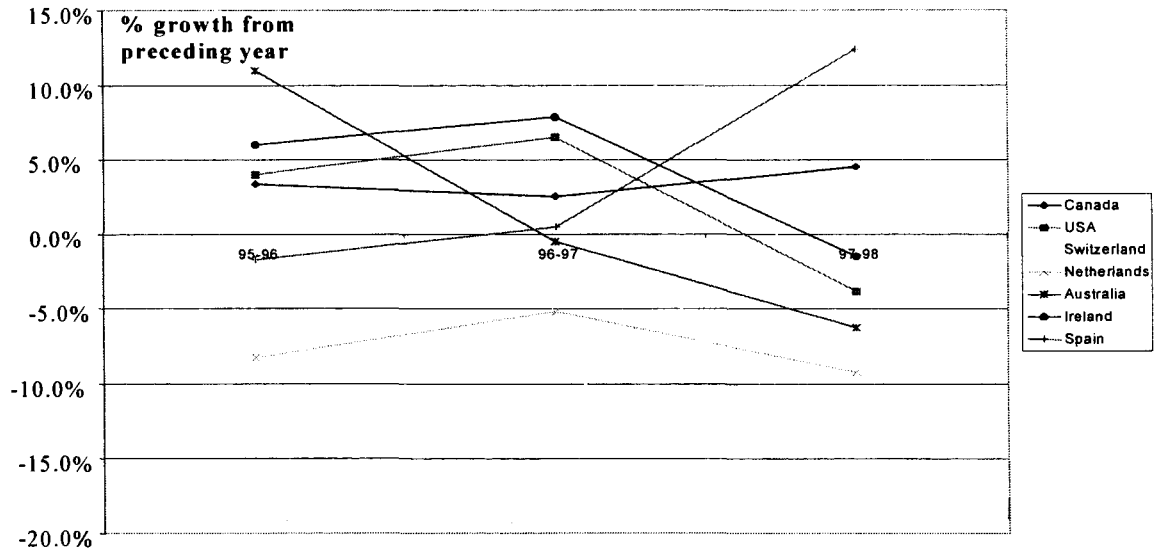
**Figure A7.2a**  
**Growth rate in tourism receipts for various countries**

Growth rates (in tourism receipts) for Canada and "comparable" countries



**Figure A7.2b**  
**Relative growth rate in tourism receipts for various countries<sup>45</sup>**

Relative performance (tourism receipts) for Canada and "comparable" countries



<sup>45</sup> "Relative performance" is calculated as the growth rate (% change in the performance measure from the previous year) for the country less the average performance (average growth rate) of the other countries in the reference group. For countries with stronger growth than the average growth of the reference group, relative performance will be positive, while weaker growth will yield negative relative performance.

**Table A7.2**  
**Overview of the different principles that are applied to calculate consequences for the NTO's budget**

TYPE OF PERFORMANCE - BASED PRINCIPLE	VARIABLE COMPONENT +	Fixed component as percentage of CTC's budget in 1995
<b>ABSOLUTE</b>  P1 : Variable part of budget based only on NTO's performance the previous year	P1a:	20%
		30%
	Variable part of budget based on absolute growth in tourism receipts the previous year	.
		70%
	80%	
<b>RELATIVE/BENCH-MARKING</b>  P2: Variable part based on performance the previous year relative to performance of six "comparable" countries	P1b:	20%
		30%
	Variable part of budget based on 1.25% of sales tax/VAT paid <sup>8</sup> by incoming tourists the previous year (here a proxy for sales taxes paid is used <sup>9</sup> ).	.
		70%
	80%	
<b>RELATIVE/BENCH-MARKING</b>  P2a:		20%
		30%
	Variable part of budget based on growth in tourism receipts relative to average growth obtained in comparable countries the previous year	.
		70%
	80%	
<b>RELATIVE/BENCH-MARKING</b>  P2b:		20%
		30%
	Variable part of budget based on growth in tourism receipts relative to a weighted average (to reflect relative similarity) of growth obtained in comparable countries the previous year	.
		70%
	80%	

countries were not considered. Figure A7.2a and b show that the growth rate in tourism receipts varies considerably from one country to another. Canada has the most stable growth of the countries listed and is the only country that has sustained positive growth rates over the entire period.

<sup>8</sup> Countries that have established a tourism economic impact system (e.g. TSA), usually have sufficient statistical tools to estimate the amount of sales taxes/VAT paid by foreign tourists.

<sup>9</sup> For Norway, the amount of sales tax paid by international tourists is about 15% of incoming tourism receipts. Sales-tax rates are somewhat lower in Canada. In this hypothetical example, let's say this figure would be 12.5% for Canada. Then, for instance, 10% (the fraction which would equal 142 million in the 1995-1996 budget with a 50/50% fixed/variable-alternative) of 12.5% (=1.25%) would be multiplied by the portion of the budget made variable (80-20%) to calculate the amount of the variable portion. This amount, plus the fixed portion (e.g. 20% to 80%), could be transferred to the NTO budgets each year.

### *The type of procedure used for linking budget to performance*

Table A7.2 provides an (non-exhaustive) overview of various conceivable performance-based principles that were applied. As we see two of the principles are “absolute” in the sense that the performance component is only based on the specific country in question (in this case Canada) and is not made relative to performance in other countries. The first of the absolute procedures (P1a) rewards the NTO for yearly change in the performance variable. The second principle ties the budget directly to a certain percentage of the sales tax revenue of tourism.

Two of the procedures are based on relative performance and thus reflect a benchmark principle. The performance is related to the performance of “comparable countries”. P2a differs from P2b in that the performance of the countries in the pool is weighted to reflect relative similarity to the country in question. The justification for using relative measures is that the procedure helps control for the effects of exogenous factors that influence all countries in the reference.

### *The degree to which the budget is based on performance alone or in addition contains e.g. a fixed amount*

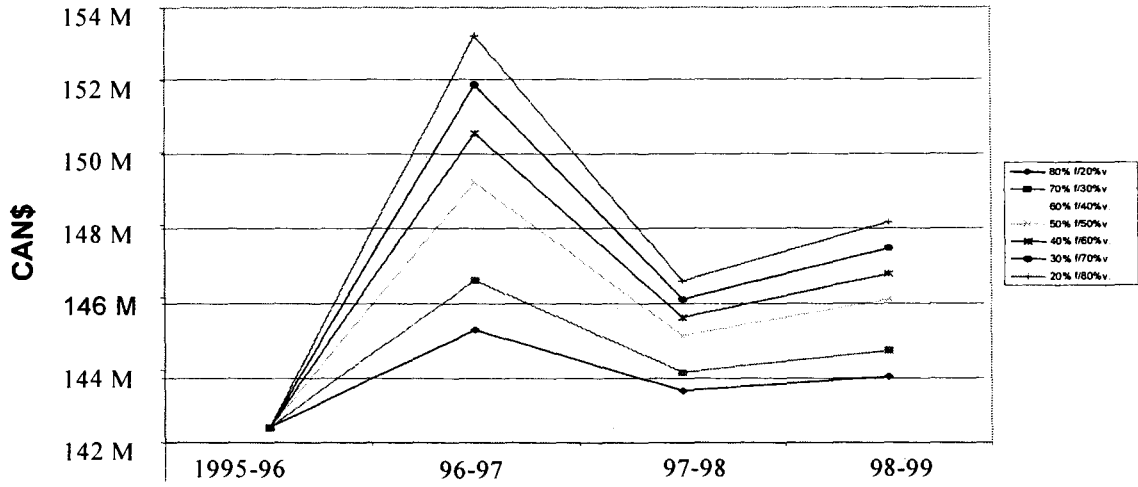
Performance based budgeting does not imply that the entire revenue for the NTO must be tied to some performance measure. Adding a fixed amount to the performance-based revenue can mitigate the effects of a performance-based principle. In the simulations we used a constant component that varied from 20% to 80 % as shown in the third column of Table A7.2.

## A7.2 Simulated budgets

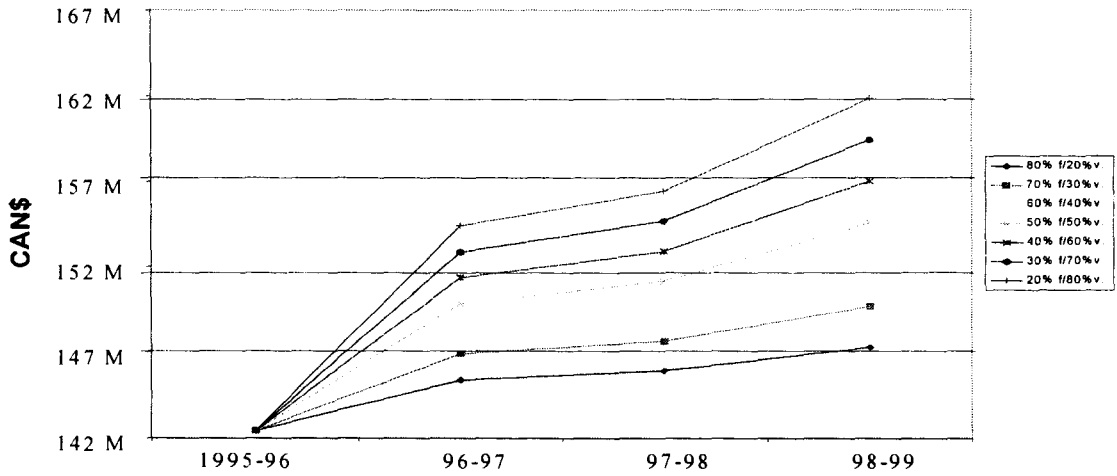
The results from applying three of the four principles listed in Table A7.2 are shown in Figure A7.3a-c for the Canada illustrative case. The following conclusions can be drawn:

1. *Different performance principles have very different consequences for NTO's revenue.* It is therefore important to evaluate potentially negative consequences of a given principle before implementing it.
2. *A performance based principle can result in considerable variations from one year to another unless*
  - the NTO is able to counter such variation or
  - a large portion (e.g. using 80% percent of the base year revenue) is fixed
3. *If the performance-based principle is tied to growth in market performance, the revenues for the NTO may be particularly volatile.* This is demonstrated in Figure A7.3a, which illustrates the consequences of principle 1a. This principle ties the
- 4.

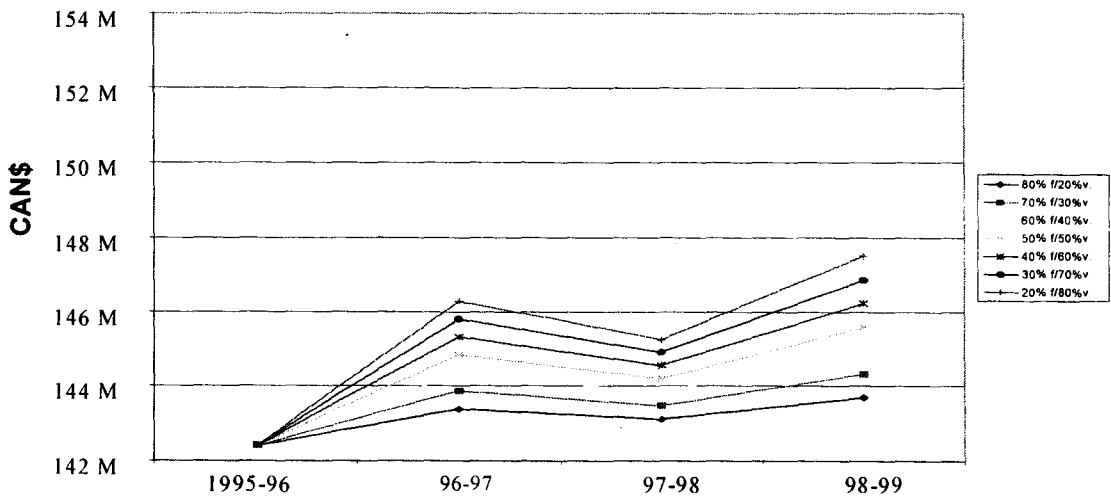
**Figure A7.3a: Budgets based on Principle 1a (tourism receipts) Canada**



**Figure A7.3b: Budgets based on Principle 1b (% of sales tax paid by visitors) Canada**



**Figure A7.3c: Budgets based on Principle 2a (tourism receipts) Canada**





revenues for the NTO to the increase in the performance measure (in this case change in tourist receipts) the previous year. The example shows a base year budget for 1995-1996 of CAN \$142.4 million. The increase in tourism receipts from 1995 to 1996 was 9.5%, giving a corresponding increase in budget size for the 1996-1997 budget. If a 80% variable + 20% fixed alternative (dark green line) had been chosen the budget gains (about 11 million CAN \$) would of course have been the greatest, while a 20/80 alternative (dark blue line) would have yielded only minor changes (about 3 million). From 1996-1997 the increase in receipts was 1.6%, resulting in a drop in budgets from the year before, but still above the 1995-1996 level, since there is continued *positive* growth. The budgets would only fall below the base year budget if the growth in receipts were *negative*. The following year, there is a growth of 4.2% from the year before, which is more than the growth from 1996-1997, resulting in an increase again in the budget. Since Canadian tourism has had positive growth in for all years in the simulation period, the CTC would have increased their budgets with such a system, and the highest gains would have resulted from a high relative variable portion (that also has the greater budget “risk”). This kind of system will work best when funds can be transferred from one year to the next. For instance, some of the extra funds gained the 1996-97 budgets could have wisely been put to use for increased marketing effort to counter the drop in growth level the following year in this simulation example.

5. *Using relative performance as a base for determining NTO's revenues may have some desirable and some unwanted consequences.* A possible outcome of this model is that a country can actually get an increase in its budget even if the absolute change in the performance measure in a given year is negative, given that the average corresponding change for the reference group is relatively more negative. Likewise, the NTO may experience a cut in the budget even with a positive growth in the performance measure if the reference group's performance is relatively better. The simulation shows that countries that deviate much from the reference group in terms of performance will be relatively higher “rewarded” or harder “punished” than in the models with Principle 1. Countries that generally only deviate a little from the average of the reference group will only experience minor changes in the budget from year to year. This is not unlike the situation for Canada for the simulation period. Still P2(a) is less “riskier” (less likelihood of substantial variance in budgets than for P1(a and b).

The selection of countries to be included in the reference group will obviously have to be done carefully, because it is necessary to include only countries that *are in fact really comparable* by some measure (see end of this Appendix7). The simulations generally show that the more countries included in the reference group, the smaller the group's average changes in the performance measure. This is analogous to a balanced stock portfolio; some stocks will decrease in value, while others will increase accordingly. The average change of the portfolio will approach zero (i.e. that the “risk” will be reduced). A “large number” of countries included in the reference group (7-8 or more countries) will approach a situation much similar to the case for Principle 1(a).

**Table A7.3**  
*(Tourist arrival data used for Principle 1 & 2 illustrative budget simulations for Canada)*

**Number of international arrivals in 1998 for Canada  
and some other comparable countries**

"Comparable" <sup>46</sup> countries	Number of international arrivals 1998 (in thousands)						
	(Canada)	US	Switzerland	Netherlands	Australia	Ireland	Spain
Common markets (Canada) ↓	-	13421	157	90	70	79	79
US	14880	-	1904	850	374	759	1207
UK	749	3975	1633	1530	467	3668	4460
Japan	486	4885	868	200	750	379	713
France	403	1013	1130	460	43	301	1932
Germany	379	1902	6431	2680	148	390	4457
Italy	102	610	953	310	48	137	1335
Sub total (incl. Canada)	16999	25806	13076	6120	1900	5714	14183
Total	18825	46395	18712	9080	4160	6073	20217
% of market	90%	56%	70%	67%	46%	94%	70%
Sub total (excl. Canada)	16999	12385	12919	6030	1830	5634	14104
Total	18825	32974	18555	8990	4090	5994	20138
% of market	90%	38%	70%	67%	45%	94%	70%

<sup>46</sup> "Comparable" is used in the sense that these countries to a large extent share the same geographical international markets. Other supplementing definitions of comparability may be feasible.