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Ao. Univ.-Prof. Mag. Dr. Josef Windsperger

Knowledge as Strategic Asset in Choosing a Market Entry Mode

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List of Abbreviations

BRIC	Brazil, Russia, India, China
CA	Competitive advantage
CC	Core competencies
CEO	Chief Executive Officer
CM	Change Management
DIKW	Data, Information, Knowledge, Wisdom
EC	Experience curves
EM	Market entry
ES	Economies of scale
ESC	Economies of scope
FME	Foreign market entry
H	hypothesis
HC	Human capital
ILA	International licensing agreement
IJV	International joint venture
JV	Joint venture
K	Knowledge
KBT	Knowledge Based Theory
KBV	Knowledge Based View
KH	Know-How
MEM	Market entry mode
OC	Organizational capacity
OCT	Organizational Capacity Theory
RBT	Resource Based Theory
RBV	Resource Based View
ROI	Return on investment
SCA	Sustained competitive advantage
SME	Small and medium-sized enterprise
SMM	Small and medium-sized manufacturing firm
SWOT	Strengths, Weaknesses, Opportunities, Threats
TCA	Transaction Cost Analysis
WOS	Wholly owned subsidiary

1. Introduction and Presentation of a Problem

“An investment in knowledge pays the best interest.”

Benjamin Franklin (cited by Davenport & Prusak, 2000, p. xviii)

In the rapidly growing, globalized, and partly digitalized economy of today, some organizations are doing well, whereas others are only striving for survival. The necessity to expand to achieve success serves as the basic difference between the two: limitations to local markets confine companies to limited markets, thus, limited growth potential. Large businesses seldom face such a problem, primarily because of significant resources, economies of scale (ES) and experience curves (EC), whereas for small- and medium-sized manufacturing enterprises (SMMs) it is a rather critical issue. Their prospects for growth depend, in the first line, upon how to obtain additional resources and how to optimally engage them through contractual agreements. Furthermore, expansion is likely to require change of current practices (upstream and downstream vertical integration), thus, significantly increasing potential risks (Chang & Zhou, 2009, p. 9).

Passive going with the stream, on the other hand, is likely to lead to constant deterioration of sales, since in today's world where, according to Richard Love (CEO of Hewlett-Packard), „*[t]he pace of change is so rapid that the ability to change has become a competitive advantage*“ (Kotler & Armstrong, 2009, p. 49), adaptation to change or constant Change Management (CM) (thus, ongoing adaptation of strategies and operations to rapid internal and external metamorphoses) is a necessity for survival and success in the short, mid and long term. Consequently, *nothing is constant but change* (Krause, 2010, p. 9).

Entering new markets implicates entering, dealing with and working on totally new markets. The opening up strategy presupposes, in turn, the selection of the new market, timing, mode and scope of entry (resources and strategic commitment), as well as developing respective marketing strategies (Remmerbach, 1988, p. 176). In particular, basic market entry (ME) decisions concern the following aspects: the size of the foreign market (present vs. potential), the purchasing power of the target market (present vs. future wealth), the suitability of the product for the chosen region, nature of indigenous competition (Kotelnikov, 2001). Furthermore, the benefits-costs-risks tradeoff helps rank countries in terms of future economic growth rates, free market system indicators, stability rate, capacity for growth, inflation rate, rates of private sector debt, etc. (Kumar & Subramaniam, 1997, p. 54). In case of an innovation, first mover advantages should be necessarily compared with those of late followers (Kotelnikov, 2001).

The new ME concept deals with numerous issues, challenges, and problems which shed light onto the degree of risks, control, required resources, and skills as well as the potential growth of ROI. The selection of the target market and the product for sales constitutes the initial stage of exploring a new territory. It is based on internal and external analysis (SWOT): information on customer preferences and social structure of the target market, potential competitors (especially, the presence of global players), suppliers, scarcity vs. abundance of resources, political regulations, trade barriers, etc. Subsequently, a respective market entry mode (MEM) is chosen (Kotelnikov, 2001; Kotler & Armstrong, 2009).

Yet, just as mentioned above, many factors as well as their weighted contributions to achieving the company's goals have to be considered before the final choice is made. In the Information Age of today, where knowledge (*not* labor, land, or financial capital) is regarded not only as a basic source of prosperity and social upliftment, but also as invaluable intellectual asset or even the new currency of the era of globalization and revolutionary IT, proper management of knowledge is a must (Stewart, 2001). In fact, transition from the industrially-based economy of the past to the knowledge-based society of tomorrow is marked by the enormously growing demand for knowledge (K). Consequently, K turned into a new product (*“both raw material and finished goods”*) (Leonard, 1995, p. 3).

As a result, K, as the key driver of global economy and competitiveness on a planetary level, has to be paid special attention to (World Bank, 2007, p. 3; World Bank Institute, 2012, p. 1). Its proper analysis and application (in business environment, in particular) open up incredible vistas, primarily for the emerging economies (BRIC: Brazil, Russia, India, and China) and the Third World countries (African continent). Thus, K helps achieve fast access to new chances to eradicate poverty, to secure organic growth and constant development, economic stability, and sustainability (Dahlman & Utz, 2004, p. 10). Moreover, back in 1996, the World Bank articulated its new strategy related to supporting poor countries all over the world not only with financial aid, but primarily through sharing of K, experience and best practices as well as learning guides as a the basic tool and an indispensable prerequisite to secure improvement and growth. Hence, the **“Knowledge Bank”** concept of the World Bank confirms the paramount significance of K as a new or parallel currency of today's global society (Knowledge Bank, 2012).

In fact, only constant learning and striving for perfection secured by K assets may lead to fundamental improvements (effectiveness, efficiency, and top quality). The time of the

“Working Smarter”, not the *“Working Harder”* Strategy finally arrived (Caballero & Hammour, 1994, pp. 1350-1351).

Thus, if applied correctly, K can become a constant source of competitive advantage (CA), material well-being and success in the long run. Yet, it is indispensable to learn how to search for it, store it, create, share and use it properly. Furthermore, in view of the information influx (data deluge), the quality and consistency of data will become one of the basic problems for the generations to come (Cisco, 2011).

There exist numerous classifications of K. The fathers of Knowledge Management (KM) – Nonaka & Takeuchi (1995, p. 59) – discriminate between two fundamental types of K: **tacit** and **explicit**. Explicit K is easily formalized and communicated, codified, and is stored in books, documents, CDs, etc. Tacit K, on the contrary, is highly individual and experiential, thus, very difficult to formalize, verbalize, share (thus, copy), since it is literally stored only in the minds of people. As a result, it is tacit K that serves as the source of CA. In addition, Nonaka & Takeuchi (1995, pp. 5-7), also underscore the relevance of constant K creation and innovation to secure the company’s organic growth and sustainability: simply being knowledgeable does not suffice any more.

According to Lundvall (1996, p. 5), on the contrary, K is subdivided into different channels and stages of the recursive K creation process: *Know-What*, *Know-Why*, *Know-How* and *Know-Who*. This process implicates the necessity of answering the *What*, *Why*, *How* and *Who* questions before applying the acquired K to repeated situational judgments in practice.

In addition, K can also be viewed from the following perspectives: **Resource Based Theory (RBT)**, **Organizational Capability Theory (OCT)** and **Knowledge Based Theory (KBT)** (Leonard, 1995). These theories will serve as the research foundation for the current thesis. In particular, the author will apply the premises of the aforementioned theories to investigate the following issues:

Is Knowledge to be regarded as Information, Data, or Capital?

Can Knowledge be regarded as a company’s strategic asset?

In view of the aforementioned, the author of the given research aims at indentifying basic characteristics of K. In addition, the paper will focus on the classification of K aspects, detailed analysis of each K component and its contribution to the optimal MEM solution.

Section 1 of the thesis provides a short introduction and presentation of various MEM. **Section 3** deals with the aforementioned theories. **Section 4** investigates the main components of Knowledge. The **Results** Section is dedicated to the presentation of the results of the research coupled with a short **Conclusion** of the thesis and a **Further Research** chapter.

2. Market Entry

2.1. Entry Modes

The key word in considering a foreign market entry (FME) is **globalization**. In order to survive, firms have to act accordingly or even manage to outperform in a smarter way. Ongoing technological advancements secured by IT-based solutions, primarily the Internet and its social media, coupled with globalization open up new perspectives and provide opportunities which were practically impossible some decades ago. Capitalization on such a rapid technological progress is therefore a must in order to secure organic growth and sustainability in the long run.

Globalization and digitalization of national economies offer an opportunity to discover and expand into new markets. On the one hand, it is an extremely lucrative perspective secured by global coverage and international markets as opposed to local, regional, or national presence. In view of the aforementioned, FME became a daily practice for all companies that could afford it financially. On the other hand, FME is a very challenging and risky initiative, since global coverage implicates quite a number of problems to be solved and barriers to overcome. For instance, a new country stands for a new partner with a different culture, religion, convictions, way of living, standards, tastes, even needs. This, in turn, significantly reshapes the scope, timing, and strategy of entry. Thorough preparation for a FME and the subsequent presence in the overseas market (control issues, protection against opportunism of foreign partners, effectiveness of acquisition of new partners' knowledge-based resources, flexibility of acquired resources, etc.) serve therefore as primary prerequisites for securing stability and profitability in the long term (Li, 2007, p. 771).

Generally speaking, FME is defined as *a form of international investment which stands for entering totally new markets with new or already existing products or services in order to expand and gain success*. It goes without saying that the primary motivation for going abroad is related to enormous growth potentials (thus, higher returns and brand awareness) (Hilmi, Ketata & Safa 2007, p. 243). Other reasons for international expansion encompass cheaper labor and raw materials, lower costs of production, improved markets, trade, and business conditions, better government policies, and macro-economical framework (Hilmi et al., 2007, p. 243). In addition, firms may sometimes be forced to relocate their businesses when government imposes trade barriers. Consequently, global expansion is intended for achieving required resources.

In view of complex transformations that a firm has to undergo, international joint ventures (IJVs) are usually a primary strategy for multinational companies (MNCs). Moreover, according to numerous studies, MNCs prefer to start their investment projects with neighboring countries that are marked by familiarity, cultural and institutional similarity, ease of access, and cross-border spillovers (Hilmi et al., 2007, p. 243).

Nevertheless, different countries may offer different opportunities, advantages, benefits, as well as disadvantages, risks, and control issues. The main strategic decision to be made hereby is to decide whether **to buy** or **to build** a completely new entity (*To buy or not to buy, that is the question!*). The most relevant problems faced by MNCs are asymmetric information, demand uncertainty, wrong timing, high establishing costs, exchange rate fluctuation, cut-throat competition, lack of CA, lack of K of foreign market peculiarities, technological mismatches, cross-cultural differences (Hilmi et al., 2007, p. 243).

Consequently, there exist numerous factors that have to be necessarily taken into account before deciding whether to expand into foreign markets. Indispensable research on determinants and patterns of entry has to be made in advance. The primary set of factors that determine the FME choice includes the analysis of political, economic, socio-cultural, and technological determinants (PEST), potential growth, and opportunities. Of significant importance are also political hazards, legal restrictions, and country risks (Hilmi et al., 2007, p. 244).

As a matter of fact, the choice of MEM was always heatedly discussed in literature. First and foremost, it is related to the **risk perceived** (decision-making under uncertainty) and **contextual specificities**. In general, the correlation between risks and actors' contribution is negative. Generally, overall risks may be subdivided into *environmental risks* (complexity of market risks, traditional factor risks and the exchange risk), *industrial sector risks* (due to industrial concentration, customer preferences, market supply), and *firm-specific risks* (due to differences of the infrastructure marketing, lack of experience, and cultural differences) (Hilmi et al., 2007, p. 244).

Hill, Hwang & Kim (1990, p. 117) claim that each of MEM offers a unique portfolio of strengths, weaknesses, opportunities, and threats coupled with a dissimilar level of control over foreign processes, resource obligations, and diffusion risks. The ultimate choice of market for expansion depends upon the weighted degree of risks to be tolerated in a foreign country, control over operations and management, commitment of resources to be placed at disposal, and the ROI to be expected. Global strategy and competition are of significant importance to the concluding stage of choice of a suitable EM.

In addition, from the **Transaction Cost Analysis** perspective, companies normally face a tradeoff between benefits of increased control and costs of resource commitment and risk (Anderson & Gatignon, 1986, p. 1).

According to Hill et al. (1990, p. 120), there exist three groups of variables that influence the EM decision, namely: **strategic**, **environmental** and **transaction specific variables**.

Strategic variables influence the EM choice primarily through **control** requirements. Different strategies implicate various degrees of control over operating and strategic decisions related to foreign affiliates (thus, different EM) (Hill et al., 1990, pp. 120-122).

Environmental variables influence the EM decision, first and foremost, through their impact on the suitable level of **resource commitment**, or, in other words, **strategic flexibility** (Hill et al., 1990, pp. 122-124).

Transaction specific variables influence the EM decision through their impact on diffusion **risks** and the appropriate level of control (Hill et al., 1990, pp. 124-126).

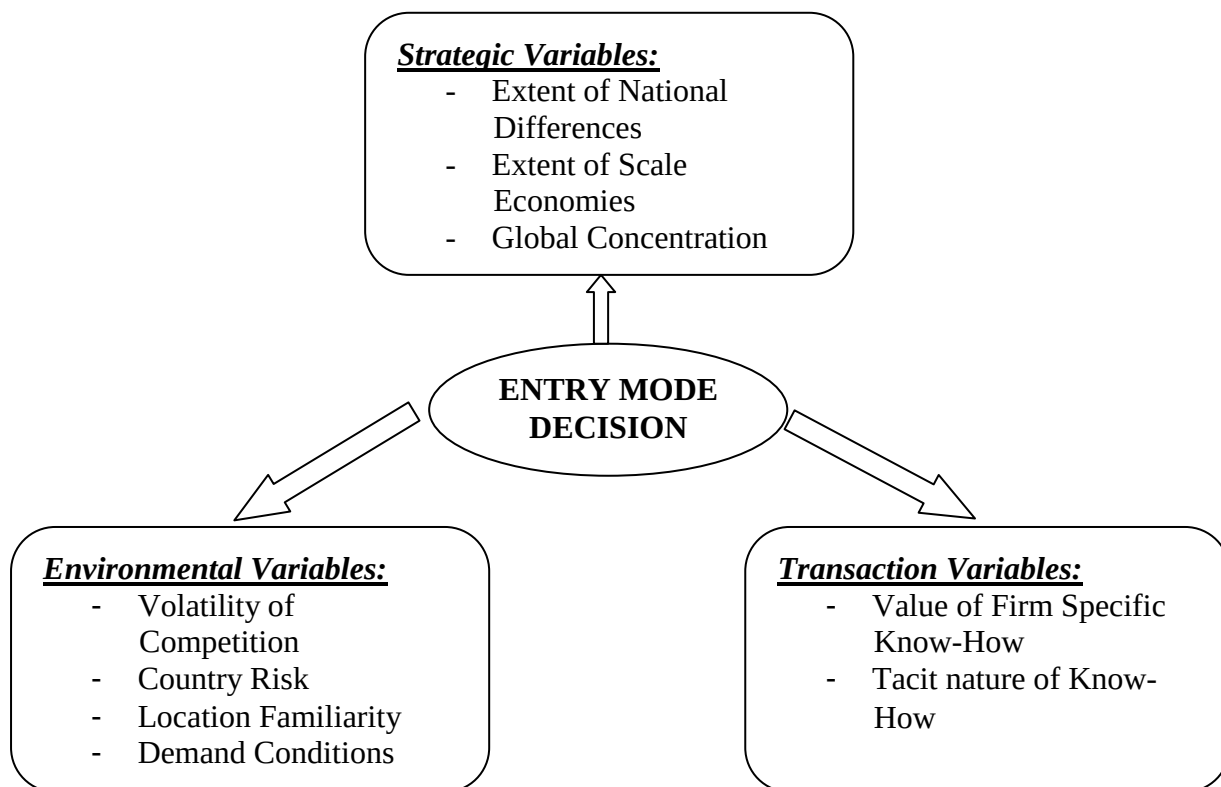


Figure 1: Variables Influencing EM Decision (Source: Hill et al., 1990, p. 120)

Just as mentioned above, primary considerations or reasons for entering foreign markets may vary from company to company, industry to industry, and country to country. However, basic similarities traced all over the globe include **profit**, **growth** and **security**

goals. Normally, corporations have a mix of all goals. Yet, one goal, assuredly, dominates over the others (Hilmi et al., 2007, p. 242).

Profit goals always implicate **cost reduction** secured by ES, tax reduction, higher demand, KH acquirement, cost reduction in labor, resources, energy, transport, ROI, etc. (Hill & Jones, 2012, p. 16). Moreover, global expansion proves attractive both for SMEs and MNCs and secures the increase in profitability non-achievable by purely domestic operations (Hill & Jones, 2012, p. 16).

Just as mentioned above, globalization is gaining pace at an exponential speed today. This, in turn, leads to similar needs, wants, and customer preferences, thus, to the abundance of similar products offered all over the globe. **Standardization** of demand and supply renders the world more and more competitive. Hence, in order to survive, businesses have to be prepared to compete on a global scale from the very beginning. Otherwise, survivability turns into a rather critical issue for them even in the short run (Levitt, 1984, p. 2).

According to Porter (1998, pp. 11, 20-21), finding viable ways for long-term profit maximization is a must (in view of the inevitability of competitors in future). This, in turn, implicates either radical cost reduction of value creation activities (**cost leader strategy**), or performing value creation activities in such a way that it renders consumers willing to pay a premium price charged for the company's output (**product differentiation strategy**), or a combination of both (**hybrid strategies**). International expansion, as an inevitable by-product of the aforementioned options, implies the rise in profits through increasing returns from the company's core competencies (CC) and the realization of ES (*Microsoft*) and location economies (LE) (*Walmart*) (Hill & Jones, 2012, 149-150).

Companies operating internationally have the opportunity to earn a much greater return from their distinctive skills (or CC), to realize *location economies* via dispersing particular value creation activities to those locations where they can be performed most efficiently, to realize greater *experience curve economies* achieved through reducing value creation costs enabled by building sales volume more rapidly (*economies of scale*) and reducing costs of value creation (*restructuring, lean production, and business process reengineering*) (Hill & Jones, 2012, pp. 149-150).

Growth goals implicate unlimited expansion plans – with no government restrictions and scarcity of resources (materials, labor, KH, etc.) (Hill & Jones, 2012, p. 17). Thus, the international expansion strategy is a viable way of securing greater returns by transferring the company's skills and product offerings derived from its CC to foreign markets where indigenous competitors lack such skills (Hill & Jones, 2012, p. 299).

Security goals, on the contrary, implicate risk diversification, the possibility of granting patents in exchange for a royalty payment in order to prevent KH outflow, CA, corporate takeover defense, etc. (Hill & Jones, 2012, p. 16).

Porter (1998, p. 120) argues that CA of a company located in a particular country are determined by certain attributes which are unique to that country. In particular, the researcher identifies **four basic attributes**:

- natural resources and created capabilities;
- the level, variation, composition and quality of output demanded by domestic consumers;
- the presence of clusters of suppliers or supporting industries;
- the extent and patterns of inter-firm rivalry and the effects that the latter have on the innovatory and competitive strategies of domestic players.

2.1.1. Classification

While expanding, companies attempt to increase their competitiveness through foreign direct investment (FDI). **Market-seeking FDI** companies are looking for *new customers* (new distribution channels), whereas **resource-seeking FDI** prioritize *natural resource* seeking. **Efficiency-seeking FDI** seek *cost reduction* opportunities (buyer-driven) or *regional proximity* (producer-driven), thus, cheaper inputs to secure ES through horizontal and vertical integration. **Strategic asset-seeking FDI** seek for the acquisition of *new assets* (technologies, skills, brand names, distribution networks, and high-valued production facilities) in order to diversify their portfolios and complement manufacturing and technological K (Hilmi et al., 2007, pp. 243, 246). The latter represent tacit K and are, thus, the primary source of CA.

Asset-exploiting FDI exert a direct influence on the company's *performance* (financial: ROA and profitability, and operational: efficiency and market share), whereas **asset-augmenting FDI** impacts it indirectly, through *competitiveness*, depending upon the firm's capacity to absorb new assets (Hilmi et al., 2007, p. 246). Moreover, FDI have two primary impacts in the host market: on industries' *competitiveness* and *restructuring*, thus, they are also connected with change management and learning.

The decision as to which MEM to choose depends primarily upon the chance and risk analysis, strength of the company's own resources and conformity to international goals. There are two main types of FME modes: **equity** (*international joint ventures (IJV), wholly-owned subsidiaries (WOS, mergers)*) and **non-equity** (*exporting, contractual agreements (international licensing agreements (ILA), franchising), cooperation*) modes.

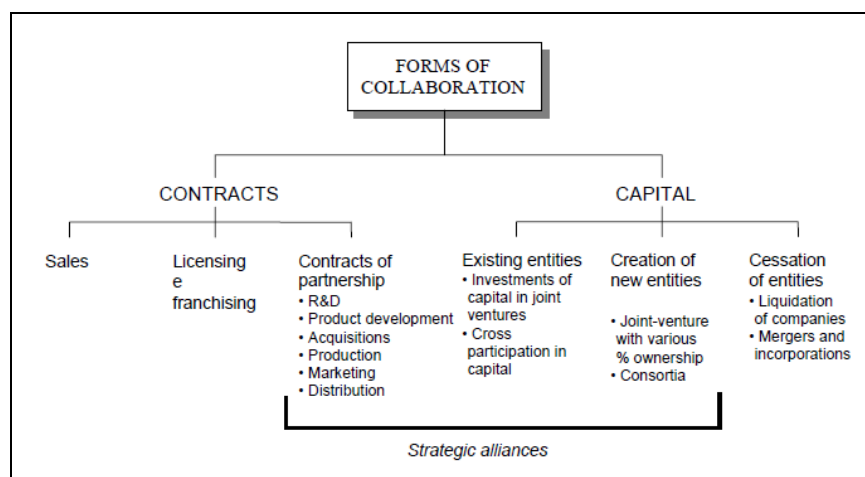


Figure 2: Forms of Collaboration (Source: Pellicelli, 2003, p. 8)

Just as mentioned above, corporations have to take one fundamental strategic decision as to whether to **buy** already existing facilities (business) or **build** a completely new one from the ground up (Hill & Jones, 2012, p. 290). The distinction between equity and non-equity

modes is, thus, not trivial, since in case of FDI, MNCs enjoy the three basic advantages of **ownership, location, and internalization** (Peng, 2011, p. 336). As opposed to developed nations, emerging economies (which possess no high-caliber technology and management KH) are marked by a different framework: **“linkage, leverage, and learning”** (Peng, 2011, p. 342). Linkage refers to the ability to identify and bridge gaps, leveraging on ES, ESC and constant learning from all over the globe (Peng, 2011, pp. 342-343). Consequently, the answer to this basic question impacts all the subsequent decisions of the company: *timing, scope and strategy of FME*.

The following figures graphically illustrate the logic behind the strategy decision-making based on the market cycle phase and the corporation’s attitude towards a MEM overseas.

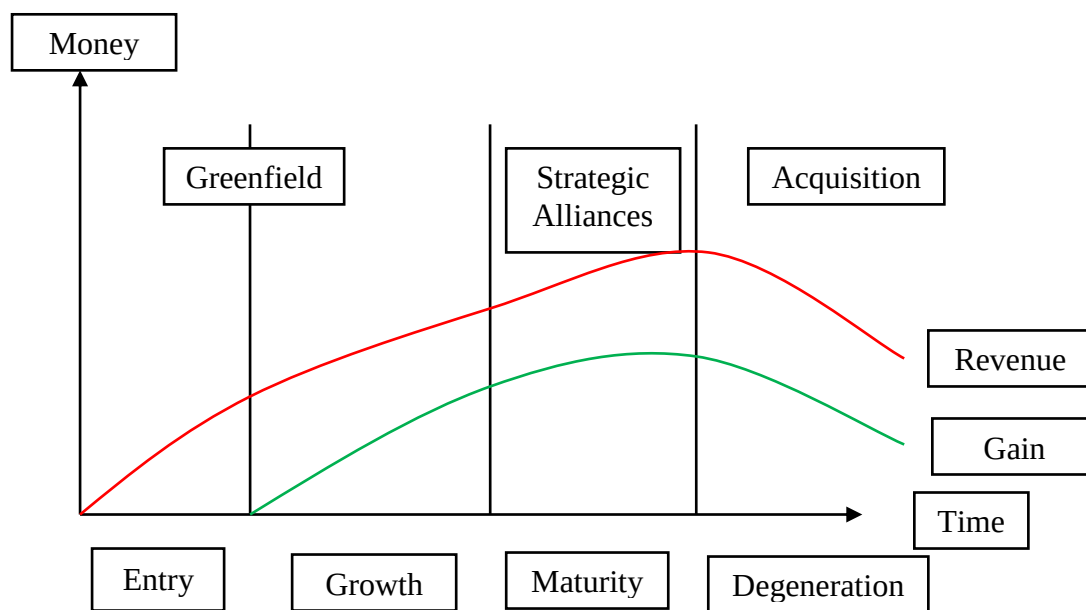


Figure 3: FME Strategy by Market Cycle Phase (Source: Hill, 1994)

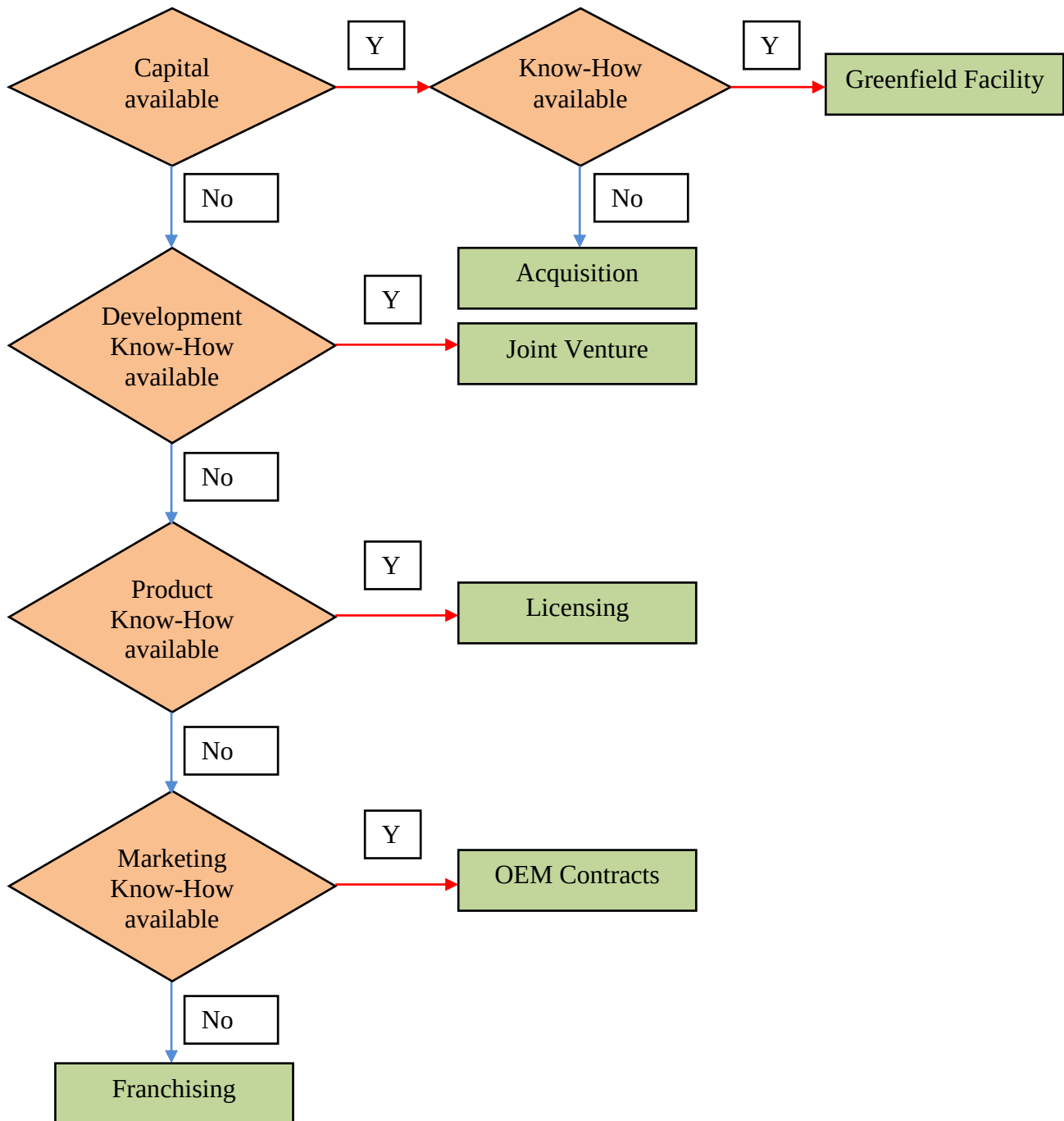


Figure 4: The Wholly New Entry Flowchart (Source: Hill, 1994)

There exist two different classifications of **wholly owned modes** (WOM) or FDI. In the case of a WOM, the firm owns one hundred percent of the stock, since there are no partners to share costs, risks, gains with. The primary advantage of WOM is tight control over operations, which, in turn, implicates the realization of LE and ES coupled with tight control over technological KH (Peng, 2011, p. 122), benefits of total profits and full control over the WOS (Chan, 1995, p. 39). And just as stated above, the main disadvantage of WOM consists in the necessity to bear all the costs and risks related to opening up a foreign market

(Peng, 2011, p. 122). Moreover, the firm incurs much higher costs and runs higher risks especially in R&D, production, financing, and market penetration (Chan, 1995, p. 39).

On the other hand, the level of control is highest in case of a WOM (Hill et al., 1990, p. 121). That means that control over daily operations and certain strategic decisions may be delegated to the WOS, but ultimate control always resides in the firm's headquarters. Resource commitment is very high, as the corporation has to bear all the costs associated with opening up and serving the foreign market. The risk of KH dissemination, on the contrary, is likely to be lowest of all. Yet, the possibility of KH outflows to competitors is never excluded. Consequently, the residual risk of dissemination is still present (Hill et al., 1990, p. 122).

A corporation may either initiate an operation overseas from the ground up (Greenfield Operation) (GFO) or it can acquire an established firm and use it to promote its products abroad (Brownfield Operation (BFO) or Acquisition) (70% of worldwide FDI) (Peng, 2011, p. 340).

GFI is a form of a FDI which implicates setting up a new plant in the host country and producing goods overseas upon constructing new operational facilities from the ground up (a WOS) (Raff, Rayn & Stähler, 2007, p. 2). This type of investment is optimal if the host market is very much or very little competitive (Müller, 2001, p. 1).

It goes without saying that a new WOS is a very complex and potentially costly project, but it is the firm's 100% property and therefore implicates full control and potential of above average returns in the long run.

GFI is usually regarded as an alternative to other MEM such as M&A, JV or ILA, when physical capital-intensive plants are planned (Raff et al., 2007, p. 2).

In accordance with Hill (1994) and Peng (2011, p. 340), the main advantages of GFI include:

- exclusive impact on a new business formation;
- exclusive shareholder rights;
- an exclusive position as an innovation leader (thus, own standards);
- no necessity to search for a cooperation partner or production facilities;
- equal organizational culture in the core and new business, etc.

The disadvantages of GFI include, on the contrary (Hill, 1994; Peng, 2011, p. 340):

- it is extremely risky and costly: high time, high staff, high KH, and high performance requirements (high risks due to high costs of establishing a business abroad and from scratch, establishing distribution networks, finding reliable and professional staff, and acquiring essential K of the foreign market from third parties);

- high risks related to wrong timing of entry;
- high risk of cost overrun;
- high risk of invincible technical problems, etc.

GFI are normally associated with creating new long-term jobs and therefore are primarily preferred by developing countries (as hosts) through offering prospective buyers numerous tax-breaks, subsidies, and other incentives (compromising at the same time on corporate tax revenue), thus, boosting the country's HC, K, KH, and technology share and enhancing economic growth in general (Hilmi et al., 2007, pp. 248-249).

Contractual entry mode, on the contrary, is a long-term **non-equity** association between an international company (actual or emerging) and a legal entity overseas which involves transfer of K and/or skills. This MEM tends to reflect relatively smaller commitments to overseas markets (Peng, 2011, p. 336). According to other researchers, contractual entry strategies are based on cross-border interactions of K assets, whereas the association between a firm and its foreign partner is governed by an explicit contract. Contractor (1990, p. 31) claimed that the contractual EM is an optimal solution when the global market for technology transfer is efficient and transactions costs are kept low.

The basic characteristics of the contractual EM (as a non-direct way of investing overseas) are as follows: (1) *the governance by a contract*, which, in turn, secures a moderate level of control over the foreign partner and, thus, sales and income, (2) *the exchange of intangible resources*, which can be pursued both independently and in conjunction with other ME strategies, and (3) *the generation of a predictable level of earnings* derived from foreign operations (Hill, 1994).

The most common types of contractual entry strategies are **exporting**, **licensing** and **franchising**. Further contractual entry modes that will be covered in this paper include **strategic alliances (SA)**, **cooperation**, **contract manufacturing (CM)**, **management contracting (MC)**, **OEM contracts**, and **turnkey projects**.

2.1.1.1. Licensing

According to Hill (2003, p. 482), an international licensing agreement (ILA) is defined as an agreement which allows an overseas entity (licensee) to manufacture, exclusively or non-exclusively, a proprietor's product and sell it for a defined period of time. In addition, the ILA grants the right to use the proprietor's commercial and industrial property (e.g. technology license, inventions, patents, trademarks and franchising, copyrights, formulas, processes, designs, managerial skills, etc.) in return for compensation, usually a *royalty payment* or other (normally calculated as a percentage of sales). Hence, ILA serves as a legitimate means of capitalizing on intellectual property in an overseas market (Kotelnikov, 2001; Root, 1987).

In view of a significant transference of K assets from the licensor (or proprietor), the level of control of the latter is rather low, primarily since the company's authority over operational and strategic decision-making is extremely limited. Secondly, strategic considerations as to the choice of ILA depend upon the level of respect the host government displays for intangible property and the licensee's ability to choose the right partners and have them cooperate, not compete (Hill, Hwang & Kim, 1990, p. 118).

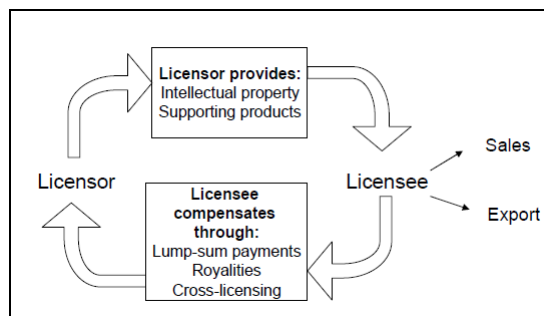


Figure 5: Licensing (Source: Cavusgil et al., 2008, p. 10)

Generally speaking, licensing is an extremely attractive EM for companies that are new to international business operations or SMEs (Kotelnikov, 2001). The licensee covers most of the costs related to entering into and serving the foreign market. Yet, on the other hand, he also owns all the revenue-generating assets, thus, depriving the proprietor from extra income from his own KH (yet, the licensee perceives most of the commercial, exploitation, and political risks). As a consequence, the level of resource commitment for the licensor is low (lower-risk EM) and limited to personnel required for training licensees and subsequently for monitoring their behavior for any violation of respective licensing contracts (Cavusgil, Knight & Riesenberger, 2008, p. 10).

The dissemination risk, on the contrary, is rather high. The primary risk is associated with the risk that the proprietor's specific advantages in technical KH might be expropriated

by a licensing partner. And since no licensor desires to rear a potential competitor (or have reduced quasi rents), protective measures are a must (e.g. cross-licensing or exchange of KH) (Kotelnikov, 2001).

The principal **motives** for establishing an ILA include:

- *resource scarcity,*
- *ability to keep the market name,*
- *import barriers and high tax* (Beamish et al., 1992; Beamish & Safarian, 1999).

In addition, ILA allow the licensor to increase earnings without the necessity to open a new operation overseas (WOS). Moreover, it is a lucrative way of participating on foreign markets with barriers to FDI.

The following table visualizes the basic **advantages** and **risks** of the Licensor and Licensee.

Licensor		Licensee	
Advantages	Risks	Advantages	Risks
Fast coverage of R&D costs due to extra income from technical KH	Income influx depends upon the licensee's performance	Low R&D costs	Risks that products might not succeed in the market
Expansion of available products with little additional capital and time investments	Licensee as a potential competitor in future and the risk of opportunism	Access to advanced technologies	
Fast ME without much risk in various countries simultaneously (rapid global expansion) (well-codified knowledge)	Trademark or image ruined by the inconsistent product quality	Profit from an established brand name or well-known copyrighted material	Licensor may refuse or fail to provide support
	Risk of violating intellectual property rights		
	Lack of control over the licensee's operations (exploitation of assets, marketing, strategy)		
Relatively low startup costs (especially appropriate for SMEs lacking resources)			
Minimized political risks (the licensee owns the business locally 100%)	No experience curve and location economies		
	Opportunity costs (rents generated through other EM might be substantially higher)		

Table 1: Advantages and Risks of Licensing

(Source: Own Work based on Beamish, 2008, p. 25; Kotelnikov, 2001)

2.1.1.2. Franchising

Franchising is a specialized form of licensing (Hill, 2003, p. 485). It is an longer-term commitment agreement where the parent company (the franchisor) gives a semi-independent business owner (the franchisee) the right to use its business format in the overseas market in exchange for a compensation (primarily fees or royalty calculated as a percentage of the franchisee's revenues) (Peng, 2011, p. 311). In other words, the franchisor not only sells intangible property (trademark) to the franchisee, but also insists on the franchisee's consent to abide by strict rules as to how the business has to be run on a daily basis (location, methods, design, staffing, supply chain, etc.). Therefore, franchising is most appropriate for service firms. *Mcdonalds* and *Coca Cola* are the most vivid examples of this MEM (Pellicelli, 2003, p. 11).

According to Cavusgil et al., (2008, p. 15), franchising is characterized by the following factors:

- *supply of a total business system;*
- *strong corporate identity*, since the franchisee acquires the right to be identified with the franchisor's trademark (for the franchisor, it translates into foreign returns from customer service and brand name assets);
- Franchisee has an opportunity to receive *training, ongoing support, incentive programs* and the right to participate in cooperative marketing programs.
- Franchisor sets *guidelines* for the franchisee (operation manuals, managerial guidelines, etc.) to follow; the latter also has to purchase materials from the franchisor.

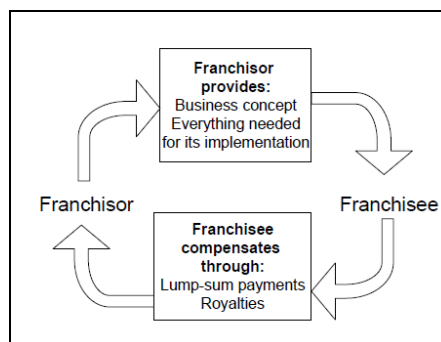


Figure 6: Franchising (Source: Cavusgil et al., 2008, p. 15)

The following table summarizes the primary **advantages** and **disadvantages** of the franchising MEM:

Franchisor		Franchisee	
Advantages	Disadvantages	Advantages	Disadvantages
Expansion without using own resources, relief of many costs and risks related to opening a new market	Large capital and time investments, tight control mechanism as compared to other MEM (e.g. exporting, licensing)	Most suitable for individuals or SMEs	Little space for creativity and own ideas
Control over the franchisee, low political risk involved	No manufacturing, thus no location economies and experience curve		
Access to “global” brand names, high recognition among customers	Highly dependent upon the quality of franchisees (master franchise as an additional layer of control on a local level)	Usage of resources of a successful franchisor	Financial risk if product/ service does not succeed
Access to local expertise	Impact of intercultural differences	Relatively low risk of business failure	
Motivation of franchisees as entrepreneurs	Franchisee as a potential competitor in future due to knowledge and strategic spillover		

Table 2: Advantages and Disadvantages of Franchising (Source: Cavusgil et al., 2008, p. 15)

As opposed to licensing with its tendency towards transference of limited rights or resources as well as short duration, franchising puts a broader package of rights and resources at the franchisee's disposal. On the other hand, **ILA** implicates the involvement of intellectual rights and trade secrets, whereas **franchising** is limited to trademarks and operating KH. Thus, licensing is most suitable for manufacturing; franchising, on the contrary, - for the servicing industry (Gutterman, 2002, p. 123; Kotelnikov, 2001).

2.1.1.3. Outsourcing

In view of increased globalization and liberalization of world trade, access to formerly restricted zones of global specialization is now open practically to all countries. This, in turn, implicates that cost leaders or differentiators that aim at competing on an international scale can significantly improve their cost structure. This is enabled by outsourcing (either domestically or overseas).

Outsourcing implicates that one or more of the company's value-chain activities or functions are performed by outsiders – independent specialized companies that focus on acquiring skills and K in just one kind of activity. As a result, ES enable them to secure the desired quality of products (Hill & Jones, 2012, p. 328; Hilmi et al., 2007, p. 244).

MNCs or other global players engage in strategic outsourcing to strengthen their business model and increase profitability. The process usually starts with the identification of the **value-chain activities** that form the basis of the company's CA or distinctive competencies (to protect them from competitors). The systematic analysis of the *non-core functions*, on the contrary, helps managers assess whether outsourcing those activities by specialized companies could be more beneficial (*differentiation* or *cost advantages*) (Hill & Jones, 2012, p. 330).

Because of constant pressures to reduce costs, normally, it is the **manufacturing** function that is outsourced (also referred to as **contract manufacturing (CM)**). According to Hill & Jones (2012, p. 328), over 60% of all global product manufacturing is outsourced today. As vivid examples serve *Nike* which does not make its athletic shoes and *Apple* that assembles none of its own products. These are produced or assembled under contract at low-cost locations dispersed globally. Therefore, in view of the complexity of value chains of the aforementioned MNCs, quality issues are the primary problems the latter may expect in case of production inconsistency or disputes with their subcontractors (Hill & Jones, 2012, p. 328).

Apart from CM, strategic outsourcing may also include outsourcing of other kinds of non-core activities such as IT, HR, and logistics (Peng, 2011, p. 99). For instance, *Microsoft* outsources *customer service* in India (Hill & Jones, 2012, p. 330). Yet, R&D, marketing and sales always remain in the company (Hill & Jones, 2012, p. 331).

The basic benefits of CM are labor cost advantages, lower costs in energy, raw materials, and overheads (ES and LE), savings via taxation, lower political and economic risks, and quicker access to foreign markets (e.g. *Boeing*, *Nike*, *IKEA*) (Peng, 2011, p. 99). In addition, the client does not have to maintain manufacturing facilities, purchase raw materials,

or hire labor in order to produce finished goods. As a result, much less capital investment is required (Kotelnikov, 2001).

Moreover, in view of the lowered cost structure (*Motorola*) and increased product differentiation (*Dell's* customer service) secured by subcontractors, the company can fully focus only on its distinctive competencies that are vital to sustain its CA and profitability in the long run (e.g. *Cisco Systems* focuses on building its CC in product design, marketing and sales, and supply-chain management) (Hill & Jones, 2012, p. 331).

The main disadvantages of CM include lower production standards and therefore potential quality issues, lack of management control, ethical issues (backlash from the home-market employees regarding HR and labor issues coupled with inhuman conditions of labor in subcontractors' countries (e.g. *Nike*)). In addition, the contract manufacturer may become a future competitor (potential security and confidentiality issues as a result of holdups or losses of important information). Hence, it is indispensable to select a reliable partner who could meet the required quality standards and low-cost requirements, as well as just-in-time delivery terms (Kotelnikov, 2001). In addition, a *parallel sourcing policy* (outsourcing by two or more service providers for the *same component*) may considerably reduce the risk of holdups (Hill & Jones, 2012, p. 332).

As opposed to CM, **management contracting (MC)** implicates outsourcing managerial functions. Thus, MC is an agreement under which operational control of an enterprise is vested by contract in a separate enterprise which performs the required managerial functions in return for a fee. MC involves not just selling a method of doing things (e.g. as in the case of franchising or licensing), but involves actually doing them. MC can encompass a wide range of functions, such as technical operations of a production facility, management of personnel, accounting, marketing services, and training (Kotelnikov, 2001).

Generally speaking, MC are characteristic of companies with the lack of local skills to run a project (primarily, in the hotel and insurance industries). Consequently, MC is an alternative to FDI, since it does not involve so much risk and can yield higher returns for the home company when foreign government actions or regulations restrict other MEM.

The basic advantages of MC include loss of control, flexibility, and quality, time delays, compliance issues (Kotelnikov, 2001).

2.1.1.4. OEM Contracts – Supply Business

OEM stands for **Original Equipment Manufacturer** that can be marketed by another manufacturer (IBM, 2003, p. 66). In other words, OEM contracts allow selling originally manufactured (or genuine) parts or products under the buyer's own brand name and logo (re-branding).

OEM contracts are applied in most industries. E.g. *Chrysler* markets cars produced by *Mitsubishi*. In computer industry, many parts are supplied under OEM contracts (e.g. *Acer*, *Compaq*) (Borrus, Ernst & Haggard, 2000, pp. 126-128).

A tremendous surge in applying OEM began in the mid-1990s. At that time a large number of high technology OEMs were revising their manufacturing strategies to improve performance and reduce asset and operations costs. In the economic downturn of today, challenges for supply chain partners that assumed greater responsibility for manufacturing are growing, whereas the provision of OEMs with broader business solutions becomes tighter and tighter (Delatre, Hess & Chieh, 2003, pp. 1-2).

As a matter of fact, most carmakers do not produce their parts themselves. Instead, they use outside independent companies who help them design (**ODM** or **original design manufacturers**) or produce (**OEM**) parts. Therefore, when it comes to automotive parts, OEM stands for replacement parts produced by the manufacturer of the original part (Kidder, 2002).

The opposite of OEM parts is **aftermarket parts** or parts produced by other companies, not the original manufacturer, but that fit and perform just like the original ones. As a rule, aftermarket companies purchase rights to reproduce parts similar to OEM ones and supply them to the same wholesale distributors. Yet, in view of various specific techniques applied in the production of OEM parts (tacit K or technical KH), aftermarket parts have minor differences in appearance and feel. On the other hand, aftermarket companies also attempt to surpass the original OEM product through improving it by redesigning it (Niosi, 1994).

OEM can be regarded as “disguised” exports. It is also an intermediate step between exporting and FDI, just as licensing is. In such a way, OEM exporters may effectively delegate marketing functions to foreign firms and learn about foreign preferences, thus, reducing the marginal cost of a possible entry into local production in future. OEM importers, on the other hand, may further on set up a JV to manufacture the product locally if the OEM contract proves successful (Niosi, 1994, pp. 165).

Thus, the main advantages of OEM contracts consist in: (1) the possibility of the purchasing company to buy necessary (standardized) components without the necessity to establish and operate its own operations; (2) the possibility of taking advantage of low cost parts and/or products secured by ES and specialization (purchasing economies, cutting edge of product development, production technology, and sophisticated quality control); (3) increased time-to-market of finished goods (indispensable in view of shortened product life cycles). This, in turn, allows the purchasing company to fully concentrate on its CC (Kaya, 2009, pp. 1-2).

The major disadvantages, on the contrary, include quality issues, since the OEM essentially determines the quality of the final product. A higher quality product, vice versa, results in an increased market potential (Kaya, 2009, p. 1).

2.1.1.5. Mergers

Mergers take place when two or more industry competitors (or equal partners) agree to go forward as a single new company rather than remain separate in order to achieve CA that arise from a large size and scope of operations (**horizontal integration**) (Hill & Jones, 2012, p. 311; Kotelnikov, 2001).

Normally, merging firms are small-size and create a new entity to pool their operations whereas an **acquisition** implicates that one big company uses its capital resources (stock, debt, or cash) to purchase another company (or swallows the target company) (Kotelnikov, 2001). Therefore, mergers are also referred to as mergers of equals, whereas acquisitions or takeovers – as hostile mergers. This is primarily due to the fact that pure equality of mergers practically never exists in practice. Usually one company purchases another under the pretext of a merger (technically, an acquisition).

Mergers are common in most industries. As a good example serves *Boeing* which merged with *McDonnell Douglas* to create the world's largest aerospace company (Hill & Jones, 2012, p. 311).

The number of mergers and acquisitions (M&A) is increasing these days, since some companies gain CA over their rivals and attempt to suppress competition, thus, improving CA and profitability of its single-business model (Hill & Jones, 2012, p. 311).

On the other hand, the coordination and transformation period takes enormous financial resources and causes instability among management (M&A, 2012, p. 9), which in most cases lead to a higher rate of unsuccessful M&A (about 50%) (Kotelnikov, 2001). Thus, it is imperative that the complexity of M&A be not underestimated. On the other hand, M&A may enable abnormally high and long-lasting returns, which, in turn, explains their popularity in recent years (Gresham, 2008).

In view of the aforementioned, M&A are indicative of “*confidentiality bubbles*”, when information flows are restricted due to confidentiality agreements. The takeover of *Chrysler* by *Daimler-Benz* in 1999 serves as a good example of it (Oxbridge Writers, 2012).

The basic advantages of mergers are ES (cost reduction, removal of duplicate departments, increased profit margins), ESC (efficiencies related primarily to demand side changes, scope of marketing and distribution), increased market share enabled by the buyer's absorption of a major competitor, synergy effects (increased opportunity of managerial specializations, increased bargaining power over suppliers, and buyers, etc.), cross-selling, tax benefits (buying a loss maker reduces the buyer's tax liability), geographical diversification,

resource transfer (combination of scarce resources, overcoming information asymmetry), etc. (Hill & Jones, 2012, p. 312; Kotelnikov, 2001).

The basic problems of mergers encompass brand and quality issues coupled with coordination and integration problems (Hill & Jones, 2012, p. 313; Kotelnikov, 2001).

With the ongoing globalization and liberalization, M&A increased considerably starting from the mid-1990s. Yet, most host governments *do* favor GFI more, since they add to country production capacity, thus, contributing to capital formation and employment generation. M&A, on the contrary, are more relevant for multinationals (foreign-owned capital stock) (Hilmi et al., 2007, pp. 248-249).

2.1.1.6. Acquisitions

Acquisitions (also **Brownfield investments (BFI)**) take place when an organization purchases or leases already existing manufacturing facilities in order to launch a new production facility or to expand/upgrade the existing one to secure superior returns (www.investopedia.com). This kind of investment is optimal when the host market is characterized by intermediate values (Müller, 2001, p. 1). Moreover, acquisition is the core MEM to *quickly* achieve a greater market share (thus, greater market power) and is primarily preferred by MNCs that may buy a competitor, a distributor, a supplier, or a business in a highly related industry (either through a friendly or hostile acquisition) to capture CA in the overseas market (Kotelnikov, 2001). The hostile acquisition implicates the purchase of the target company's stock (thus, gaining control over its assets and operations).

Hill (1994) stated that advantages of BFI are the disadvantages of GFI and that their costs depend on the goodwill of the overseas company to be acquired. The main advantages and motivations for an acquisition are (Hill & Jones, 2003, pp. 312-313):

- the *fastest* and the *largest* market entry and market penetration *of all* MEM alternatives through acquisition of a complementary product/ technology/ business /markets / distribution channels, etc.;
- fast realization of ES and economies of speed enabled by the acquired additional mass;
- fast refunding of the flowed inventions and quick generation of profits;
- a lower risk investment due to easier and more accurate estimations of costs, risks, and benefits;
- the possibility of absorption of the already existing strategies, structures, and processes, and experienced HC;
- low risks related to product development;
- an easy way to overcome ME barriers, etc.

The disadvantages identified by Hill & Jones (2003, p. 316) include:

- poor offers from firms that can be acquired;
- high resource requirements;
- high danger of non-acceptance in the host market;
- integration problems as the most complex issue of all: primarily because of culture and organization differences, different control systems, relationships, etc.);
- financial problems because of increased levels of debt;

- competitive constrictions;
- too much diversification (thus, lack of performance management in the long run), etc.

In view of its updating power, BFI are often preferred to revive the abandoned or ineffective facilities (e.g. to reconstruct old mills).

2.1.1.7. Strategic Alliances

Strategic Alliances (SA) are cooperative agreements between independent partners (actual or potential competitors) who intend to collectively manage to achieve objectives of common interest (Pellicelli, 2003, p. 1). According to Inkpen & Ross (2001, p. 132), SA are often difficult to realize because of their cost- and time-consuming nature. They are also more complex and fraught with more uncertainty than other MEM. That is why SA emerge only after a long-term negotiation process.

On the other hand, SA are characteristic of a turbulent economy (technological innovations that break barriers between sectors, ever-increasing competition, market globalization) (Pellicelli, 2003, p. 2). In the globalized world of today marked by converging industries, blurred traditional lines between business sectors and the same basic product offerings worldwide (Levitt, 1984, p. 2), SA seem to be the only rational way of developing complex skills within a limited time frame. Furthermore, SA help decrease competitive intensity excluding potential entrants and also secure the establishment of complex value chains that will serve as further entrance barriers.

The basic forms of SA are: **shared research**, **formal JV** and **minority equity participation** (Kotelnikov, 2001).

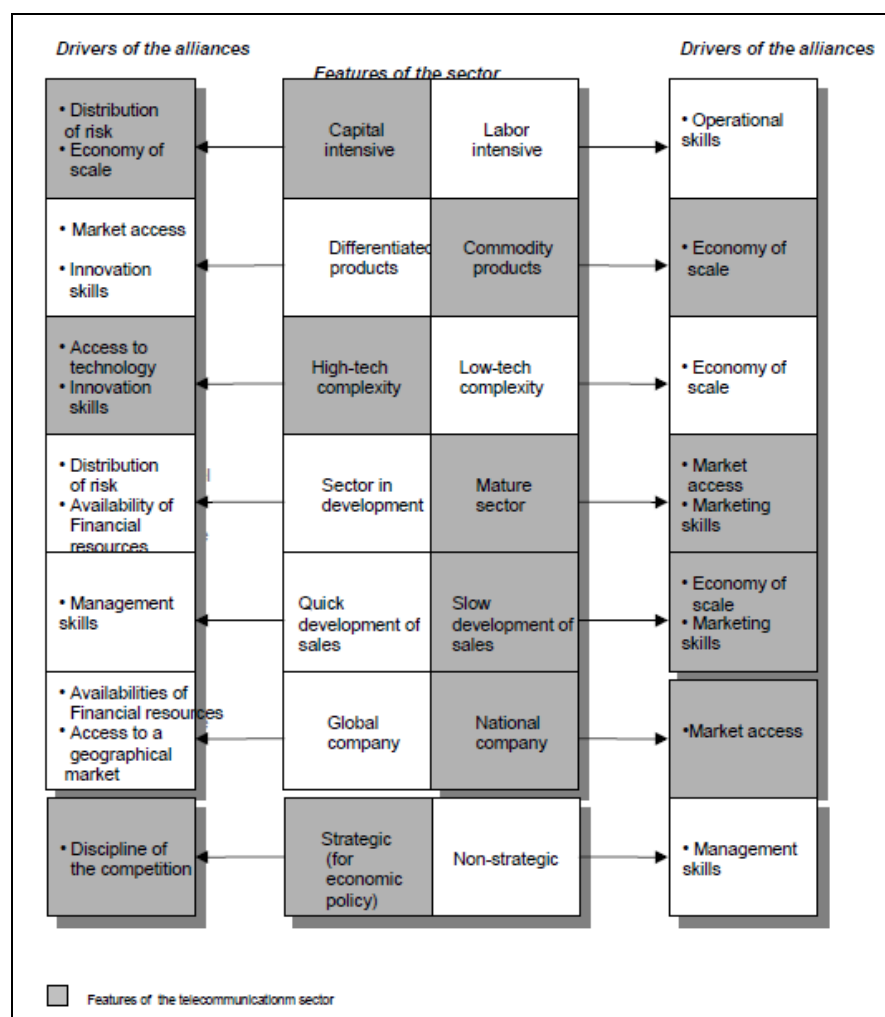
The logic behind SA is the **Defend**, **Catch-up**, **Remain**, and **Restructure** strategies (Kotelnikov, 2001). Therefore, the primary motivations for SA are (Lymbersky, 2009, pp. 207-209; Hill, 1994):

- increased ES and ESC, thus, significant cost reduction;
- ease of market entry enabled by shared risks and costs, shared K and expertise (acquisition of new KH);
- synergy and CA, thus, no concerns about rivalry;
- relatively high flexibility;
- financial benefits guaranteed by limited capital requirements;
- easy implementation of standards, especially in case of developing and commercializing a system technology (e.g. in the electronic industry).

Basic disadvantages, on the contrary, encompass (Lymbersky, 2009, pp. 217-220; Hill, 1994):

- a long reconciliation process because of the incompatibility of partners, conflicts over distributing earnings and constantly changing circumstances;
- threat of KH outflow, thus, loss of critical technology, CC, and skills (or CA);

- hampered balance between cooperation and competitiveness, which may lead to the asymmetry of distribution of critical resources and CC and even to the erosion of the other partner's competitive position or a take-over;
- lame motivation enabled by limited commitment;
- complicated profit measuring;
- limited access to information and significant problems caused by the wrong partner choice.



Generally speaking, SA have a long history. The alliance between *Ford* and *Mazda*, e.g., dates back still to 1931 (Pellicelli, 2003, p. 2). Another classical example of a SA is *Caltex* which got access to petrol deposits in Bahrain upon creating an alliance with a crude oil supplier from the Middle East (Pellicelli, 2003, p. 2).

2.1.1.8. Joint Ventures

In contrast to WOM, International Joint Ventures (IJV) are established by already existing firms which pull together complementary resources (financial, technical, HR, goodwill, KH, team spirit, and other intangible assets) in order to secure returns that none of the parties could obtain acting on its own (Hill, 2003, p. 486; Kotelnikov, 2001). Therefore, IJV can be defined as an enterprise in which two or more investors share ownership and control over property rights and operations.

The common objectives of IJV include: a fast and effective ME (entering into new geographic markets or related businesses), risk/cost/benefit sharing (increase in profit margins, acceleration of revenue growth), technology sharing and joint product development (share of scientists or professionals with unique skills), fast and easy access to new distribution channels and political connections, conformance to government regulations. In other words, JV are a practical vehicle for outsourcing operations and transfer of K (or CA, or even innovation), thus, securing enhancement of performance, quality, and efficiency of local companies.

The level of control depends hereby on the ownership split and the number of parties involved, which, in turn, implicates that control must be necessarily shared among venture partners (Root, 1987, p. 7). The dissemination risk is, therefore, very high. The overall risk refers to the risk related to the fact that the corporation's specific advantages in KH will be expropriated by a licensing partner. This, in turn, would reduce quasi rents that could be earned from the KH.

In view of the conflicting pressures to cooperate and compete, IJV are frequently established only for a limited life span because of limited amount of assets, limited service life of assets, limited efficacy of joint manufacturing activities. Further factors and requirements to consider before setting up an IJV include (Hill, 1994):

- understanding of CC, needs, and resources of overseas partners;
- choice of an appropriate partner and securing the effective organizational design;
- compatible corporate vision, strategies, management styles, and company size;
- engagement and motivation of all partners to enable productivity of an IJV (ownership, control, length of agreement, pricing);
- Capital and KH have to be united, so that partners' inputs complement those of one another (shared resources and simultaneous protection of own proprietary resources).
- financial strength and stability;

- complementary products, markets, and services;
- effective two-way communication;
- government intentions.

In view of the aforementioned determinants, IJV involve a very long negotiations and coordination process, in which each party attempts to overtake the hierarchal control, maximize its advantage and own competitive position at the same time. A too hasty establishment of IJV and poor planning (cost overruns, poor analysis of customers and environment, etc.) lead to significant problems. On the other hand, IJV are most favorable when (1) partners' strategic goals converge and their competitive goals diverge; (2) when partner's size, market share and resources (finance and management skills) are much lower as compared to industry leaders; (3) K and property share coupled with simultaneous access limit to parties' proprietary skills; (4) when IJV is used to reduce political friction in an overseas market. Thus, the primary benefits of IJV include: *joint financial strength* and *source of supply for a third country*.

The disadvantages, on the contrary, encompass the following issues:

- partners do not have full control of management or may have an ineffective blending of managers who are not accustomed to working together or approach issues in an entirely different way (thus, a slowdown in decision-making and efficiency);
- impossibility to recover capital;
- partners may have mistrust over proprietary K and disagree on third party markets (asymmetric new investments);
- different views on expected benefits (performance ambiguity) and other financial disputes;
- cultural clashes;
- conflicts over the termination of the relationship (Guterman, 2002, pp. 4-6).

During the Cold War and political susceptibility of the communist party to foreign property of means of production, IJV were the only means of entering Eastern European markets (low-cost labor vs. technology and financial means). In the early 90s, IJV turned into the best way for setting up collaborations between the post-communist and capitalist worlds (modernization of production facilities) (Pellicelli, 2003, p. 10).

2.1.1.9. Cooperation

Cooperation is a contractually arranged or silently agreed upon collaboration between legally and economically independent companies in order to achieve common goals and objectives (Contractor & Lorange, 2002, p. 26). The main characteristics of cooperation are just-in-time supply, public-private partnerships (regardless of sectors), common objective setting, optional collaboration, etc. (Hill, 1994). The basic motives for choosing cooperation as a foreign MEM are advancement of mutual interests and success, external growth, product and K connection, cost reduction and cost optimization, innovation, and tax benefits (Contractor & Lorange, 2002, pp. 27-28; Beamish & Killing, 1997, p. 4; Hill, 1994).

Advantages of starting cooperation include primarily synergy effects enabled by sharing risks, responsibilities, CC, and benefits (Kotelnikov, 2001; Beamish & Killing, 1997, p. 134). In particular, advantages are related to collaborative labor, better information and experience flow, collective accomplishment of large projects, collective and advanced further education of staff, corporate advertising campaigns, improved customer service, constant productivity growth and quality enhancement, improved market position secured by a broader and more attractive portfolio of products and services. Risks of cooperation, on the contrary, encompass significant losses of company autonomy, waste of time and effort related to long coordination and planning (thus, high coordination costs), share of KH, liabilities of partners, the wrong choice of partners, etc. (Contractor & Lorange, 2002, pp. 13-14; Kotelnikov, 2001; Hill, 1994).

In view of the fact that governmentally recognized partnerships may enjoy significant **tax benefits**, cooperation is often favored over corporations in terms of tax policy (especially in developed countries where dividend taxes are levied before dividends are distributed among partners). On the other hand, partnerships of politicians and corporations may lead to ethical problems and corruption. Thus, anti-trust laws which are called forth to restrict monopolistic practices and foster free market competition are a must (Kotelnikov, 2001).

2.1.1.10. Exporting

First and foremost, it should be pointed out that exporting is almost always the first EM companies consider before entering a foreign market due to its simplicity in implementation, minimal risks and limited international marketing effort. Subsequently, they may switch over to another MEM. In addition, exporting is the basic MEM used by manufacturing firms where there are barriers to investment (Peng, 2011, p. 166; Kotelnikov, 2001).

One distinguishes between **Indirect** and **Direct Exporting**. *Indirect exporting* presupposes the participation of domestically-based intermediaries (importers or distributors) that overtake export transactions, whereas production is effected in the home country (Peng, 2011, p. 312). *Direct exporting*, as the most common mode of exporting for SMEs, implicates, on the contrary, selling directly to foreign markets, i.e. involving *no* local market middlemen. Nevertheless, sometimes intermediaries in the overseas markets may overtake the job (Peng, 2011, pp. 312-313).

The major types of direct exporting include **direct agents** who are responsible for marketing exported goods overseas (sales on commission) and **direct branches** or **subsidiaries** where the organization uses its own sales teams to sell in foreign markets (Kotelnikov, 2001; Hill, 1994).

Apart from the aforementioned **advantages**, benefits of exporting also encompass ES, avoidance of costs associated with setting up manufacturing facilities in a foreign country, better protection of intangible property (e.g. patents). In addition, exporting allows a company to participate in the overseas markets with barriers to FDI (Kotelnikov, 2001; Hill, 1994).

Disadvantages, on the contrary, include high transport costs (especially for bulk products), trade barriers, susceptibility to exchange rate fluctuations, and problems related to dealing with local marketing agents. Nevertheless, the indicated problems may be successfully solved if the company sets up a wholly owned marketing subsidiary in the host country (Kotelnikov, 2001; Hill, 1994).

Generally speaking, *direct exporting* is most recommendable for companies with the primary focus on *international markets* as their crucial marketing distribution strategy (e.g. for manufacturers of highly technical services or production machinery), whereas *indirect exporting* is advisable for firms which prefer to avoid financial risk as threat to success, since the export partner normally overtakes most of the expenses related to sales in the overseas markets (Peng, 2011, pp. 312-313).

Nowadays, the **Internet** is becoming an increasingly important foreign EM. In the past, Internet sales were limited only to domestic marketing. Today, a surprisingly larger number of companies receive orders from all over the globe (*Amazon*). This development results, in turn, in the so-called **international Internet marketing** (Albaum & Duerr, 2008, p. 571).

2.1.1.11. Turnkey Projects

Turnkey projects (TKP) implicate that a product or service can be implemented or utilized with no additional work required by the host company. The only thing that is left is just to “*turn the key*,” so to say. Therefore, the contractor agrees to handle all the details of the project for a foreign client including training of the operating personnel (Albaum & Duerr, 2008).

In view of the utmost complexity, TKP are very popular in sales to foreign governments and serve as a means of exporting process technology in chemical, pharmaceutical, petroleum, and mining industries (Onkvisit & Shaw, 2008, pp. 243-267).

The primary advantages of TKP are related to earning great economic returns from the KH and exporting process technology (especially to countries where FDI is limited by host government regulations). TKP are less risky as compared to FDI in countries with unstable political and economic environment (Albaum & Duerr, 2008, p. 383).

The basic disadvantages of TKP include the fact that the investor has no long-term interest in the host country. Further disadvantages encompass the threat of creating a potential competitor, since selling a source of CA automatically implicates selling the CA to potential rivals (Kotelnikov, 2001).

SUMMARY:

The choice of a specific MEM is a rather case-specific. Each has its advantages and disadvantages, risks and benefits. Yet, in general, the choice of the FEM depends upon the following decision criteria: market size and growth, risk perceived, host government regulations, competitive environment and cultural distance, local infrastructure.

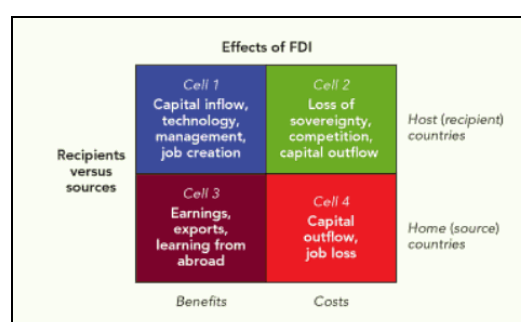


Figure 8: Effects of FDI on Home and Host Countries (Source: Peng, 2011, p. 194)

In addition, FDI increase insecurity and risks of job loss and reduced wages in the invested industries as well as income distribution in the parent country caused by the relatively higher demand for skilled and unskilled labor (not to mention of ethical issues).

Still, the *job-creating effect* of FDI exceeds the job-substituting effect. At worst, their impact on employment both in the home and host countries is neutral (Hilmi et al., 2007, p. 247).

From the perspective of the host country, proper balancing between positive (technology transfer, increased exports, upgraded skills) and negative effects of foreign investment (financial volatility, anti-competitive practices, dependence on foreign ownership) both in the short term (entailing economy deterioration) and in the long run (increase in host economy performance) is the primary task of governments to secure not only quantity, but also quality FDI.

2.2. Market Entry Strategies

According to Hill & Jones (2012, p. 261), market entry strategy (MES) aims at identifying and taking actions that will reduce costs of value creation and/or add value through better serving consumer needs. As opposed to strategy development for a single country (with one government, one legal system, one currency, and one accounting system), international strategic management implicates dealing with multiple governments, currencies, and cultures. This, in turn, underscores the relevance of international complexities that offer three basic CA: **global efficiencies**, **international flexibility**, and **worldwide learning**. Consequently, effective international strategic management should be understood as an ongoing and comprehensive process that has to be constantly updated and adapted to (Lymbersky, 2008, pp. 23-25; Kotelnikov, 2001).

Just as mentioned above, an internationally operating company may improve its efficiencies in a number of ways: through **location efficiencies**, **economies of scale** and **economies of scope** (Lymbersky, 2008, p. 26). **Location efficiencies** are achieved when production or R&D are placed in a country with cheap labor and/or skilled workforce. This, in turn, lowers the product price and distribution costs, improves quality and customer service. One of the illustrative examples is *Volkswagen* that placed its production in China (low-cost labor). *IBM*, on the contrary, capitalizes on India's skilled programmers (Lymbersky, 2008, p. 26; Kotelnikov, 2001).

Economies of scale designate an increase in economies due to the increase in the scale of production. *Daimler* e.g. produces its *M Class SUV* in Alabama and then delivers it throughout the world. Centralized production and decentralized marketing prove much more cost-effective than building factories in various countries (Lymbersky, 2008, p. 26).

Economies of scope are achieved by diversifying the company's product lines in each of the countries of entry in order to lower overall production costs and enhance overall bottom lines. In particular, this strategy implicates that one single product is related to comparatively high distribution and marketing costs, whereas costs per unit are significantly reduced in case of a diversified product portfolio (Lymbersky, 2008, p. 26).

International flexibility turns out a successful strategy in case of changes in demand, economies, political systems, changes in law in the home country. Most corporations modify their production or processes because of domestic changes. Yet, some do *not*, since international demand flexibility offers a valuable solution. A good example is the chicken processor *Tyson Foods* which benefited from the increased demand by health-conscious US consumers for chicken breasts. The surplus of chicken legs and thighs were sold at the

Russian market where dark meat is preferred over the light one, whereas the Chinese market was targeted with chicken feet which are considered a tasty delicacy there (Lymbersky, 2008, p. 26).

Worldwide learning, which is of primary importance for the author of the current thesis, is an integral part of global operations: companies learn through adapting their business models, processes, and marketing techniques to local requirements. This invaluable K can be also used in other countries (e.g. some corporations may learn how to deal with strikes or how to quickly and efficiently end one) (Mintzberg et al., 2003, p. 284).

Yet, the most important example of worldwide learning is “**emerging opportunities.**” This term implicates K share and K diffusion to secure *constant improvement* and *sustainable CA* in *all* subsidiaries internationally. E.g. *General Electric* introduced a system of 12 management councils. Their members are senior executives who meet on a regular basis and have to present an idea that could also be applied in other business units. As a consequence, creative, innovative, and, assuredly, effective solutions are spread quickly, whereas their implementation is effected almost simultaneously in *all* subsidiaries all over the globe. Another good example is the *Bayern AG*, Germany, which offers highly skilled young managers an International Management Trainee Program (different job positions in sales, marketing and controlling over three years abroad) (Lymbersky, 2008, pp. 27-29).

In view of the aforementioned coupled with extremely competitive markets driven by the liberalization of world trade and ongoing globalization, a MES is a must (Mintzberg et al., 2003).

To find the right balance between *global efficiencies*, *worldwide learning* and *multinational flexibility* (or cost pressures coupled with pressures for local responsiveness), companies normally have to adopt one of the following **four strategies: global strategy, international strategy, multi-domestic strategy** and **transnational strategy** (Hill, 2003, p. 422).

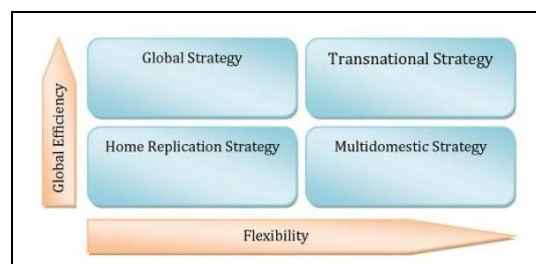


Figure 9: Market Entry Strategies (Source: Lymbersky, 2008, p. 29)

2.2.1. Global Strategy

Establishing a successful global strategy (GS) is a long and tedious process where the main issue consists in understanding the nature of global industries and dynamics of global competition (Bartlett & Ghoshal, 2002, p. 28). GS is based on the assumption that the world is the market with homogeneous wants and needs, or one big Village, so to say. Thus, companies prefer to market a *standardized* product, *not* to customize it (e.g. *SAP* standardized cross-company software). *ES* are therefore an integral part of GS (Hill & Jones, 2012, p. C251; Mintzberg et al., 2003, p. 283).

Sometimes only one department can be used for global marketing. Standardized marketing and distribution, centralized decision-making coupled with production outsourcing are typical characteristics of GS. E.g. *Sony* produces its TV sets, stereos, and gaming consoles for the global market, whereas only cheap parts like power supplies and fuses are adapted to some local markets (Lymbersky, 2008, pp. 30-31).

Hill et al. (2012, p. 334) claim that GS involves configuring the firm's value chain to maximize value adding at each stage. The strategy in question demands high degree of control over operations in different affiliates. Therefore, a WOS for centralized production is favored most. GS is also highly concentrated, which implicates that oligopolistic interdependence spills over national boundaries and significantly impacts competitive strategies of the parties involved.

Bartlett & Ghoshal (2002, p. 31) provide a illustrative example of *Matsushita Electric* and *Panasonic Corporation* whose GS resulted in a strong global distribution network; the company-wide mission statement; high level of financial control; more applied and market-driven R&D; ability to reach the target market quickly and impose own standards, since an individual country's buy-in was not required any more.

2.2.2. International Strategy

According to Hill (1994), international strategy (IS) stands for *manufacturing and marketing in major host countries under the control of the headquarters coupled with inland R&D*. Corporations that follow this strategy are established brand names such as e.g. *IBM, Procter & Gamble*.

The basic components of IS encompass *distinctive competence, resource deployment, scope of operations, and synergy* (Lymbersky, 2008, pp. 32-33). The company's **distinctive competency** can be characterized either by **technological KH** (e.g. Anti Lock Brakes of *Bosch GmbH*, Germany, which are very hard to beat even today) or **management KH** (e.g. *McDonalds* and its distinct efficiency in customer service known worldwide) (Hill & Jones, 2012, pp. 291-292).

Resource Deployment implicates deployment of resources upon choosing an appropriate market for entry: i.e., a WOS (100% ownership) vs. only a limited percentage of investment coupled with the involvement of other investors. An illustrative example is *Disneyland Paris*, whose parent entity, *Disney*, made a strategic decision to sell a certain percentage of the stock of its holiday and recreation center in Paris to outsiders (instead of bailing it out of financial difficulties all on its own) and saved the economized finances for more lucrative ventures and acquisitions instead (Lymbersky, 2008, p. 33).

Scope of operations (SO) stands for a geographical region or a market that the company intends to enter (high-quality market vs. low-cost market). SO is tied to distinctive or CC, since resources might be scarce in certain regions. In addition, distribution costs might be too high to capitalize on the advantages of the distinctive competence. Thus, SO focuses on *where* CA could be exploited to advantage most. E.g. *Texas Instruments* focuses on digital signal processors that can convert analog signals into digital signals. Such chips are found in mobile phones or modems of all kinds today (Lymbersky, 2008, p. 33).

Synergy implicates that the company's benefits outweigh the sum of single benefits. *British Airways* e.g. gives away and/or sells merchandising products on their flights. These, in turn, lead interested people to Internet sites of merchandise manufacturers and/or sellers in new foreign countries, which again suggest visiting them directly through booking a flight with *British Airways* (Lymbersky, 2008, p. 33).

2.2.3. Multi-Domestic Strategy

According to Hill (1994), a multi-domestic strategy (MDS) is identified as a customized product offering adapted to specific local conditions. MDS is based on the so-called **home replication strategy** (HRS) which implicates the replication of the home market advantages in an overseas market, or the transfer of the company's CA from its home market abroad. German carmakers *BMW*, *Mercedes*, *Audi* e.g. apply this strategy worldwide (Lymbersky, 2008, p. 30). Yet, in the case of MDS, multi-replication of the home strategy takes place: subsidiaries in each country of entry are relatively free to customize their marketing, products, and operations to suit local consumers most.

Hill et al. (1990, p. 120) stated that MDS is based upon the assumption that national markets differ considerably with regard to consumer preferences, competition, operating conditions and political, legal, and social structures. Thus, MDS is marked by a low degree of control and favors contractual agreements or IJV as the primary mode of entry.

Besides, in the case of big cultural differences, customization is a very effective strategy. On the other hand, low ES caused by customization of production, distribution, and marketing lead to a more complex coordination process. Corporations that pursue a MDS are *marketing-driven*. E.g. customers of *Unilever* and *Kraft* have to be targeted with special campaigns in each market (Lymbersky, 2008, p. 30).

Consequently, the main features of MDS are (Bartlett & Ghoshal, 1997): product customization for each distinct market, decentralized control and local decision-making. The basic advantages include product differentiation, local responsiveness, minimized political risk, and minimized exchange rate risk.

Philips is one of the vivid examples of a company that pursued MDS. Its strategy resulted in innovation from local R&D, lively entrepreneurial spirit, products tailored to the needs of individual countries, high quality due to backward integration (Bartlett & Ghoshal, 2002, p. 101; Hill, 1994). On the other hand, MDS created numerous challenges for *Philips* (Bartlett & Ghoshal, 2002; Hill, 1994):

- (1) high costs incurred because of custom-tailored products and duplication throughout the world;
- (2) Innovation from local R&D resulted in R&D-driven, *not market-driven*, products.
- (3) Decentralized control entailed the necessity of national buy-in before a product launch, thus, time-to-market took very long.

2.2.4. Trans-National Strategy

Transnational strategy (TNS) combines the advantages of the GS (ES, thus, efficiency) with those of MDS (no centralized decision-making, thus, flexibility). As a result, parts of production and R&D can be centralized, marketing and HR, on the contrary, are decentralized to adapt to specific and rapidly changing requirements of local markets and cultural differences. Yet, just like a MDS, TNS are often very costly to coordinate (Lymbersky, 2008, p. 31).

As a good example serves *IKEA*, a world-known producer of inexpensive furniture. It goes without saying that the company's cost-efficiency depends heavily upon standardization. On the other hand, *IKEA*'s marketing campaigns vary from country to country to appeal to local tastes and habits (Lymbersky, 2008, p. 31).

SUMMARY

In the final analysis it should be pointed out that the rise of numerous MNCs on the global arena is the indication of the essentially indispensable liberalization and internationalization of world trade. Rising costs, intense local and global competition, overseas opportunities and liberalized investment policies further contribute to the rapidly expanding globalization (Hilmi et al., 2007, p. 243).

As a result, MNCs located in developing countries are characterized by similar firm specific advantages as compared to those from developed countries. Nevertheless, the essence, proportion, and distribution of CA differ considerably: developed nations possess key assets, such as technological KH, global brands, intellectual property, whereas in developing countries production process capabilities and networks coupled with organizational structures prevail (Hilmi et al., 2007, p. 243). In addition, developing countries are still focusing on raw materials (primarily, state-owned) as their major strategic export asset. Hence, they are still bound to lag behind internationally until the strategic importance of K and intellectual assets gains more weight on a national scale (Hilmi et al., 2007, p. 243).

In view of the above mentioned, it is obvious that the choice of MEM has significant impact on international operations and the company's success in general. Therefore, it can be regarded as a frontier issue in international marketing (Wind & Perlmutter, 1977, cited by Zhao & Decker, 2004, p. 2) and as one of the most critical strategic decisions for MNCs (Root, 1994, cited by Zhao & Decker, 2004, p. 2). As a consequence, the choice of MEM will influence *all* future decisions and performance indicators of the company in overseas markets, and will entail a concomitant level of resource commitment that are so difficult to transfer

from one country to another (especially from high level to low level) (Zhao & Decker, 2004, p. 2; Hilmi et al., 2007, p. 243).

3. Firm Theories

Just as mentioned above, K is the source of CA (Eisenhardt & Santos 2000, p. 1). Moreover, K is a dynamic resource that can expand and develop over time (and with its use). Intellectual capital (both tangible, or explicit K, and intangible, or tacit K, that resides in the minds of individuals) (Nonaka & Takeuchi, 1995, p. 59) is, therefore, used to create wealth (Stewart, 1997). The abundance of virtual products coupled with the current movement towards intellectual property confirms the aforementioned phenomenon.

Consequently, the ongoing dialogue between tacit and explicit K plays a critical role in the dynamic process of organizational K creation (Nonaka & Takeuchi, 1995, p. 14). K search, articulation and share, K storage, creation, and transfer are an integral part of the K creation spiral.

Nevertheless, since K creation is very difficult to control, it is easier to manage the environment in which it is shared, created and applied. Hence, **culture** is of paramount importance to secure CM and ongoing K share and new K creation. Thus, culture change serves as the foundation of proper knowledge management (KM). As a vivid example serves Procter & Gamble and its Open Innovation Strategy as well as the corporation's close collaboration with lead users on a global scale (Huston & Sakkab, 2006, pp. 1-3).

In addition, *"firms are organizations that represent social knowledge of coordination and learning"* (Kogut & Zander, 1996, p. 502). On the one hand, **productivity grows with the division of labor**, yet, on the other hand, **specialization increases the costs of communication and coordination (the fundamental dilemma of MEM)**. Therefore, the shift from treating firms only as those concerned with ownership, incentives, and self-interest towards "unsocial sociality" leads to understanding of social K as an economic value and strategic asset that supports coordination and communication. Moreover, since firms are also *social structures* (i.e. learning, coordination and communication reside not only in physical products, but also mentally), the assemblage of elements that compose an organization are subject not only to the primarily considered technical feasibility and permissibility, but also to the logic of shared identity (Kogut & Zander, 1996, p. 502).

Numerous studies show that sharing of KH with the goal of helping the entire organization learn from frontline employees' experience, ideas, and insights is one of viable ways of transferring tacit K as a critical resource for ordinary work practice. On the other hand, mere codifying of tacit K into corporate policies, procedures, and beliefs as guidelines for effective action proves inadequate or even erroneous for generating new K, managing its

distribution, and fostering creativity and innovation, especially in large organizations (e.g. Xerox) (Bobrow & Whalen, 2002, p. 1).

An extensive analysis of literature related to the topic in question leads to the conclusion that no prominent theories were developed recently, although a wide range of empirical studies were conducted to test the validity of the prevailing models. These, in turn, help identify the determinant factors that impact the choice of a specific MEM and measure their respective effects (Zhao & Decker, 2004, p. 3).

First and foremost, the “resource-based perspective on strategy” (RBP) is traditionally traced back to Edith Penrose and *The Theory of the Growth of the Firm* (1959). Its modern manifestation is dated back to 1984, the year of publication of Wernerfelt’s *A Resource-Based View of the Firm* and Rumelt’s *Towards a Strategic Theory of the Firm*. Later on, works of Barney, Montgomery, Dierickx, Cool, Amit and others appeared. Their primary interest was placed around **resources**, **capabilities**, and **competencies**. Nowadays, the RBP is arguably the dominant contemporary approach towards strategy research (Foss & Robertson, 2000, p. 11). This, in turn, implicates that (1) **firms** are viewed *essentially* as **repositories of competence** (or repositories of K capital that allows its holders to perform activities and solve problems more efficiently as compared to others), and (2) **the firm’s ability to accumulate, protect and eventually to deploy its competencies** is regarded as the primary determinant of its long-term or **sustained CA** (Foss & Knudsen, 1996, p. 1). In view of its skill-like character, competence is, thus, on the one hand, tacit in nature and asymmetrically distributed, and, on the other hand, in the context of the theory of the firm and strategic management, it is viewed as a property of firms rather than of individuals (therefore, it is hard to replicate and transfer).

In addition, in the last decade, a lot was said as to the role of MNEs in the global economy. Some view such corporations as agents for economic development upgrading the quality of indigenous resources and capabilities (Dunning, 1993, p. 362), whereas others argue that MNEs constitute potential threats to welfare and democracy (van Tulder & van der Zwart, 2006, p. 268). Those who have mixed feelings see MNEs rather as multinational creatures with a *Janus face* and take the standpoint that multinationals have to be sufficiently controlled by governments and international regulating bodies to secure their positive contribution to different countries’ economic welfare (Forsgren, 2008, p. vii).

Generally speaking, the basic approaches towards understanding the MEM include: (Zhao & Decker, 2004, pp. 3, 27):

(1) **the Stage of Development (SD) Model** (Johanson & Paul, 1975), according to which internalization of SMEs entails a slow incremental process of cultural and geographical

expansion and commitment. Thus, the SD Model is based on experiential learning moving from a low-commitment MEM (i.e. no regular export activities) to high-commitment modes (exporting via independent agents up to the establishment of an overseas WOS) depending upon the level of experience and K of the host market (Susman, 2007, p. 231). Furthermore, the strategies of smaller firms are normally subject to high degrees of serendipity or fortunate and unplanned discoveries made by chance (Meyek & Skak, 2002, cited by Susman, 2007, p. 231);

(2) the Transaction Cost Analysis (TCA) theory and its extensions (Anderson & Gatigton, 1986; Hill et al., 1990; Erramilli & Rao, 1993), according to which efficiency maximizing companies adopt the MEM which minimize transaction costs. The rationalists of the TCA theory underscore the primary relevance of *risk, uncertainty and control* for the MEM decision. Moreover, numerous uncertainties may be eliminated through government programs and network contacts (Susman, 2007, p. 232). Thus, indirect exporting is referred to as a MEM of relatively low risk, low resource commitment, low ROI, low uncertainty and low control, whereas FDI, on the contrary, - as a MEM of high risk, high resource commitment and high ROI (Chung & Enderwick, 2001, cited by Susman, 2007, p. 232);

(3) the Ownership, Location and Internalization (OLI) Model or Eclectic Theory (Dunnig, 1977), according to which the choice of the respective MEM depends upon the three sets of advantages: *ownership, location, and internalization* (a static model). The Eclectic Theory is rational and focuses on the advantages that impact the internalization process. It was tested and supported by numerous researchers (Brouthers et al., 1999, cited by Susman, 2007, p. 232), who conclude that the OLI Model is particularly suitable for predicting the MEM of SMEs (Nakos & Brothers, 2002, cited by Susman, 2007, p. 232);

In addition, the ownership-specific advantages implicate the relevance of the resource-based view (RBV), thus, necessitating the ownership of assets that substitute the firm's *core competences* (e.g. patents, trademarks, raw material possession, and technological KH).

(4) the Organization Capacity (OC) Model (Aulakh & Kotabe, 1997; Madhok, 1998), according to which the MEM decision is dependent upon the deployment and development of the firm's capacity. This, in turn, implicates that the OC view of the firm-specific advantage extends far beyond its ability to reduce transaction costs. The rents stemming from the firm-specific advantages are mostly entrepreneurial rents, thus, implicating the uniqueness of each firm as well as its resources and capabilities (Forsgren, 2008, pp. 56, 64);

(5) the Decision Making Process (DMP) Model (Root, 1994; Young et al., 1989), which view the MEM decision as a multistage decision making process, whereas the impact of organization efficiency and decision maker is ignored.

Generally speaking, the choice of a respective MEM depends heavily upon the TCA theory and the RBV of the firm. In other words, when entering into new markets, firms have to consider the costs and resources required to sell and service their products overseas as well as to learn from customers, competitors, and other stakeholders. In addition, issues related to the choice of protecting the firm's own intellectual capital is of paramount importance (Susman, 2007, pp. 233-234).

Moreover, according to Ellis (2000, p. 445), K of foreign market opportunities is commonly acquired via existing interpersonal links rather than through systematic collection of data and market research. In addition, the relevance of *social media*, *complaint management* (Kotler & Armstrong, 2009, p. 154), and *relationships marketing* (Payne, 1993, p. 32) (as sources of invaluable information for improvement and organic growth) further confirm the importance of relationships and K as basic strategic assets in today's business environment. Thus, *network connections* (such as existing customers) and *motivation* for expanding abroad impact the MEM significantly. If e.g. there is already a captive sales audience waiting for the seller, ownership overtakes a primary role (e.g. the WOS decision). If, on the contrary, the firm is the "initiator" and is seeking potential markets, then it is likely to contract for its sales and probe the new territory (Susman, 2001, p. 232).

In the past decade, most of the significant studies were related to examining the influence of specific factors on the choice of the respective MEM. Among these determinants, institution attracted most attention. Some papers extended the TCA theory by complementing the framework of analysis with institutional factors (Brouthers, 2002, and Lu, 2002, cited by Zhao & Decker, 2004, p. 4). Other researchers argued that institution affects the MEM choice by increasing the cost of uncertainty and transaction (Said & McDonald, 2002, and Meyer, 2000, cited by Zhao & Decker, 2004, p. 4). Further determinants which were examined empirically encompass (Zhao & Decker, 2004, p. 4):

- *technology transfer* (Mattoo, 2001),
- *immigrant effect* (Chung & Enderwick, 2001),
- *market size* (Nakos & Brothers, 2002; Eicher & Kang, 2002; Chung & Enderwick, 2001),
- *firm size* (Leung et al., 2003; Nakos & Brouthers, 2002; Evans, 2002),
- *CEO successor characteristics* (Herrmann & Datta, 2002),

- *cultural distance* (Leung et al., 2003; Chen & Hu, 2002; Gillespie, 2002; Evans, 2002; Cristina & Esteban, 2002),
- *industry barriers and firm advantages* (Chen & Hennart, 2002; Siripaisalpipat & Hosbino, 2000),
- *international experience* (Reuber & Fisher, 2003; Evans, 2002; King & Tucci, 2002),
- *country risk and environmental uncertainty* (Cristina & Esteban, 2002),
- *role of staffing* (Konopaske et al., 2002), as well as
- *foreign exchange rate and host country currency* (Baek & Kwok, 2002).

All the aforementioned factors can be generalized grouped into **country specific factors** (cultural distance, institution, exchange rate), **industry specific factors** (market size, market structure, etc.), **firm specific factors** (firm capacity, firm size, etc.) and **product specific factors** (product type, product maturity, etc.) (Zhao & Decker, 2004, p. 4).

Just as indicated above, there is not much congruence as to which of the models is/are most applicable to the respective MEM: each model has its limitations and critical issues. Yet, apart from environmental and transaction-specific factors (or efficiency considerations) that influence MNCs' choice of MEM, an MNC's global strategic posture is also of paramount importance. The results of studies conducted by Chan & Hwang (1992, p. 50), underscore the significance of expanding in mindsets and decision-making beyond the narrow confines of each MEM decision. A global strategy mindset is, thus, a must, especially when it comes to considering an ILA, IJV, and WOS.

As far as technology transfer is concerned, MNEs generally prefer direct entry to acquisitions, when technology transfer is related to high costs (thus, a smaller cost advantage over domestic firms and a high acquisition price). Host governments, on the other hand, prefer acquisitions, since they lead to a larger extent of technology transfer and a relatively higher acquisition price for the domestic firm (Mattoo, Olarreaga & Saggi, 2001, p. 22).

In addition, a thorough understanding of local, indigenous markets and the ability to service these needs without compromising on the company's goals, ethics, and reputation is key to success on an international scale. In particular, despite increased globalization and consolidation of markets, there are still significant discrepancies between various regions and nations which are necessarily to be taken into account (Hite, 1991, pp. 35-36).

In view of the complexity of the MEM models and their paramount importance for the firm's future, the author of the given paper will further focus on the **knowledge based theory (KBT)**, **resource based theory (RBT)** and **organizational capability theory (OCT)** to

examine how these strategies influence the choice of the respective MEM. Various other theories suggest other interpretations. Yet, in view of the market dynamics and global complexity, it is evident that there is a gradual shift towards an integrated approach towards studying MEM (an amalgamation of most valuable and congruent ideas).

3.1. Knowledge Based Theory

According to Nonaka & Takeuchi (1995, p. 8), knowledge is distinct from just data and information. It secures valuable insights and expertise for solving problems in daily practice. Thus, the Knowledge Based Theory (KBT) has to be more than just a concept of information and information processing, as it was viewed in the past. Nickerson & Zenger (2004, p. 3) claimed that K has to be necessarily formatted, whereas profit gaining is possible only if the firm is capable of continually discovering new K or new solutions from the already existing K. Moreover, K is embedded in multiple entities including *organizational culture*, *corporate identity*, *the company's policies*, *routines*, and *employees* as primary carriers and creators of tacit K. Nelson & Winter (1982, pp. 63-64) defined *organizational K* as the “*input-output combinations achievable with all possible mixes and levels of activities known to the firm.*”

Anyway, according to the KBT of the firm, **knowledge** is regarded as the most strategically significant resource of the firm. The logic behind this assumption is that K is very unique, and socially complex (e.g. expertise in a certain field) and, thus, it is extremely difficult to imitate it. Consequently, heterogeneous K bases serve as the foundation for SCA and superior performance in the long term.

KBT was initially promoted by Penrose (1959) and later elaborated and empirically tested by other researchers. According to Einsenhardt & Santos (2000, p. 46), the KBT offers extremely useful theoretical insights into how to address the multi-level social processes through which K is sourced, transferred and integrated inside and outside the firm. Besides, K has the ability to create value both internally and externally. And although the KBV is *not* fully developed for mapping out strategy or “a theory of the firm in any formal sense,” it is capable of providing theory-building and managerial practice to secure a pluralistic understanding of K and views organizations as complex adaptive systems (Grant, 2002, p. 135; Alavi & Leidner, 2001, p. 107).

The foundations of the KBT are grounded upon **knowledge transferability** (especially critical for internal purposes), **capacity of aggregation** (ease of transferability depends upon the potential for aggregation; enhanced through common language and IT), **appropriability** (tacit and explicit K), **specialization in K acquisition**, **K requirements of production** (K is the primary input of production).

Krogh (cited by Scharmer, 1999, pp. 2-3) claimed that over the past few decades KM passed through three main stages:

1. During **Stage 1**, K was simply located and captured through *technical systems*. At the initial stage of KM, firms had to find the right people to make the process work. This, in turn, implicated the ability to identify key HC, transform it into structured capital, keep the right documentation, analyze data, etc. Market leaders of Stage 1 can be characterized through building K bases primarily using business information systems via collecting and analyzing information about competitors, new scientific trends, business development, etc.

2. **Stage 2** deals primarily with *transferring and sharing K* captured internally or in the organization. Ng (2002, p. 2) stated that the biggest challenge hereby, to achieve a CA, lies in the effective transfer of K. Krogh (cited by Scharmer, 1999, p. 3) claims that in order to share K, it is imperative to establish infrastructure and trust between all stakeholders and partners. The primary issue resultant from Stage 2 is related to the identification of the basic *factors that motivate staff* in order to secure that K is shared willingly and on a daily basis as well as to find effective and novel ways of building strong relationships to enable effective K sharing among respective stakeholders (Scharmer, 1999, p. 2).

Unfortunately, most companies speak of negative experiences associated with K sharing. According to Nickerson & Zenger (2004, pp. 12-13), the two impediments of K sharing are: a) people are cognitively inhibited in the *tempo with which they can learn* or are susceptible to new information (e.g. different people accumulate and apply K differently), and b) employees tend to *self-interest*, which may lead to opportunistic behavior and opportunistic K sharing patterns. Therefore, on the one hand, K transfer may implicate not only transfer of best practices, expertise, and insights among employees, but also unleashing creativity and innovation to secure constant growth and sustainability. On the other hand, K sharing might also lead to the leakage of valuable firm-specific tacit K (especially KH or CA), thus, leading to losses of a unique competitive position (Liebeskind, 1996, p. 93).

3. **Stage 3**, according to Professor Krogh (cited by Scharmer, 1999, p. 4) is characteristic of firms which survived the first two stages. At this level, new K is created. This is primarily done through focusing on business processes, thus, underscoring the relevance of a shift from the merely IT-based solutions of Stage 1 (e.g. large-scale intra- and inter-firm KM) to organizational structures (Stage 2) up to creating new values (Stage 3). Consequently, simply being knowledgeable does not suffice any more: firms need to be K-creating (Nonaka & Takeuchi, 1995). Moreover, in view of complexity of the third stage, it is rather future-oriented and aims, in the first line, at proactive thinkers (e.g. *Nokia*). K-creating corporations envisage which K they would need in future and, therefore, keep experimenting with new methods and test new solutions.

On the other hand, the KBV is not a flawless theory. Krogh (cited by Scharmer, 1999, pp. 4-5) identified some primary issues related to it. First and foremost, the KBV has to go beyond the concept of information and information processing prevalent some decades ago to secure advancement onto higher levels of KM, thus, leading to enhanced productivity and progress. Moreover, in view of KM complexity and its social context, speed, accuracy, and diligence as the primary peculiarities of the K-based economy of tomorrow (and as opposed to the Industrial Age of the past) have to be paid special attention. Besides, today high mobility and low loyalty of HC which are characteristic of modern organizational structures place additional challenges for companies creating new tasks, manageable only for more knowledgeable workers and based on ongoing K generation and creativity. In addition, shared leadership based on voluntary cooperation and voluntary giving coupled with care and support ought to create a climate more conducive to K sharing. Yet, for the time being, most K sharing experiences are still rather negative. Sometimes, even years pass until positive changes *do* emerge (Scharmer, 1999, pp. 4-5).

Moreover, according to Scharmer (2000, p. 2), tacit K, as opposed to Nonaka & Takeuchi's classification of K (1995), is subdivided further into *tacit-embodied K* and *tacit not-yet-embodied K*. The latter is also referred to as *self-transcending K* and requires a different type of K environment and learning infrastructure. Consequently, in order to compete on markets with increasing returns (as opposed to markets with constant or decreasing returns), market leaders have to find the type of K that will allow them to sense, tune into and actualize emerging opportunities. Hence, the true challenge is to develop the capacity for "*precognition*" or ability to sense emerging potentials (or coming-into-being of the new which is conventionally associated with **artists**, *not business managers*) to secure the firm's long-term CA and organic growth (Scharmer, 2000, p. 3).

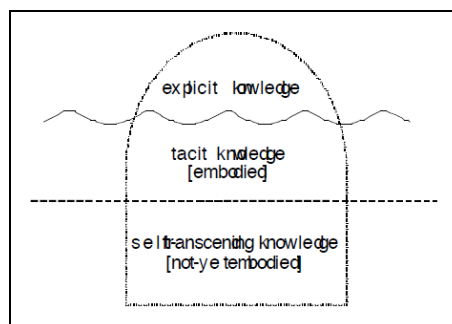


Figure 10: Three Forms of Knowledge (Source: Scharmer, 2000, p. 6)

3.2. Organizational Capability / Capacity Theory

The Capability Theory (CT) was born thanks to G.B. Richardson, who, in turn, was influenced by Edith Penrose (1959, cited by Garzarelli, 2006, p. 3). In the context of CT, **capabilities** are defined as specific or not easily transferable production K.

According to Richardson (1959, cited by Garzarelli, 2006, p. 5), firms may share some capabilities of production, but they do not necessarily share coordinative capabilities for the production process. E.g. the production of electronics for cars shares similar capabilities with the production of electronics for laptop computers. Yet, the coordination of the above mentioned processes of production are normally *not* shared, as the two processes belong to different types of production processes, thus, defining the boundary between the firm and market or other firms.

The two basic problems faced by organizations, according to the CT, are ***the search cost problem*** (search of capabilities dispersed throughout the larger economic systems to organize them in a most productive way) and the ***coordination cost problem*** (to match capabilities to stages of production (both internally and externally) and to secure economies of specialization) (Garzarelli, 2006, pp. 10, 13, 14). Thus, the benefits of specialization are never obtained at zero cost and always entail coordination costs due to differences in capabilities.

Generally speaking, the organizational theory studies how organizations are structured. The pursuit of self-interest and power are the basic characteristics of firms. The sources of power are authority, expertise, control of resources, control of processes, control of decision-making, and, assuredly, information and K. According to Follett (1998, p. 113), lack of training is related to the inability of cooperative thinking and action. Thus, *the key factor to organizational success is in getting people to coordinate in accomplishing the organization's purpose* (Barnard, 1938). Hence, it is imperative to motivate employees to join the community and then to have them contribute willingly.

Logically, the identification of the motives and inducements that satisfy different employees are of paramount importance to secure long-term success of a firm. The primary incentives may include ***material incentives*** (money, compensation, bonuses), ***personal incentives*** (prestige, distinction, power), ***values*** (pride of workmanship, altruistic service, loyalty, patriotism), ***associational incentives*** (social compatibility and social status), ***opportunities*** (participation, efficacy), ***security incentives*** (job security, support) (Balachandran, 2009, pp. 251-252). These are, by the way, in resonance with Maslow's Hierarchy of Needs (Smoke, 2010, pp. 138-139).

Aulakh & Kotabe (1997) and Madhok (1998, pp. 260-261) introduced the organizational capacity (OC) theory (OCT) which is based on the organization theory (OT) (Zhao & Decker, 2004, p. 3). This model, or rather theory, views firms as a collection of capabilities and K where **individual skills, organization, and technology** are regarded as inextricably interwoven components (Nelson & Winter, 1982, cited by Madhok, 1998, p. 266). In particular, the evolutionary theory of organizational capabilities and behaviors by Nelson & Winter (1982, p. 58) underscores the relevance of **motivation** by *profit maximization*. In addition, OC are evolutionary, or intrinsically dynamic, thus, providing the source of continuing growth. Particular attention is also be paid to *uncertainty, bounded rationality, institutional complexity, and the dynamics of the adjustment process*, where *imperfect information* and *imperfect competition* coupled with *transaction costs, increasing returns, and historical change* are interconnected (Nelson & Winter, 1982).

According to Nelson & Winter (1982, p. 16), **routines**, as part of OC, are characteristic of all regular and predictable behavioral patterns of firms whose function may be compared to the role of genes in biological evolutionary theory. Routines determine the firm's possible behavior and serve as a persistent feature of the organizational organism. Regularities of individual behavior, on the other hand, that have expected consequences at the organizational level (Dosi, Nelson & Winter, 2000) are the analogue of organizational routines and provide understanding of how routinization secures organizational functioning based on skills of individual functioning (Nelson & Winter, 1982, p. 73). Moreover, according to numerous researchers (Polanyi, 1962, p. 49; Nelson & Winter, 1982; Schein, 2004), **skills** are (1) **programmatic** (most steps and details are executed without conscious volition), (2) **the K** underlying a skillful performance is, in large, **tacit** in nature, thus, it is difficult or impossible to articulate all the relevant details; (3) **the exercise of a skill involves making choices**, yet, in most cases, options are selected automatically.

Consequently, in view of the aforementioned, organizations consisting of numerous members who perform many distinct roles and make complementary contributions to production, face a substantial **coordination** problem. Hence, it is imperative to study the relationships between organizational learning (OL), social capital (SC), the effectiveness of K transfer coupled with perceived organizational performance. The integration of OL capacity with SC networks lead to the holistic K sharing approach and management enterprise framework as significant strategies to secure organizational success (Rhodes et al., 2008, p. 245).

Moreover, firm resources (physical capital, HC, and organizational capital resources) can be a source of SCA only when they are valuable or when they can exploit opportunities or neutralize threats in a firm's environment. One firm resource that is required in the implementation of almost all strategies is **managerial talent**. Moreover, according to the RBT, the bundle of firm resources should necessarily be *rare*. If these resources are *not imperfectly imitable*, then it is assuredly a source of sustained CA (Barney, 1991, p. 106). E.g. computers or machines in general that can be easily purchased across markets are just part of the physical technology of a firm. K and information (or intangible assets) that reside in human minds and are deeply embedded in a firm's formal and informal decision-making, on the other hand, may hold the potential of SCA (Barney, 1991, p. 114). Brand names and reputation which are dependent upon historical difficult-to-duplicate settings or informal social relations between firms and key stakeholders (or socially complex structures, thus, imperfectly imitable components) can also be a source of SCA (Barney, 1991, p. 115).

On the other hand, **routines** have to be understood as:

a) organizational memory, whereas the routinization of activity constitutes the most important form of storage of the organization's specific operational K. Moreover, *organizations basically remember by doing* (Nelson & Winter, 1982, p. 99). Hence, exercise of a routine serves as a key resource of economies and cause of persistent differences among firms and innovation (Schumpeter, 1934, pp. 65-66). On the other hand, an individual lacking skills appropriate for novel situations leads to poor routines or skills of the organization as a whole.

According to Sidney Winter (cited by Davenport & Prusak, 2000, p. xxii), firms are "*organizations that know how to do things*." Thus, it is not just a mere collection of people organized to produce goods and services, or both, but their ability to manage to produce depends upon what they know (in other words, the K embedded in the routines) and factors of production. Hence, material assets are of limited worth unless employees know how to use them. Consequently, "*knowing how to do things*" is critical for the firm's success. Moreover, **knowledge is the only unlimited resource that grows with its use** (Davenport & Prusak, 2000, p. xxii). So, not to capitalize on it contradicts all the principles of the economic theory.

Summarized, it should be pointed out that the only **sustainable CA** that the firm possesses reduces to **what** the firm collectively knows, **how efficiently** it uses what it knows, and how readily it acquires and uses **new knowledge** (Davenport & Prusak, 2000, p. xxiv).

According to Zander & Kogut (1995, cited by Mahoney, 2005, p. 201), the transfer of manufacturing capabilities is influenced by the degree to which capabilities may be codified

and taught to others. Therefore, the nature of dynamic capabilities and the nature of competitive positioning are critical issues in this context. Hence, **routines** are *institutionalized*, **networks** and **knowledge** are more *dynamic* components.

It goes without saying that **a product** or **an invention** (*idea, creation, etc.*) **is normally associated with just one person**, whereas the inventor seldom overtakes all the stages of product creation, normally only finding the clue to the right solution. As a matter of fact, there are thousands of registered cases when people did not manage to finalize their inventions. Therefore, **K**, **networks**, and **routines** are **very personal**. As a vivid example serves *Apple*, where Steve Wozniak and his technical genius helped the company produce computers engaging his visual experience of digital information. Steve Jobs, Wozniak's partner, emerged as a visionary leader and built strong network connections around his primary team. As a consequence, *iPod*, *iPhone*, and *iPad* products appeared (truly unique and inimitable products).

In the case of *Microsoft*, Paul Allen whose genius was bound to the command line interface could not commercialize his product because it was not quite understandable for non-programmers. Bill Gates, on the contrary, who understood the roots of the problem, used his huge business connections to introduce personal computing on the desktop, thus, radically changing the world of today.

b) routines as truce, since routine operation involves a comprehensive truce in intra-organizational conflict (Cyert & March, 1963, cited by Mahoney, 2005, p. 192). Adaptations involve a perceived threat to internal political stability, and thus, success;

c) routines as target: control, replication, and imitation: *Replication* is often a non-trivial exercise, since it requires complex skills with large tacit components, acquired over years of experience, not to mention of high costs related to it (Nelson & Winter, 1982, cited by Mahoney, 2005, p. 192; Polanyi, 1962, p. 52).

According to Leonard (1998, p. 19), the organization's CC are related to *employee K and skills, technical systems, managerial systems, and values and norms*. Besides, in order to take advantage of CC, it is imperative to mitigate core rigidities of the firm. Critical issues hereby involve proper management of such information attributes as *acquisition, evaluation, assimilation, integration, diffusion, deployment, and exploitation of K*. Such information management is a process and a routine where internal K is constantly developed and integrated into the functioning of the organization (Madhok, 1998, p. 266).

Zhao & Decker (2004, p. 9) maintained that the OCT postulates that the MEM decision, *the firm's boundary issue*, is a capability related issue and is made under the

calculus governed by considerations related to the deployment and development of the firm's capabilities. This, in turn, implicates, that the OT is necessarily taken into account when the MEM choice is made. The theory is still not perfectly developed and there are several restrictions to it. Yet, on the other hand, this theory is supported strongly by numerous empirical studies and the evidence of efficiency and effectiveness in the development, acquisition, and deployment of organizational capabilities in practice (Teece, Pisano & Shuen, 1997, cited by Mahoney, 2005, p. 203).

According to Nonaka & Takeuchi (1995, p. 48), most MNCs face a corporatwide problem related to the dominance of a specific strategic business unit (SBU). Thus, it is imperative to overcome it by developing organizational skills through moving competencies from one SBU to the others (via training - both adaptive and generating). Moreover, CA should be found in the resources and skills "*inside*" the company, as opposed to the market environment or "outside" the firm, as argued by Porter's structural approach.

According to Aulakh & Kotabe (1997) and Madhok (1998, p. 261), the EM decision, from the perspective of the OC, depends upon the deployment and development of the firm's capacity. Zhao & Decker (2004, p. 9), on the contrary, argued that the assumption that the capacity of an individual firm is limited to ownership is *not* valid when the firm's efficiency-related decisions are significantly influenced by collaborative agreements. This, in turn, might significantly modify its overall capacity. The main conclusion, therefore, consists in the fact that strategy formulation depends not only upon the organization's *capacity*, but also on the organizational *efficiency*. This, in turn, necessitates the relevance of developing measures for evaluating organizational efficiency (Zhao & Decker, 2004, p. 9). The impacts that have to be considered, according to the OCT, are, thus, related to ***decision-making, sociological and political factors***. Hence, organizational capabilities serve as basic determinants which are developed through *experience* (the source of CA) and help the firms to compete both nationally and internationally (Madhok, 1998, p. 266).

Furthermore, the OCT maintains that firms compete for a CA, and to gain it, they have to learn from each other. Therefore, ***collaboration*** is one of the most efficient ways of improving competitiveness. Madhok (1998, p. 266) claimed, that, from the OC perspective, the personality and sample of the firm's experience and information management abilities (the two being interrelated), are critical for understanding the firm's international activities.

Chandler (1990, p. 172) stated that in order to develop OC or CC, firms have to make the following inter-related investments for achieving organizational capabilities: ***(1) investments in production facilities*** large enough to utilize the potential economies of the

technology (ES and ESC); (2) *investments in product-specific marketing, distribution, and purchasing networks*, and (3) *investments in managerial recruitment and training* to plan, coordinate, and monitor the firm's dispersed operations. OC, in turn, provide an internal dynamic for the continuing growth of the firm. In particular, OC stimulate their owners and managers to expand into more distant markets both in their own country and overseas. In addition, they also encourage the company to diversify through developing products competitive in markets other than the original one, thus, turning it into a multi-product enterprise (Chandler, 1990, p. 177).

Furthermore, since change is the only constant today, organizations have to learn to adapt and be flexible. In particular, in order to build a culture in which effort and experience coupled with cooperation, openness, lifelong learning lead to constant improvements, it is imperative to eradicate the *fixed mindset* that creates internal competition, defensiveness, and constant judgment. *A growth mindset*, on the contrary, encourages growth and constant improvements and leads to numerous benefits both for individuals and the organization as a whole (Sims & Nelson, 2011, p. 35). Therefore, the role of leaders to secure CA is crucial. Leaders create *culture* and manage it on a daily basis directing employees in the direction chosen. They are like *artists* who envisage future trends and help others get there too (Scharmer, 2000, p. 3).

Moreover, according to Edgar Schein, the researcher of organizational culture (2004, p. 17), the cultural paradigm is acquired due to *external adaptation* and *internal integration* and is thus most difficult to change as opposed to other organizational attributes as products, leadership, etc. *External adaptation* helps firms to survive and grow. Therefore, valuable cultures hold potential for the generation of CA and sustainability. *Internal integration*, on the contrary, is acquired through daily socialization and secures the formation of the required social structures which enable everyday functionality, thus, reinforcing cultural values and beliefs. Hence, *communication* plays primary role in securing organizational success and fostering cooperation, voluntary K sharing, support, and trust (Schein, 2004, p. 27).

According to Schein (2004, pp. 12-13), the cultural paradigm encompasses primarily *myths* (or explanations that maintain group cohesion anchoring the present in the past), *rituals and ceremonies* (performance appraisals, award ceremonies, committee meetings, management training programs), etc. Even the firm's products as artifacts are its physical or tangible manifestation of corporate culture.

As far as MEM are concerned, the compatibility between the requirements for a particular operation and the existing K base is a primary factor in the firm's strategic

evaluation of a specific EM (Johanson & Vahlne, 1977, and Tallman, 1991, cited by Madhok, 1998, p. 266). The main issue hereby is the cost of development and deployment of requisite capabilities within the firm because the choice of the EM is influenced by the costs related to K replication within the firm resultant from a specific market transaction (Kogut, 1992, p. 22). But if the existing routines of K replication can be used, implementation costs may be significantly reduced (Galbraith & Kay, 1986, cited by Madhok, 1998, p. 266). On the other hand, if a firm possesses a strong K base and required routines, then internalization will be preferred because it increases efficiency of resource use and effectiveness of K transfer within the organization (Madhok, 1998, p. 266). In addition, companies can also consider less costly and more effective alternatives to supplement their resources, grab new K from competitors and integrate it into the firm's K base (Huber, 1991, cited by Madhok, 1998, p. 266).

Summarized, from the OC point of view, **K resources** are the main issue; **collaboration** within the company involves restructuring of the firm's information boundaries; **management** and **coordination** of collaborative relationships are frequently reduced to management of K flows (Badaracco, 1991, cited by Madhok, 1998, p. 267). Due to this acknowledgment, ME by WOS results in the perpetuation of similar routines (Madhok, 1998, p. 267); licensing is not really adequate because of subtle aspects of KH; IJV are more attractive for enhancing the firm's capabilities in the core business because the development of all the necessary KH in-house is viewed as too slow, thus, unproductive (Madhok, 1998, p. 267). Therefore, JVs provide a greater degree of K interchange.

Licensing as a MEM will be preferred when there is limited experience in international operations, since experience builds up confidence. Hence, the greater confidence in the firm's abilities and possibilities to manage all the issues on its own, the faster it will decide for a WOS as a preferable MEM.

Consequently, the company's K base is the evolutionary outcome of the OC pattern and nature of the firm's experiences where the acquired set of experiences manifests itself in organizational routines, or the blueprint for the firm's actions; it becomes the medium through which the firm's behavior can be understood to external stakeholders (Madhok, 1998, p. 267).

3.3. Resource Based Theory

A vast majority of empirical literature points out that the availability or access to similar resources does not guarantee similar results or outcomes. In fact, in view of the liberalization of world trade and increased globalization, most firms today have similar opportunities. Yet, still very few compete globally, whereas others cannot even compete on a regional level. Therefore, varying performance is resultant from the heterogeneity of assets (Lopez, 2005, p. 662). In other words, certain **resources** coupled with certain **capabilities** and **established business relationships** secure a competitive position and CA.

Generally speaking, the RBV serves as the theoretical starting point in strategic management. In classical military roots, **strategy** stands for complex decision making to outperform competition. Yet, in the last decades, strategic management turned more into a “*scientific discipline*” and a field of research and managerial practices. In the 1980s, a *synthesis* in the RBV of the firm emerged (Peteraf, 1993, cited by Eikelenboom, 2005, p. 14). On the one hand, as opposed to Porter’s Five Forces (1980), the resource-based logic switched the focus from the “*outside*” to the “*inside*” of companies. As a consequence, the internal organization coupled with the firm’s *valuable, rare and costly to imitate resources and capabilities* were seen as a source of CA (Stacey, 2003, and Barney & Hesterly, 1999, cited by Eikelenboom, 2005, p. 14). On the other hand, since internal capabilities are connected to the external environment (competition, demand, globalization, lead users, Open Innovation, etc.), the RBV is often referred to as **an inside-out approach**. Therefore, the RBV is regarded as an influential theoretical view for comprehending how CA is achieved and how it could be sustained in the long run (Eikelenboom, 2005, p. 15; Schein, 2004, 17).

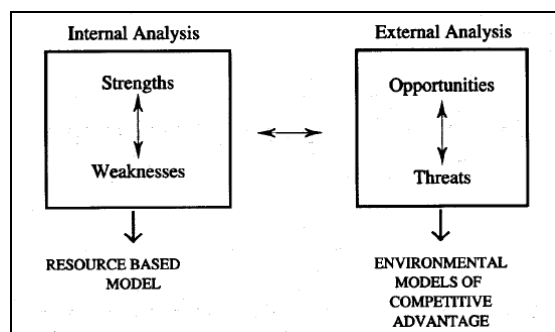


Figure 11: The Relationship between SWOT, Resource Based Model and Environmental Models of Competitive Advantage (Source: Barney, 1991, p. 100)

Generally speaking, the Resource Based Theory (RBT) postulates that **firm-specific resources** and **capabilities** are crucial determinants of the firm’s performance and, thus, economic rent (Amit & Schoemaker, 1993, p. 33). According to the creator of the RBT, Jay Barney (1991, p. 117), the two assumptions of the RBT are: **(1) resources are spread**

heterogeneously across firms; (2) resources cannot be transferred from firm to firm without costs. Thus, the bundle of valuable **resources** and **capabilities** are the source of the firm's CA (Eisenhardt & Martin, 2000, pp. 1-2; Wernerfelt, 1984, p. 172). The major challenge for managers consists hereby in the identification, development, protection, and deployment of these *heterogeneous* and *not perfectly mobile* resources and capabilities in such a way that they provide the company with a sustained CA, thus, securing a superior ROI in the long run (in other words, a CA is independent of the time frame and unsusceptible to imitable actions of competitors) (Amit & Schoemaker, 1993, p. 33; Peteraf, 1993, p. 180; Barney, 1991, p. 117; Rumelt, 1984, p. 562).

Uncertainty, complexity, and intra-organizational conflicts, on the contrary, highlight the firm's limitations to developing an appropriate RBT strategy, since decision making takes place *ex ante* (Amit & Schoemaker, 1993, pp. 33-34). Moreover, *Key Success Factors (KSF)* should not be easily accessible, since otherwise they cease to be KSF. Therefore, the company's unique resources have to fulfill the following criteria to secure a CA: (1) **valuable** (*value creation outperforming competitors or reducing own weaknesses*), (2) **rare** (*to secure above average returns*), (3) **imperfectly in-imitable** (*not easily duplicable, whereas the source of inimitability of CA should be unknown to competitors (causal ambiguity)*), (4) **non-substitutable** (*substitutable products will drive prices down leading to discounted future rents*) (the so-called **VRIN** characteristics) (Barney, 1986, pp. 1231-1241; Dierickx and Cool, 1989, p. 1506).

In other words, when value is created, the company automatically improves its organizational performance both in terms of *effectiveness* and *efficiency* (e.g. *Apple*). Resources owned must be *exclusive* in order to achieve a SCA (e.g. *Google*). Resources should not be easily reproduced or copied by competitors (e.g. *Apple's* proprietary software *iOS5* is only available to use with *Apple's* products). Resources must not be strategically equivalent resources that are not valuable or rare (e.g. patents).

Just as mentioned above, as opposed to Porter's strategic development process which looks at the relative position of a firm in a specific industry, the RBT can be regarded as an "inside-out" process of strategy formulation, since, in the first line, the firm looks at the resources it possesses. Subsequently, it assesses the potential for value generation and later on develops a strategy to capture the maximum of value and sustain it in the long run (Grant, 1991, p. 1).

Moreover, **causal ambiguity** is one of the basic factors of inimitability, in particular, if the resource for CA is either **knowledge-based** (*tacit in nature*) or **socially complex**

(difficult or even impossible to duplicate). Thus, knowledge-based resources can be defined as “*the essence of the resource based perspective*” (Conner & Prahalad, 1996, p. 477). In addition, resources might be imperfectly inimitable due to historical events (e.g. Nike was founded by two world-known athletes). As a result, such resources will lead to strengthening of the CA and will be impossible to replicate through *acquisition* or *imitation*. Summarized, in order to remain competitive in the long term, the firm’s **strategic assets** are to be **not easily bought, sold, imitated, or substituted** (Amit & Schoemaker, 1993, p. 38).

From the RBV, **resources** are defined as “*stocks of available factors that are owned or controlled by the firm*” (Amit & Schoemaker, 1993, p. 35). They can also be referred to as “*inputs*” into the production process (Black & Boal, 1998, p. 131). To convert (externally available and transferrable) resources into final products, a wide range of other assets and mechanisms are applied (e.g. technology, incentive systems, trust, etc.).

According to Amit & Schoemaker (1993, p. 35), **firm-specific resources** encompass:

- **technological KH** (patents, licenses, trademarks; processes, systems and software);
- **financial assets** (cash/assets on hand; the ability to easily raise capital; relationships with banks and other sources of cash, etc.);
- **physical assets** (natural resources, location, land, property, etc.);
- **intellectual and human capital** (skills of employees; specialized K and training; attitude towards customers; entrepreneurial perception; networks and communities of practices, Open Innovation, etc.);
- **reputational assets** (public perception of the firm’s quality, fair treatment, role in community, etc.), and
- **organizational assets** (flat organizations encourage creativity and innovation; entrepreneurial culture; ability to make fast decisions; short implementation periods, etc.).

Capabilities, on the contrary, stand for **the firm’s capacity to deploy its resources** (Amit & Schoemaker, 1993, p. 35). They are information-based, tangible or intangible firm-specific processes developed over time that secure superior performance. Capabilities are regarded as the main source of CA. Prahalad (1993, p. 45) refer to the capabilities that are crucial for the organization’s CA as “*core competencies*” (e.g. collective learning). Complex organizational capabilities (**Competence = Technology x Governance Process x Collective Learning**) pose a huge barrier for other firms to enter the market, thus, these are much easier to sustain in the long term. On the other hand, economies of experience or learning curves may be less relevant in a more dynamic environment of today, since radical changes occur too

fast and the K of the past may prove totally obsolete (or rather an impediment to growth) (Prahalad, 1993, p. 45).

In addition, the experience of management, just as mentioned above, significantly effects productivity. When management attempts at the optimal usage of the available resources and fosters a truly “dynamic” interacting process, this, in turn, secures continuous growth.

Abstractly, capabilities may be interpreted as “*intermediate goods*” generated by the company to secure improved productivity of its resources as well as strategic flexibility and protection of the final product. Unlike resources, capabilities are based upon the development and exchange of information among the firm’s HR. Capabilities are often indicative of functional areas. As a vivid example serve highly reliable services, product innovations, or manufacturing flexibility (Amit & Schoemaker, 1993, p. 35). In addition, the social context of certain resource conditions marked by *tacitness* of K accumulated through learning by doing (skill-based resources), *complexity* of inter-related resources, as well as specificity of certain resources helps secure competitive barriers (Wernerfelt, 1986).

Routines, just as indicated above, are regular and predictable patterns of activity which encompass a sequence of coordinated actions by individuals (Nelson & Winter, 1982, p. 16). Routines result from the recurrent interaction (*learning*) between employees and other resources of the organization. Moreover, routines are marked by a high degree of *semi-automatism* or *tacit K* that shows the limits to which capabilities can be articulated (Grant, 1991, p. 2).

Yet, CA may erode over time for two main reasons: *depreciation* and *imitation* by rivals. Thus, it is indispensable to analyze the firm’s resources for: (1) *durability* (rate at which they become obsolete); (2) *transparency* (degree of imitability); (3) *transferability* (e.g. geographical immobility, imperfect information, firm-specific resources, immobile capabilities which make resources not easily acquirable); and (4) *replicability* (the more complex the routines, the more difficult it is for a rival to replicate them inside his organization). Moreover, resources must be appropriable (or be able to capture rents derived from business activities) (Grant, 1991, p. 2).

In view of the aforementioned, new entrants (except for technology-dependent industries where revolutionary innovations eliminate the advantages of early entrants) enjoy first mover advantages: (1) new entrants possess *technological KH* derived from “*learning*” or “*experience*” curves, where costs fall with cumulative output; success in *patents* or *R&D*, where advances in products or processes are related to R&D expenditures, thus, securing a

higher quality and higher level performance; **(2)** new entrants have *experience, capabilities* developed over time and *scarce assets* (controlling assets that already exist rather than those created through development of new technology), and **(3)** *buyer switching costs* and *brand loyalty* are rather high (later followers have to invest more resources to attract customers away from the first-mover firm) (Kim & Park, 2006, p. 45; Lieberman & Montgomery, 1987, pp. 2-8).

Summarized, *capabilities* include dynamic routines which secure the firm's improved efficiency; *resources*, on the other hand, encompass HR, K transfer, finance, and technology (Moingeon et al, 1998; Makadok, 2001, pp. 388-389; Corner & Prahalad, 1996, p. 477). In order to sustain a CA, resources have to be skillfully used through capabilities. The relevance of K as a strategic asset is, therefore, undisputable.

Moreover, it is of paramount importance to create barriers to imitation ("*isolating mechanisms*"), which are primarily characterized by *information asymmetries, corporate culture, managerial capabilities, and property rights* (Winter, 2003, p. 992). E.g. by creating an asymmetry (a skill, process or asset that competitors cannot easily duplicate at an affordable cost), companies can create a CA (e.g. *Walmart*). Nevertheless, the relevance of *managerial practices* (except for property rights) is critical in all of the aforementioned cases. On the other hand, according to Ma (2003, p. 76), SCA is, by definition, anti-competitive.

Generally speaking, research based on the RBT covers the following issues: strategic management, marketing, international business, entrepreneurship, HR management, finance, and accounting. The RBT sheds light onto how companies achieve CA and sustain it in the long run (Eisenhardt & Martin, 2000, p. 1). RBT explores strategic capabilities as a group of internal resources which are strategically important for the creation of a CA.

Furthermore, based on the premises of the RBT, the value of the firm's KH influences its collaboration preferences in international MEM (Madhok, 1998, p. 269). In order to maintain competitive internationally, firms enter foreign markets by locating their production close to their rivals, but using different resources and capabilities. The RBV supported by Lieberman & Montgomery (1998, p. 1113) underscores the relevance of resources (both tangible and intangible, including employees' skills) for the timing of entry.

Yet, on the other hand, static perspectives of the RBT and industrial organizational economic perspectives do not accommodate for evolutionary changes of network knowledge (Ng, 2002, p. 2). **Knowledge-based CA**, on the contrary, is the dynamic configuration of resource choices to the rapidly changing K in today's social networks (Ng, 2002, pp. 28-29). Consequently, it goes without saying that K will remain one of the most important resources

of firms still for generations to come. Yet, the future of KM is likely to shift more in the quality direction (both embedded in corporate culture and daily operating procedures) (Davenport & Prusak, 2000, p. xv).

The aforementioned analysis makes obvious to which extent *K*, *resources* and *capabilities* are interconnected within a firm, sometimes even causing market failures or impossibility to trade these units in perfect markets (Amit & Schoemaker, 1993, p. 44).

Based on the aforementioned factors, **a strategic asset** can be defined as *a set of difficult to trade and imitate, rare, appropriable and specialized resources, capabilities and K that secure the firm's CA* (Amit & Schoemaker, 1993, p. 37).

The three theories examined in the above chapters are summarized in the following Figure.

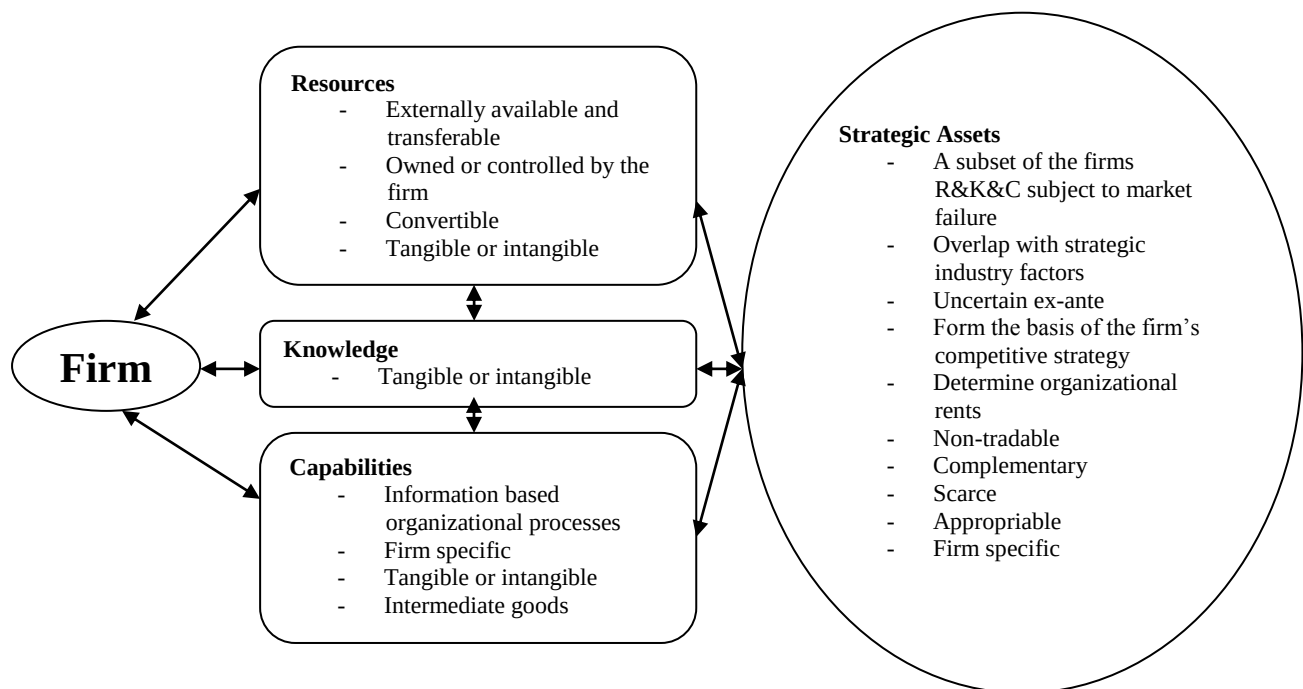


Figure 12: Strategic Assets of a Firm (Source: (Amit & Schoemaker, 1993, p. 38))

4. Knowledge

“Knowledge is power, but without the adequate management of that knowledge, the consequences for [organizations] could be devastating.”

Cameron (2000, p. 3)

Understanding sources of SCA is a primary issue for MNCs and a major area of research in strategic management. Just as mentioned above, strategic resources (both tangible and intangible) are heterogeneously distributed across firms and nations. These differences remain stable over time, whereas uncertainty and changes grow exponentially. This, in turn, underscores the relevance of understanding the links between the firm's resources and SCA as well as the potential of specific resources for generating SCA (Barney, 1991, p. 99). Knowledge overtook the first-rate role in this context.

Moreover, in the Information Age of today and in the transition phase towards to the K-based economy of tomorrow, it is knowledge (*not* capital, raw materials, land, or labor) that is the company's **key economic resource** and **source of wealth and sustainability**. In other words, K differs significantly from resources of the industrial economy of the past (Stewart, 1997).

Furthermore, according to Dorothy Leonard's Wellsprings of Knowledge (1995, p. xiii): *“Products are physical manifestations of knowledge, and their worth largely, if not entirely, depends on the value of the knowledge they embody.”* That implicates that all products and services are knowledge-intensive and that K has to be regarded as the primary strategic asset for each and every firm.

In addition, since K accumulates slowly over time and is not a static pool¹, but a wellspring, constantly replenished with new data, information, K, wisdom, ideas, insights, etc., accumulation of this ever-flowing source of corporate renewal and the development of the firm's core capabilities are inseparably linked to **constant** or **lifelong learning**. Hence, **“K is both raw material and finished goods in today's corporations”** (Leonard, 1995, p. 3).

Moreover, the ability and willingness to share with others was always considered a unique way to achieve human happiness (e.g. in old civilizations), K being the most valuable thing of all (Cağatay, 1989, p. 277).

Just as indicated above, effective use of K is imperative to secure economic growth, development and stability of nations (Dahlman & Utz, 2004, p. 10). According to the World Bank Institute, the Knowledge Economy Index (KEI) designed as an interactive tool for

¹ According to Cisco Visual Networking, the global mobile data traffic will increase 26-fold between 2010 and 2015 (Source: Cisco, 2011).

quantifying countries' ability to generate, adopt and disseminate K and for benchmarking in the K-based environment on a global scale underscores the relevance of economic stability for securing higher susceptibility to K and innovation (The World Bank, 2012).

Rank	Country (click on the name to see basic scorecard)	KEI	KI	Economic Incentive Regime	Innovation	Education	ICT
1	Sweden	9.43	9.38	9.58	9.74	8.92	9.49
2	+6 Finland	9.33	9.22	9.65	9.66	8.77	9.22
3	Denmark	9.16	9.00	9.63	9.49	8.63	8.88
4	-2 Netherlands	9.11	9.22	8.79	9.46	8.75	9.45
5	+2 Norway	9.11	8.99	9.47	9.01	9.43	8.53
6	+3 New Zealand	8.97	8.93	9.09	8.66	9.81	8.30
7	+3 Canada	8.92	8.72	9.52	9.32	8.61	8.23
8	+7 Germany	8.90	8.83	9.10	9.11	8.20	9.17
9	-3 Australia	8.88	8.98	8.56	8.92	9.71	8.32
10	-5 Switzerland	8.87	8.65	9.54	9.86	6.90	9.20
11	Ireland	8.86	8.73	9.26	9.11	8.87	8.21
12	-8 United States	8.77	8.89	8.41	9.46	8.70	8.51
13	+3 Taiwan, China	8.77	9.10	7.77	9.38	8.87	9.06
14	-2 United Kingdom	8.76	8.61	9.20	9.12	7.27	9.45
15	-1 Belgium	8.71	8.68	8.79	9.06	8.57	8.42
16	+3 Iceland	8.62	8.54	8.86	8.00	8.91	8.72
17	-4 Austria	8.61	8.39	9.26	8.87	7.33	8.97
18	+7 Hong Kong, China	8.52	8.17	9.57	9.10	6.38	9.04
19	+7 Estonia	8.40	8.26	8.81	7.75	8.60	8.44
20	+2 Luxembourg	8.37	8.01	9.45	8.94	5.61	9.47

Figure 13: KEI and KI Indexes (2012) (Source: The World Bank, 2012)

First and foremost, it should be pointed out in this context that **data, information, and knowledge** are *not* interchangeable concepts (Davenport & Prusak, 2000, p. 1). The clear distinction between these concepts and wisdom is reflected in the epistemological system called **Data, Information, Knowledge and Wisdom (DIKW) Pyramid** – one of the most fundamental and widely recognized models in KM (Firestone, 2001, p. 15).

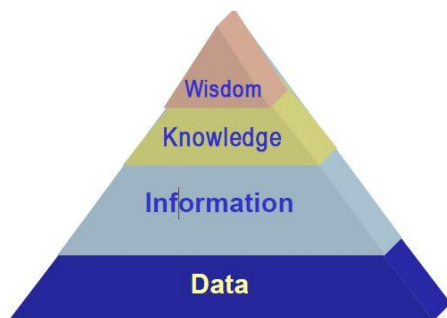


Figure 14: The Data, Information, Knowledge, and Wisdom Pyramid (Source: Firestone, 2001, p. 15)

According to Milan Zeleny, one of the initiators of the Knowledge Pyramid, its elements may be referred to as **"know-nothing, know-what, know-how and know-why"** (Zeleny, 1987, p. 59). **Data** (know-nothing) is *a set of discrete, objective facts about events*. It may be also described as structured records of transactions (Davenport & Prusak, 2000, p. 1). Data is stored in some sort of technology system and is entered into the system by different

departments: finance, accounting, marketing, etc. Quantitatively, firms evaluate data management in terms of *costs, speed, and capacity*. Qualitative measurements, on the contrary, are *timeliness, relevance, and clarity* (Davenport & Prusak, 2000, p. 1; Zeleny, 1987).

As a matter of fact, *all* organizations need data. But some industries are heavily dependent on it (e.g. banks, insurance companies which have to keep track of all their

transactions), whereas for other companies, quality data matters more, as *data has no inherent meaning* (offering no judgment or interpretation of what happened, thus, providing no sustainable basis of action). Consequently, data has little relevance or purpose, yet, it serves as the essential raw material for the creation of information (Davenport & Prusak, 2000, p. 1; Zeleny, 1987).

According to Peter Drucker, one of the most important personalities in KM (cited by Davenport & Prusak, 2000, p. 2), **information** (know-what) is “*data endowed with relevance and purpose.*” In other words, it is a message that has a sender and a receiver and which is intended to make a difference in the receiver’s outlook and/or insight. Information moves around organizations through *hard* (wires, addresses, electronic mail-boxes, satellite dishes, etc.) and *soft* networks (ad hoc: less formal and visible) (Davenport & Prusak, 2000, p. 3; Zeleny, 1987).

Quantitatively, information is measured by *connectivity* and *transactions*. Qualitatively, on the contrary, it is measured by *informativeness* and *usefulness* (new insights, contributions to decision-making or new solutions to problems, etc.). Therefore, information is marked by **value-adding**: answering the fundamental questions *who, what, where, when* and *how many*, data becomes contextualized, categorized, calculated, corrected, and condensed (Davenport & Prusak, 2000, p. 4).

There is a heated discussion all over the world as to the relevance of technology (computers, in particular) for adding value to data. Assuredly, computers *can* help to add value and transform data into information (through data categorization, calculation, and condensing), but they rarely manage to contextualize data. In other words, computers will *never* substitute humans in their role of K creators (Davenport & Prusak, 2000, pp. 4-5; Zeleny, 1987).

Knowledge (know-how) is a much broader, deeper, and richer term than data or information. K resides in humans and is part and parcel of human complexity and unpredictability. It derives from information as information derives from data. The transformation process involves comparison, consequences, connections, and conversation and is acquired exclusively through the process of **learning** (Davenport & Prusak, 2000, pp. 6-7; Ackoff, 1989, p. 3).

There is no accepted definition of K: epistemologists spend their lives trying to understand what it means to know something. But the working **definition** of K offered hereby runs as follows: “*Knowledge is a fluid mix of framed experience, values, contextual information, and expert insight that provides a framework for evaluating and incorporating*

new experiences and information” (Davenport & Prusak, 2000, p. 6). It originates in the minds of knowers. In organizations, it is embedded not only in documents or repositories but also in organizational routines, processes, and norms. Thus, K-creating activities take place only within and among humans. K, as a result, can be traced both as **process** and **stock** (Davenport & Prusak, 2000, p. 6; Firestone, 2001).

K is valuable because it is closer (than data or information) to **action** and **practice**. In business environment, it provides insights into measurable efficiencies in product development, and production. It may also be used to make wiser decisions about strategy, competitors, customers, distribution channels, and product life cycles (Davenport & Prusak, 2000, p. 6). Yet, the mere accumulation of K may soon lead to its transformation into data. Therefore, it is imperative to manage to reduce K to very few useful things only.

According to Ackoff (1989, p. 7), **wisdom** (knowing why), the highest level of the DIKW Pyramid, is characterized by the ability of humans to evaluate choices and decisions or the evaluated understanding. Wisdom is also influenced by moral and ethical codes and secures understanding where there was no previous understanding, thus, reaching far beyond understanding itself, so to say. In fact, wisdom is very subtle and therefore extremely difficult to acquire, even over time. Moreover, according to Ackoff, it is regarded as a uniquely *human* state, since only humans have a soul. Therefore, wisdom can never be substituted by computers (even in future) (Ackoff, 1989).

Summarized, the first three categories are based on past experiences and K already known, thus, pertaining to the present and the past. Wisdom, on the other hand, looks into the future and incorporates vision and design (Ackoff, 1989, p. 9).

In view of K complexity and its ambiguity, it is indispensable to further spilt it into key components and analyze each of them in detail to better understand its subtleties and creation process.

4.1. Classification

Today, “[we] are entering the knowledge society in which the basic source is no longer capital, or natural resources, or labor, but is and will be knowledge, and where knowledge workers will play a central role” (Skyrme, 1999, p. 11). As a consequence, interest in K (primarily, tacit K) which is regarded as the primary source of wealth is increasing tremendously (Johannessen et al., 2001, pp. 3-4). Therefore, maximization of the organization’s intangible assets and the subsequent capitalization on them are the primary tasks of KM.

Moreover, according to Dr. J. K. Mishra (2009, p. 50), most of the K found in organizations is tacit (about 80%), i.e., it resides in individuals’ minds and is thus very difficult to “extract” or codify. And only about 15-20% of valuable K is explicit: i.e. can be found in books, databases, recordings, graphs or other images.

Generally speaking, there exist various classifications of K and KM. KM can be approached either through the **technological** or **hierarchical method** (primary focus on ICT and well-articulated processes) or **unassisted** or “**knowledge ecology**” **approach** (Bergeron, 2003, p. 111; Firestone, 2001, p. 23). The aforementioned approaches differ, first and foremost, in the *type of K involved, initial investment cost, scalability and volume of transactions, ideal organization type*, etc. (Handzic, 2004, p. 222).

If the issues to be dealt with are too subtle and require very specific K, then an organic approach and a K worker are a much more suitable solution as compared to a computer database. In addition, a technological approach is most appropriate for larger organizations (training is required to secure effective use of enormous databases), whereas an organic method of managing intellectual capital (or improvement enabled by ongoing social interaction) is more feasible in smaller firms (Bergeron, 2003, pp. 111-113). By the way, the organic approach is most indicative of *communities of practice* which secure constant sharing of K and experience and cooperation on a global scale (Firestone, 2001, p. 23).

Yet, according to numerous researchers, KM is marked by a very little dependence upon high tech solutions (Bergeron, 2003, pp. 111-113). In the past, it was technology that was regarded as the primary impediment to successful implementation of KM in practice. Nowadays, it is 90% attributable to organizational culture or culture change and only 10% - to technology (CHIPS Magazine, 2001). Other researchers provide other figures. Yet, in principle, they *all* agree to the following: **technologies** of today are the least impediment to implementing KM (or may be compared to the green light according to the street light analogy), **leadership** as the yellow light and **culture change** is viewed as the biggest

impediment to the successful implementation of KM projects (or the red light) (Asoh, Belardo & Neilson, 2007, p. 9).

In view of the aforementioned, it is much more reasonable to combine the two competing KM strategies (technological and organic approach to KM) into an integrated approach and synthesize KM as a complex multidimensional concept marked by a combination of dynamic (r)evolutionary technological solutions (a catalyst for facilitating K generation and transfer even real-time and on a global scale) and the natural flow of K generation secured by social interaction (creation of a climate conducive to K generation and sharing: leadership and culture change) (Handzic, 2004).

Just as indicated above, ***K is the precursor to any further decision***. Therefore, it has to be classified and properly studied.

Apart from the above mentioned approaches to managing K, KM can also be characterized by a diversified number of KM strategies. The main difference between them consists in the KM aspect that is primarily focused on. Therefore, some KM strategies concentrate on ***knowledge***, whereas other strategies are directed at ***business processes***, still others target at ***end results***.

Classification by Knowledge

KM practitioners underscore the importance of combining ***K accessibility*** with ***K transformation***, which are, first and foremost, indicative of constant adaptation and changes of the K creation process secured by learning. This perspective serves as the foundation of ***the “Knowledge Spiral” by Nonaka and Takeuchi*** (1995) and ***the “Information Space” (“I-Space”) Model by Boisot*** (1998). *Innovation* and *learning* are the primary outcomes secured by constant flow and transformation of intellectual assets.

The “**Knowledge Matrix**” is one of the most accepted approaches to classifying KM strategies today. According to it, K is divided into ***tacit*** (or individual) and ***explicit*** (or collective). Their “**Knowledge Spiral**” is marked by the spiralling K process interaction, which, in turn, undergoes the following stages: **Socialization, Externalization, Combination and Internalization (SECI Mode), thus securing ongoing new K creation and innovation. Hence, to render implicit K into explicit, tacit K has to be “extracted” from an individual’s mind and, vice versa, in order to make explicit K more implicit, K should be “re-internalized” (Nonaka & Takeuchi, 1995, p. 70; Mascitelli, 2000, pp. 179-183).**

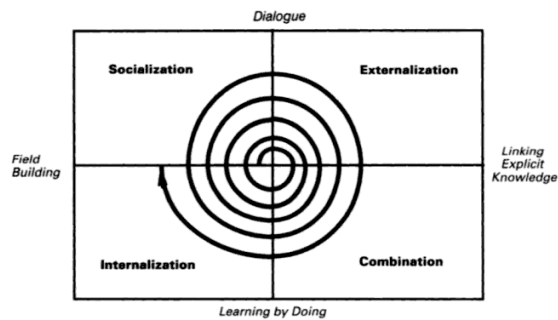


Figure 15: Knowledge Spiral

(Source: Nonaka & Takeuchi, 1995, p. 71)

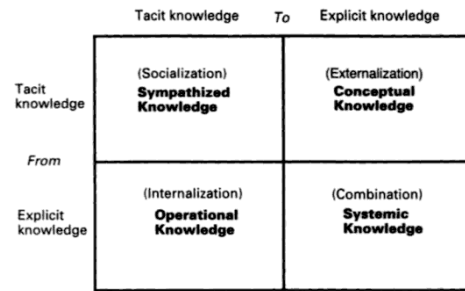
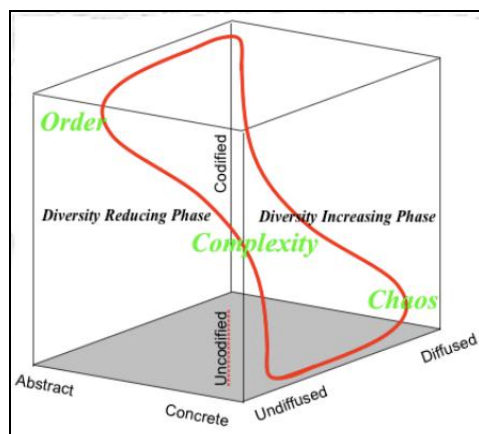


Figure 16: Contents of Knowledge Created by the Four Modes

(Source: Nonaka & Takeuchi, 1995, p. 72)

The K creation cycle commences with **Socialization (Phase 1)** marked by interaction, information communication, and sharing of experiences and mental models (**Tacit to Tacit, or field building**). **Phase 2 or Externalization** is indicative of using metaphors or analogies to articulate hidden tacit K, which is otherwise almost impossible to articulate (**Tacit to Explicit, or dialogue / collective reflection**). **Phase 3 or Combination** is characterized by “networking” or combining the newly created explicit K with the already existing explicit K available in other SBUs of the organization, thus, crystallizing it into a new product or service (**Explicit to Explicit, or linking explicit K**). **Phase 4 or Internalization** implicates that explicit ideas turn anew into “Know How” due to practicing and repetition (or internalization) (**Explicit to Tacit, or learning by doing**). Then, K reverts to socialization and the K spiral re-iterates the generation of K again (Nonaka & Takeuchi, 1995, pp. 70-71).

Boisot’s I-Space Model is often referred to as the model of K asset development. In this sense, it resembles significantly Nonaka & Takeuchi’s Matrix of Knowledge Types. Yet, as opposed to its counterpart, Boisot’s I-Space Model acquired an additional dimension (**abstraction** or *K generalization to various life situations*). This, in turns, secures a much more detailed analysis of the K generation and transfer cycle (Snowden, 2010; Boisot, MacMillan & Han, 2007, p. 137; Haggie & Kingston, 2003).



Generally speaking, the Information-Space Cube by Boisot locates K within a 3 dimensional cube. The three axes are: (1) from “un-codified” to “codified”, (2) from “concrete” to “abstract,” and (3) from “un-diffused” to “diffused” (Dalkir, 2005, p. 66). In addition, the Model is also characterized by a “**Social Learning Cycle**” (SLC) which, coupled with the aforementioned I-Space Cube is

Figure 17: Boisot's Information-Space Model (Source: Snowden, 2010)

used to simulate the dynamic flow of K assets. The K creation process undergoes, according to Boisot, the following sequence of stages: **(1) scanning** (*scanning of insights in the generally available but often fuzzy content*), **(2) abstraction** (*generalization of the newly codified insights to numerous situations*), **(3) diffusion** (*the newly acquired “abstract” K is shared with others*), **(4) absorption** (*application of the newly codified K to real-life situations causing new “learning-by-doing” experiences or new tacit K*), and **(5) impacting** (*abstract K is embedded in rules and behaviour patterns*) (Boisot et al., 2007, p. 68; Haggie & Kingston, 2003).

Boisot compares the K creation cycle with the laws of thermodynamics underscoring the dynamic nature of intellectual capital. Thus, according to his Model, K is characterized by the two opposite extremes: *the “most ordered” K* (*highly abstract, highly codified and undiffused*) or the lowest rate of entropy generation and the maximum potential for the useful value-adding versus *the “least ordered” K* (*least abstract, least codified and most diffused*) or the highest level of entropy production and the least potential for adding useful value. Hence, an organization targeting at increasing or sustaining its CA should be constantly in search of moving its intangible assets to the maximum value adding area. Nevertheless, the dynamic nature of the SLC implicates, on the other hand, that K is never constantly located at some distinct point (or the extreme maximum productivity point) due to the incessant cyclicity of K generation secured by its continuous usage and innovation or new learning experiences and new insights (Boisot et al., 2007, pp. 26-31; Mishra, 2009, p. 70).

Classification by Business Processes

According to Karl Wiig (1997) and the American Productivity and Quality Center (APQC), KM strategies are classified into six basic categories (Wiig, 1997, pp. 1-2; WIIG Model, 2011; Haggie & Kingston, 2003):

- (1) Knowledge Strategy as Business Strategy** (*K is viewed as a product*);
- (2) Intellectual Asset Management Strategy** (*aims at exploiting and improving the already available K assets*);
- (3) Personal Knowledge Asset Responsibility Strategy** (*aims at fostering K development and K sharing only in some individual employees*);
- (4) Knowledge Creation Strategy** (*focuses on innovation and new K creation based on R&D*);

(5) Knowledge Transfer Strategy (focuses on sharing best practices to secure improved quality, effectiveness and efficiency);

(6) Customer-Focused Knowledge Strategy (aims at satisfying customer wants and needs).

According to the classification by **McKinsey & Company** (1998), KM strategies applied by MNEs are grouped into the following five basic categories (Day & Wendler, 1998, pp. 19-20; Haggie & Kingston, 2003):

(1) Developing and Transferring Best Practices (similar to Wiig's spreading of best practices across the industry);

(2) Creating a New Industry from Embedded Knowledge (revealing gaps in the market and the subsequent development of new products or industries);

(3) Shaping Corporate Strategy around Knowledge (the strategy comes from the mid-1990s' *Monsanto's* experiences related to pursuing two different groups of business activities: one – based on best practices and the second one – based on innovation. The dissimilar (thus incompatible) strategies resulted in Monsanto's decision to concentrate only on one strategy) (Junnarkar, 2011, p. 34);

(4) Fostering and Commercializing Innovation (this strategy is similar to that advocated by Wiig and targets at sustaining CA through technological innovation and decreased time to market);

(5) Creating a Standard by Releasing Proprietary Knowledge (this strategy is similar to the "Intellectual Asset Management Strategy" advocated by Wiig and can be best explained by the example of *Netscape*. Its declining Internet browser market share had to be urgently supported. As a consequence, the firm decided to change its corporate strategy: they made their source code publicly available for free. Free access to the Internet helped the company establish its browser as a worldwide standard. Profit, on the other hand, was generated in an indirect way: through a complementary product, the server software).

Classification by End Results

This classification was introduced by Treacy and Wiersema who put forward the idea of the three "**value disciplines**" (**customer intimacy, product leadership, and operational excellence**) (Haggie & Kingston, 2003). These activities are regarded as the primary focus of attention of market leaders, which rather than dispersing their efforts via pursuing all activities, normally focus only on one specific area of business activity and excel at it (CA or SCA). Outsourcing is one of the confirmations of the aforementioned.

The above indicated value disciplines underscore the importance of a trade-off between **convenience, quality and price** which are key determinants of a product purchase. As a result, the basic elements to any competitive business include: **the business itself** (“**Operational Excellence**”: sharing best practices, improving effectiveness and efficiency,

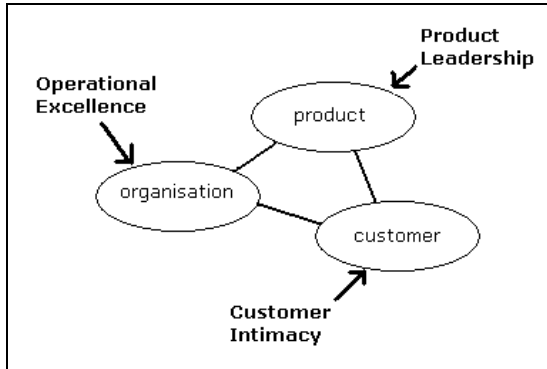


Figure 18: Focus Areas for Value Disciplines
(Source: Haggie & Kingston, 2003)

reducing costs), **its product(s)** (“**Product Leadership**”: constant improvement of the existing product(s) and development of new products, application of the best marketing techniques), and **its customers** (“**Customer Intimacy**”: improving customer satisfaction, identification of customers’ preferences, wants and needs, etc.) (Haggie & Kingston, 2003).

Other Approaches

Another approach to KM strategies is **Zack’s Knowledge Strategy** (1999, p. 125), which is indicative of sustaining or (re)-establishing the organization’s CA. Zack’s K Strategy is characterized by unique links between K and strategy, whereas the respective **competitive knowledge** is subdivided into: **core K** (the K required by all industry players to secure the normal functioning of a business; nevertheless, it does not necessarily implicate a CA), **advanced K** (CA is secured either through K differentiation or application of K in different ways as compared to rivals), or **innovative K** (K that secures a market leader position and is regarded as a differentiating factor in the entire industry) (Zack, 1999, pp. 125-127; Haggie & Kingston, 2003).

According to Zack, in order to secure a competitive K position, it is imperative for a company, to apply a **SWOT** analysis and identify strategic gaps in its K base:

- **Exploration versus Exploitation** (the degree to which K resources have to be improved versus the opportunity for leveraging the under-exploited K base), and
- **Internal versus External K** (building up new K either externally or internally, or Closed vs. Open Innovation).

As a result, companies that exploit internal K more frequently are regarded as rather “**conservative**,” whereas those which innovate more often than their rivals (e.g. thanks to Open Innovation) are referred to as more “**aggressive**” (Zack, 1999, p. 125; Haggie & Kingston, 2003).

A Synthesized Approach

In view of a wide range of complex approaches to managing intellectual capital, a comprehensive KM Spectrum is necessarily indispensable. Such a framework was introduced by Derek Binney (2001, p. 33).

According to Binney (2001; cited by Haggie & Kingston, 2003), KM activities are classified into 6 main groups:

- (1) **Transactional KM** (K is embedded in technology);
- (2) **Analytical KM** (K originates from external sources, mainly from customer-related issues, e.g. feedback and complaint management);
- (3) **Asset Management KM** (explicit K resultant as a by-product of everyday business activities can be exploited in numerous ways);
- (4) **Process-based KM** (improvement of business processes secured by sharing best practices);
- (5) **Developmental KM** (focus on continuous learning, training and staff development programs);
- (6) **Innovation/ Creation KM** (focus on new K generation through R&D and collaboration with other teams).

Summarized, the most relevant KM strategies are presented in the following table:

Transactional	Analytical	Asset Management	Process	Developmental	Innovation and Creation
Case Based Reasoning (CBR)	Data Warehousing	Intellectual Property	TQM	Skills Development	Communities
Help Desk Applications	Data Mining	Document Management	Benchmarking	Staff Competencies	Collaboration
Customer Service Applications	Business Intelligence	Knowledge Valuation	Best Practices	Learning	Discussion Forums
Order Entry Applications	Management Information Systems	Knowledge Repositories	Quality Management	Teaching	Networking
Service Agent Support Applications	Decision Support Systems	Content Management	Business Process (Re) Engineering	Training	Virtual Teams
	Customer Relationship Management (CRM)		Process Automation		Research and Development
	Competitive Intelligence		Lessons Learned		Multi-Disciplined Teams
			Methodology		
			SIE/CMM, ISO9xxx, Six Sigma		

Table 3: KM Spectrum and Applications (Source: Binney, 2001)

4.1.1. Key Components

Unfortunately, the idea of KM is *still in its infancy*, learning the essential walking steps (Davenport & Prusak, 2000, p. vii). As soon as the running starts, so to say, the competition will intensify significantly. Yet, step by step, more and more companies institute K repositories, supporting diverse types of K: best practices, lessons learned, product development and customer K, HR management K, etc. Moreover, nowadays numerous magazines, journals, and newsletters address KM issues, whereas prominent business schools offer more and more courses and programs on the topic. Even the World Bank announced the shift of its original function of money-lending towards two basic strategies: dispersing development-oriented K on the same level of importance as the money it loans. As a consequence, the “**Knowledge Bank**” concept appeared (Knowledge Bank, 2012). Thus, KM is gradually becoming an essential feature of advanced business culture today (Davenport & Prusak, 2000, pp. vii-viii).

Yet, unfortunately, the majority of organizations wastes too much time just acquiring K (or merely simply accumulating data), and spends actually not enough time on using K property. The so-called “**analysis paralysis**” is thus one of the primary challenges of KM today (Davenport & Prusak, 2000, p. xiii).

Moreover, KM should be embedded in the familiar aspects of the business: **business strategy** (application of highly strategic K to increase effectiveness and efficiency of business processes), **business process** (better channeling of the flow of K through redesigning of the K process and elimination of non-value-adding activities), **corporate culture** (creating K-oriented cultures that value creation, share and use of K), and **corporate behavior** (securing K-oriented behavior: focus on the factors that motivate and stimulate employees to create, share and apply K, managing information and K overload, eliminating the bottleneck of personal distraction and learning capacity) (Davenport & Prusak, 2000, p. iii).

4.1.1.1. Skills

Henry Ford, the pioneer in the field of management, once stated, “*Take out my building, take out my machines and all capital but leave my men with me, I will become Henry Ford again*” (Khurana, Parveen & Sharma, 2010, p. 1). This statement underscores the critical role of HR in an organization. As a matter of fact, management of HR is one of the most important and challenging tasks, since the use of any other resources depends upon the human factor, not to mention of the fact that humans as the carriers of tacit K are the source of constant CA and organic growth.

In fact, “*all businesses are alike except as to people,*” which highlights that achieving excellence of HR leads, as a result, to organizational excellence. Therefore, K, skills, abilities, values, and beliefs possessed by the organization’s workforce determine the efficiency and effectiveness of the organization in general (Khurana et al., 2010, p. 1).

The starting point for managing K in an organization is to understand its **core capabilities (CC)**. These constitute a CA for a firm: they are built over time and cannot be easily replicated. Thus, in order to create and maintain core technologic capabilities, it is indispensable to learn how to manage the K-creating activities and possess understanding of all the dimensions of the CC (Leonard, 1995, p. 4).

As a good example serves *Chaparral* (Leonard, 1995, pp. 13, 23). Its expertise is embodied in the energy and skills of each and every individual who day by day accumulate experience. And although much of this K is tacit in nature, i.e. resides in people’s heads, it is also embedded in *superior physical equipment and technical systems* (e.g. cutting-edge equipment as an automobile shredder which is believed to be the fastest and most efficient in the world or some of the most advanced digital furnace controls found at Chaparral) and *managerial systems* (the organized routines guiding resource accumulation and deployment).

Generally speaking, skills may be defined *as learned capacity (or abilities) to fulfill certain tasks with the minimum outlay of time, energy, or both*. From the employer’s perspective, professional skills coupled with the learning-to-learn skill (or knowing how to learn) are most desirable, since this set of skills secures fast execution of tasks and problem solving. Moreover, today with the growing uncertainty and necessity to constant adaptation to global change and innovation, the learning-to-learn skill gains more significance. It is cost- and time-effective, since it reduces the necessity for staff re-training (Ricketts & Ricketts, 2011, p. 602).

Just as mentioned above, **skills** and **K** embodied in employees is the dimension related to the organization’s **CC**. This dimension encompasses both **techniques** specific to the firm

and **scientific understanding**. One of engineers at Chaparral, e.g., is a recognized industry expert on the design of molds (Leonard, 1995, p. 20). This very person also helped design a set of measurement instruments including a clock accurate of one second in two million years (or to set atomic time standards). Such and/or similar skills which are based on public K or K available to all, that further require subtle understanding of the matter, are often referred to as **T-shaped**, meaning that they are both *very deep* (the stem of the T), but at the same time *broad enough* (the cross of the T) to enable K owners to explore the interfaces between their particular K and applications of that K in particular products. This combination makes the skills especially critical to the organization's CC (Leonard, 1995, p. 20).

In addition, the deep skill may be a rather rare occasion (not exclusive to one organization). Therefore, most companies hire an expert. E.g. Chaparral Steel metallurgists often apply for a consultation with experts from the Massachusetts Institute of Technology (MIT) to augment their K on specific issues. On the other hand, their internal expertise secures understanding of how the metal composition of a particular mold interacts with the evolving crystalline structure of the steel to create particular shapes. This K is not obtainable from books or in the laboratory: only on-line experimentation can secure it (Leonard, 1995, pp. 20-21).

Such K became critical in 1991, when the company decided to launch large structural beams for construction. The challenge was to provide an innovative design remaining a low-cost producer. As a result, Chaparral management achieved its purpose by purchasing some expertise from outside specialists, whereas the unusual mold was designed *in-house* by its own specialist. It goes without saying that the main idea behind internal design was related to keeping the KH inside (Leonard, 1995, p. 21).

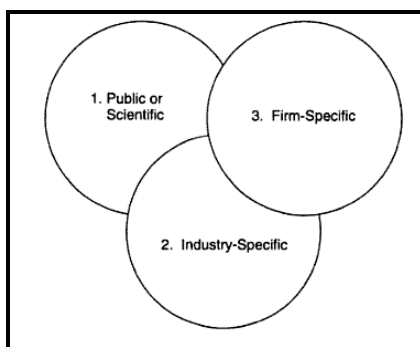


Figure 19: Types of Skills and Knowledge (Leonard, 1995, p. 21)

As a result, the three kinds of skills and K constituting CC are: **(1) scientific (or public) K**, **(2) industry-specific K**, and **(3) firm-specific K**. Moving from 1 to 3, skills become less codified and transferrable. In the above mentioned case study, the science of metallurgy is public (or codified in professional journals and textbooks). Industry-specific K about steel

manufacture is diffused among numerous experts, including suppliers and consultants (Leonard, 1995, p. 22).

In-house or firm-specific K, on the contrary, is not easily duplicated. Consequently, in order to approximate Chaparral's near-net-shape process, it does not suffice only to access the same scientific K of metallurgy and hire the same MIT consultants, and hire *all* the individuals involved in the process. It is also indispensable for a competitor to duplicate Chaparral's CC – the ability to transfer technological KH into viable products. Thus, compilations of K derived from multiple sources (embedded in software, hardware, and accepted procedures) coupled with skills and expertise of multiple experts (especially those who possess K of various functions) lead to synergy effects when the outcome is greater than the sum of its parts (Leonard, 1995, p. 22).

Apart from the aforementioned skills, ***problem-solving skills*** serve as the foundation in business (Ricketts & Ricketts, 2011, p. 360). They help easily recognize problems, invent and implement solutions, monitor and evaluate results. ***Creative thinking*** helps to transcend to innovation. Unsolved problems, on the contrary, lead to dysfunctionalities in the workplace, which further develop into impediments to flexibility, thus, to success. Individual capacity for ***creative thinking*** serves as the infinite source of new approaches to problem-solving, organizational design, and product development. Therefore, creative problem solving (in particular, analysis of problem solving) could be one of the critical moves towards strategic goals (Leonard, 1995, p. 240).

Furthermore, since most valuable K is primarily tacit in nature and in view of the complexity resultant from decentralized processes and organizational structures of the knowledge-based economy, ***communication skills*** are required to secure effective K transfer and the required integration.

Interpersonal skills help employees easily interact with each other, avoiding stress, coping with undesirable behavior in others or ambiguity, etc. ***Teamwork skills*** are critical for cooperative problem-solving (Ricketts & Ricketts, 2011, p. 602), thus practical innovations and solutions (e.g. through brainstorming), since radical innovations require inter-disciplinary cooperation (e.g. communities of practice or Open Innovation) (Huston & Sakkab, 2006).

Just as mentioned above, the ***learning-to-learn skill*** is key to acquiring new skills and critical thinking. It opens mental doors to thinking more efficiently, learning differently (*smarter, not harder*) as well as to creating and innovating. The learning-to-learn skill is particularly indispensable in the Information Age with its rapid change and obsolescence as an interminable danger. This, in turn, requires constant updating of employer-specific technical

K. In particular, it implicates the necessity to learn to distinguish between essential and non-essential information to help employees discern patterns and relationships in available information, thus, significantly improving job performance. Hence, productivity, creativity, innovation, and competitiveness all depend upon the employees' learning capability. Whereas machines and processes are easily purchased (or transferrable) between countries, human K is the key asset that secures CA and sustains it in the long run (Leonard, 1995, p. 240).

One of the HR development mechanisms applied to identify, capture and use tacit K (or to secure no outflow of valuable tacit K when employees leave their jobs or as a result of downsizing) is **job rotation**. In such a way, employees rotate over various routine jobs in a department, division, or unit before they are due for promotion as managers, e.g. This technique helps them acquire diversified skills and a broader outlook (turning specialists into generalists). In addition, job rotation increases the inter-departmental cooperation and helps to reduce the monotony of the work (Khurana, Parveen & Sharma, 2010, p. 104).

In addition, in view of the current data deluge, it is imperative to start structurizing the already available K to secure better quality messages and insights through determining which K is most valuable and synthesize it. Yet, such skills are not easy to find, since good K workers at any level should have a combination of “hard skills” (structured K, technical abilities, and professional experience) and “softer” skills (a sure sense of the cultural, political, and personal aspects of K), in other words, both technical KH and intuitive skills. Moreover, it is indispensable that K workers work closely with K users to secure K updating and constant progress (Davenport & Prusak, 2000, p. 110).

It goes without saying that organizations cannot exist without coordination. To be effective, employees need to understand how the organization works and how their actions effect organizational and strategic objectives. Therefore, acquiring skills in determining factors that impede or interfere with the organizational productivity and effectiveness (**organizational skills**) help one become a team builder or an innovator. Thus, organizational effectiveness skills are the building blocks for leadership. Proactive thinking and shared leadership have a positive effect on productivity (Hastings, Bixby & Chaudrhry-Lawton, 1986). One of the approaches is the superteam which is characterized by a highly performing team that produces outstanding achievements at *General Electric* (Lyubersky, 2008).

On the other hand, shared leadership as opposed to the traditional hierarchical system marked by employee empowerment and decision-making disclose a direct correlation between shared leadership practices and product improvement, creative and innovative problem-solving, and a more hospitable environment for culture change.

According to Leonard (1995, p. 89), individual, and thus organizational creativity is limited by background, training, and personal preferences in approach to problem solving. Yet, elimination of those core rigidities through constant reexamination of whatever perspective dominates at a certain period of time and ongoing learning and improving skills (specialization, cognitive style preferences, etc.) are likely to unleash creativity and stimulate innovation. One of the primary issues hereby is to ensure that the energy generated by the cognitive friction among individuals is channeled into creative K-building actions (encouraging the integrative skills of employees), *not* siphoned off into *unproductive* or *couterproductive* personal battles.

4.1.1.2. Articulation

Just as mentioned above, the KBV focuses on K as the company's most strategically important resource. In this sense, the KBV is an extension of the RBV. Organizational K as part of the company encompasses different types of K. It is not limited to scientific or technological K, but represents all types of K such as marketing, administrative, logistical K, and so forth, since all activities along the value chain require K and expertise (Choo & Bontis, 2002, p. 701).

In addition, in view of the prevalence of tacit K (about 80%) which resides in people's minds is intangible, dynamic, and difficult to quantify, proper articulation of tacit K is thus a real challenge. Moreover, articulation (**Tacit to Explicit**) as part of the aforementioned **SECI Model** by Nonaka & Takeuchi (1995, p. 60) plays one of the major roles to improve the company's learning capacity and organic growth. Articulation of tacit mental models can be viewed as "mobilization" of intangible resources, or a key factor for creating new K. New K, in turn, is indispensable to create CA and sustain it in the long run (Nonaka & Mascitelli, 2000, pp. 179-183).

Furthermore, in the Information Age of today with its prevalent media (traditional and digital, primarily, the Internet), attainment, storage and transmission of explicit K (easily coded, and symbolized) is reduced to accessing the right information. Thus, proper articulation through communication or dialogue coupled with finding the right metaphors and analogies to properly articulate the hidden tacit K is a must to transfer the skills and insights underlying the organization's CC. According to the pioneers of KM, one of the most effective ways of grasping and elucidating the rationality underlying the tacitly-informed behaviour leading to the refinement of comprehension is *brainstorming* (Nonaka & Takeuchi, 1995, p. 69).

On the other hand, there is a risk hereby to transfer valuable tacit K to those who might leave the company and copy it elsewhere. Therefore, articulation should be regarded as a strategically relevant move (Lubit, 2001, p. 166). Hence, inter-firm information flows are of significant importance, especially when it comes to K-intensive industries marked by sophisticated mechanisms of disseminating technical K and expertise (Choo & Bontis, 2002, p. 537).

According to Nonaka & Takeuchi (1995), Japan's example of a globally successful country is associated with its constant search for *talent, inspiration, and novelty*. As opposed to the Japanese who underscore the relevance of non-linear and intuitive K (or tacit K),

Americans are more inclined to focus on explicit K (or unambiguous, scientific and formal data), which, in turn, just as indicated above, is not necessarily a long-term CA.

The divergence between the two approaches leads, therefore, to ***incremental improvement*** in the case of Americans, and ***true creativity*** and ***innovation***, on the other hand in the case of the Japanese. One of the vivid examples is the development of a breadmaking machine described in the book by Nonaka & Takeuchi (1995). In order to secure production of tasty and profit-making home-baked bread, one of the famous Japanese companies entrusted its engineers with finding the kneading mechanism for making the proper dough texture. Upon long-term experimenting, the team of engineers apprenticed themselves to a well-known master baker and spent long hours observing his special twisting motions and kneading techniques. As a consequence, the “socialization” of the master’s technical skills as well as the articulation of its tacit K embedded in the kneading techniques led to the creation of the kneading mechanism of the final product – the breadmaking machine. A propos, the breadmaker proved a huge success (Nonaka & Takeuchi, 1995, pp. 95-107).

4.1.1.3. Commitment

Mere K (formal education) coupled with professional skills does not suffice, since K or CA is not just pooling together diverse bits of data and information. According to Nonaka & Takeuchi (1995, p. 58), “*knowledge, unlike information, is about **beliefs and commitment**.*” In their theory of organizational K creation, both academics *do* adopt the traditional definition of K as “*justified true belief*.” Yet, as opposed to traditional epistemology which emphasizes the absolute, static, and non-human nature of K, typically expressed in formal logic, Nonaka & Takeuchi (1995, p. 58) shift the paradigm to the “***dynamic human process of justifying personal belief toward the “truth.”***”

Thus, K is a highly individual process of personal and inter-personal (or organizational) self-renewal, whereas personal commitment of employees coupled with their identity with the company proves a necessity (Nonaka & Takeuchi, 1995, p. 10). Moreover, commitment may sometimes be crucial to implement a company strategy, especially when it comes to servicing.

Just as mentioned above, commitment as well as beliefs are both deeply rooted in individuals’ value systems (Nonaka & Takeuchi, 1995, p. 59). Furthermore, both information and K are context-specific and relational. They depend upon the situation and are created *dynamically* in social interaction among people, thus, constructing social K as a reality, which, in turn, influences their judgment, behavior, and attitude.

In order to successfully manage the organization’s K base, it is imperative to possess the commitment and loyalty of its employees (Storey & Quintas, 2001; Pellicelli, 2003, p. 17). This is primarily due to the fact that most of the organizational K is highly personal (or tacit). The biggest challenges hereby are related to the behavioral “problems” or reluctance to share K willingly caused by the conflicts in the employment relationships (Hislop, 2003, p. 1).

As a matter of fact, motivating an organization proves not an easy task, primarily because of insufficient communication, failure to integrate KM in everyday activities, lack of time or willingness to share K among colleagues (self-interest), failure to use K effectively (information overload and time-consuming search), difficulties of capturing tacit K, etc. Consequently, the acceptance of KM implementation should not be driven or imposed from top. The proactive use of KM systems, on the contrary, is based upon the use of ***incentives and cultural interventions***: fostering commitment and motivation are indispensable prerequisites for the success of KM implementation (Nonaka & Takeuchi, 1995, pp. 57-60).

Generally speaking, commitment may range from ***negligible or partial commitment*** (or avoidance, non-use, and unenthusiastic use) to ***absolute commitment*** (or skilled,

enthusiastic and consistent use) to the organization's KM program. As the primary motivators serve the three processes of **compliance (reward)**, **identification (relationships)**, and **internalization (behavior congruent with the organization's value system)** (Malhotra & Galletta, 2003).

Commitment by compliance results as a result of rewards, or punishments, which, in turn, implicates that the employee may not necessarily understand the value of the desired change and K sharing. Consequently, the latter will focus primarily on the maximization of incentives, *not* on maximizing value-adding. Quantity-based incentives for K sharing are likely to be associated with minimal investments. Yet, in the longer term, they will lead to information overload and waste of time and effort to locate the high quality information (Malhotra & Galletta, 2003).

Commitment by identification results from the employees' need for acceptance (both by peers and managers) and esteem based upon social recognition. This type of commitment is characteristic of the employees' adoption of the values and beliefs associated with the well-known or recognized figures in order to replicate their social image. Nevertheless, the basic disadvantages of commitment by identification are its relative ineffectiveness:

- (1) if the specific role model is ill-chosen, and
- (2) if the content of the desired behavior proves alien to employees (Malhotra & Galletta, 2003).

Commitment by internalization is related to the need for imparting values that would guide culture change. Primarily, this is due to the fact that internalization of values and behavior patterns have a much longer-lasting effect than rewards, punishments, or social recognition (extrinsic rewards and rather manipulative methods of commitment) (Nonaka & Takeuchi, 1995, pp. 62-69; Malhotra & Galletta, 2003), since they are related to deepest level of the culture paradigm ("basic assumptions") (Schein, 2004, p. 25).

As a consequence, commitment by internalization (a self-governing process of commitment) proves a self-generated and natural process, whereas the chance of deceiving is considerably lesser as compared to the two other types. In this case, employees sincerely contribute high quality K adding value to the overall K creation process and are genuinely invested in it as opposed to artificially inflating the quantity regardless of quality K (Malhotra & Galletta, 2003).

Numerous research confirms that changes in employment enabled by downsizing and delayering, focus on flexibility of the workforce and the emergence of virtual organizations

have adverse effects on the organizational commitment. Even survivors of downsizing show much lower levels of loyalty and trust, as a result (Hislop, 2003, p. 2).

On the other hand, paradoxically, as it may seem (despite the K deluge characteristic of these days), the creation and management of K as the source of CA, is becoming more and more difficult to achieve, primarily because of the constant evolution in organizational forms and structures (Hislop, 2003, p. 2).

4.1.1.4. Affirmation

Nowadays, organizations start to understand the power of unleashing K among individuals. The main struggle consists in identifying *how* exactly to unleash that power and render employees willing to share their insights, instead of hoarding the K they possess. Thus, the major challenge is to figure out ***how to create a K-sharing culture*** in an organization.

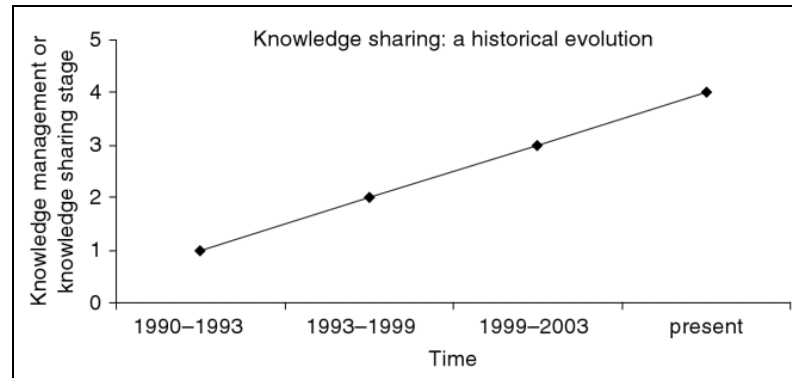


Figure 20: Knowledge Sharing: A Historical Perspective
(Source: Thatchenkery & Chowdhry, 2007, p. 3)

From the historical perspective, K sharing increased four-fold as compared to the 1990s. Yet, only if K is shared appreciatively, managing K becomes no longer an issue. Thus, **affirmation** is rather a psychological need of sharing insights and ideas with others. This need may be fulfilled in the presence of an explicitly appreciative format to openly have a say without being questioned, critiqued or put on the defensive. Hence, to secure organizational excellence, it is imperative to *institutionalize* K sharing (Thatchenkery & Chowdhry, 2007, p. 3).

Moreover, it is necessary to locate and enhance the “*life-giving-forces*” or core values of organizations as “*systems of shared meaning and beliefs where the critical ability is the continued construction and maintenance of the meaning and belief systems which assure compliance, commitment, and positive effect on the part of the participants*” (Thatchenkery & Chowdhry, 2007, p. 46).

K can take a long time to accumulate, but the things that a person really needs to know might enlighten the person like a stroke of a thunder. And if an appreciative culture of K sharing internalizes corporatewide, a breakthrough or innovation will become only the matter of time.

4.1.1.5. Doubt

Deep down, a human being is credulous in character, since the most compound stratum of our lives consists in believing. Yet, enormous gaps of doubt might open up new vistas to our beliefs, since doubt often leads to new dimensions and insights. Therefore, doubt may be regarded as a modality of belief that belongs in the same stratum of life (Ortega, Gasset & García-Gómez, 2002, pp. 185-186).

According to Nonaka & Takeuchi (1995, p. 23), questioning all beliefs in an attempt to create one's own philosophy from scratch started long ago. The Platonic and Aristotelian views were inherited through intermediate philosophers by the two mainstreams of modern epistemology (the theory of knowledge): the **Continental rationalism** (René Descartes) and the **British empiricism** (John Locke). Descartes' methodological skepticism was seen in the following question: "*What can I hold as true beyond any doubt?*" Descartes argued that objects cannot be sensible (e.g. wax changes its qualities if placed near fire), thus, true knowledge about external things can be obtained by the mind, *not the senses* (Nonaka & Takeuchi, 1995, p. 24).

John Locke, the founder of British empiricism, on the contrary, criticized Descartes's rationalism stating that things existing in the real world are objective in nature and that even if the sensory perception of things is illusory, something, undoubtedly, *can* be perceived. According to Locke, the human mind is **a tabula rasa** ("*white paper, void of all characters*"), that has no a priori idea and has to be filled with **experience (sensations and reflections)** to provide the mind with ideas (Nonaka & Takeuchi, 1995, p. 24). Therefore, experience is crucial to secure values and beliefs.

In the eighteenth century philosophy the two streams of rationalism and empiricism were synthesized by Immanuel Kant. Kant argued that the basis of K is again *experience*. Yet, the philosopher disagreed with the empiricist argument that experience is the sole source of all K (closer to rationalism than empiricism). Moreover, in view of his vision of the "phenomenon" as the "**transcendental object**" or "**thing in itself**," which transcends experience, his philosophy is often referred to as "**transcendental idealism**" (Nonaka & Takeuchi, 1995, p. 24).

According to Descartes et al. (1947, p. 1997), *K that may be defined as a conviction based on a reason so strong that it can never be shaken by any stronger reason*. Yet, when there remains some reason which might lead to *doubt*, there is only a conviction, or *no true K*. Moreover, doubt implicates the **intermediate stage** between *belief* and *complete disbelief*. It is an alternate belief and disbelief, with an element of uncertainty ("*I think so, but I don't feel*

sure”) (Russel et al., 1984, p. 142). This, in turn, is indicative of deep insights or profound knowledge (tacit K or intuition) which help find alternatives or accommodate the disbelief.

It may be labeled as a paradox, yet, it is hard to describe genuine doubt except by saying that one believes in it (Ortega, Gasset & García-Gómez, 2002, p. 186). Hence, the difference between belief and doubt consists not in a “*not believing*,” as opposed to a believing, nor is it a “*believing it is not the case that*” as opposed to a “*believing that it is*.” The basic discrepancy between the two lies in that which is believed in. As a result, doubt places people in the sense of being placed on something *unstable, non-solid, or a non-firm medium* (Ortega, Gasset & García-Gómez, 2002, pp. 186-187). Thus, it is ***the instability of doubt*** that leads to the exploration of the terra incognita of K, securing *new ideas, creative problem-solving and innovation*.

Since nothing is constant but change, K in the unstable world cannot be stable as well. Thus, humans cannot rely heavily on the solutions of the past: they need to have doubt (to a reasonable extent) to secure change and progress in the long run. As a result, doubt brings closer to the unlimitedness of K. On the other hand, doubt should *not* be in excess. Equilibrium between *doubt* and *confidence* is indispensable to secure sound decision making. It is of paramount importance, especially in business environment, where some decisions may involve not only the future of the company, but also the fate (social security) of millions of people worldwide. Not to mention of politicians whose decisions impact lives of whole nations.

4.1.1.6. Experience

Even before the days of “CC,” “*the learning organization*,” “*expert systems*,” or “*strategy focus*,” all managers valued experience, KH and insights of their employees, or their K (Davenport & Prusak, 2000, p. xviii). As opposed to traditional theorists who viewed the company as a “*black box*” with resources going in, products coming out and the markets in which the company participated, today’s theorists pay more attention to the dynamics inside the box: the K embedded in routines and practices that the company transforms into valuable products and/or services in still rather imperfect “knowledge markets” (Davenport & Prusak, 2000, pp. xviii, xxi).

One of the primary benefits of experience is the historical perspective which it provides to help evaluate and act in new situations and events, since K born of experience recognizes similar patterns and draws connections between the present and the past (Davenport & Prusak, 2000, p. 8). On the other hand, it is imperative to point out in this context that the number of years of “experience” (or e.g. a bachelor’s degree or an MBA) does not quantify the value of experts’ experience (Sioma, 2000, p. 2). The experience of the latter is measured by the **quality** of experience-based insights, performance, actual qualifications, informativeness about the current discoveries and industry advances, etc.

Moreover, the current trend towards *leaner organizations* and the *quality movement* intensify the relevance of quality K and quality experience, in particular. K develops over time, through experience – things done or experienced in the past. In addition, experience includes what people absorb from *books* and *mentors* as well as through *informal learning*. Therefore, “experience” and “expert” are related words. Both are derived from Latin and mean “to put to the test.” Hence, experts are people with profound K of a subject which was further tested and trained by experience. As a result, the firm that hires experts is ready to pay premiums for the experience-based insights provided by the latter (Davenport & Prusak, 2000, pp. 7-8; Ortega y Gasset & García-Gómez, 2002, p. 200).

According to Nonaka & Takeuchi (1995, p. 63), experience is key to acquiring tacit K. The mere transfer of information from one person to another (without some form of shared experience) would fail to project one’s own self into another individual’s thinking process or even express it in words.

On the other hand, tacit K serves as the foundation of CA and organization K creation. Therefore, it is indispensable to focus on transfer of tacit K as the primary source of new K (future) based on a combination of best practices (past and present) and intuition. Hence, sharing of tacit K among multiple individuals with different backgrounds, perspectives, and

motives (e.g. communities of practices) is crucial to secure new K creation, and thus innovation and sustainability (Nonaka & Takeuchi (1995, p. 85).

4.1.1.7. Ground Truth

Experience changes perceptions about what *should* happen into K of what *does* happen. Therefore, experience should be based on practice or ground truth, *not* theory or generalization. In fact, the word combination “**ground truth**” was borrowed from the U.S. Army’s Center for Army Lessons Learned (CALL) used to designate the rich truths of real-life situations or K gained “on the ground” (Davenport & Prusak, 2000, p. 8).

It goes without saying that effective K transfer is critical for the army, since *knowing what to expect* and *what to do* in military situations might literally implicate a life-or-death matter. Thus, ground truth is translated into ***knowing what works*** and ***what does not***. As a vivid example serves regular participation of experts from CALL in real military operations as learning observers. In such a way, they collect material and disseminate the gathered K in the form of photos, video tapes, briefings, and simulations. As a result, lessons learned in the early 90s, e.g., were passed on to the troops in later missions (Davenport & Prusak, 2000, p. 8).

Moreover, the army’s key to success at managing K lies in its “After Action Review” (AAR) program which involves the analysis of what was supposed to happen and what actually happened. The comparison of the two leads to the identification of disparities and reasons for positive and negative trends. As a result, lessons learned are incorporated into formally documented procedures and training programs, and serve not only as a means of accountability, but also as K and a learning tool in the AAR (Davenport & Prusak, 2000, pp. 8-9).

Another breakthrough in the army’s K experience was due to the reflections of one senior officer who, late in his career, read Tolstoy’s *War and Peace*. Struck by the differences between Tolstoy’s true-to-life depictions of Napoleonic War battles and the rational abstractions of those taught in classes (the gap between ground truth (or real-life K) and rational analysis found in books), he prompted the necessity of introducing something similar to the present-day CALL program (Davenport & Prusak, 2000, p. 9).

In the battle between business competitors, strategists identify similar distinctions between how strategy actually works in practice and how it is taught in business schools. Thus, sharing and understanding details and meaning of the ground truth or real experiences is generally much more valuable than expounding on theories about them (Davenport & Prusak, 2000, p. 9). Consequently, transfer of K of the everyday, complex reality of practice (intimate or tacit K of the world) secures invaluable insights into best practices, thus, providing growth and stability on a global scale (Pickles, 1995, p. 101).

4.1.1.8. Complexity

Experience and ground truth indicate of person's ability to deal with complexity. Since K is not a rigid structure, it can be easily contextualized. Moreover, ***K can deal with complexity in a complex way***, so to say. This is one of the most essential sources of K value creation. In particular, it implicates that knowing "less," even if the "less" seems to be clearer and more definite does not usually secure improved decision making. Certainty and clarity may often overlook quite essential (yet, minor) factors. Thus, reliance upon one single, uncontradicted data source may give a feeling of omniscience or illusion of accuracy. On the other hand, such data may lead to non-adaptive action and thus failure in the long run (Davenport & Prusak, 2000, pp. 10-11).

It is imperative to point out in this context that K is aware of what it does *not* know. This fact is confirmed by many knowledgeable or wise people who become more and more humble as soon as they learn and know much. A very interesting thing that confirms the relevance of the aforementioned illusion of accuracy happened in one genetic-engineering firm. This company created a new tomato that could be stored longer and shipped later than current varieties. It was expected that the newly developed sort of tomatoes could become a real hit. Yet, it turned out that different sorts of tomatoes do not equally do in different climates (this fact is, by the way, known to all experienced farmers engaged in tomato growing). Thus, since the new tomato was derived only from one variety, it was a success only in some small areas. As a result, a scientific triumph turned into a commercial failure.

Generalized, the above indicated example is a vivid illustration of an R&D-oriented product development, when either only one data source is used or when the new product is not market-oriented (Davenport & Prusak, 2000, p. 10), whereas K transfer and digestion of change among various stakeholders is, unfortunately, limited to speed of learning or susceptibility to new ideas (Eisenhardt & Santos, 2000, pp. 1, 11).

4.1.1.9. Judgment

Unlike data and information, K is often highly personal, thus, contains judgment. K also refines or updates itself in response to new situations and information. Thus, it can be compared to a living system, developing and modifying itself via interaction with the outer environment (Davenport & Prusak, 2000, p. 10).

According to Nonaka & Takeuchi (1995, p. 59), both information and K are created dynamically in social interaction among people, thus, constructing social K as a reality, which, in turn, influences their *judgment, behavior, and attitude*. This, in turn, confirms both advantages and limitations of non-logical processes, and some circumstances in which such non-logical “good judgment” or “good sense” have an advantage over rationality (Nonaka & Takeuchi, 1995, p. 53). On the other hand, when K stops evolving, it turns into *opinion* or *dogma*. As a vivid example serve “experts” whose K seem to consist only of stock responses and the same old answer to any new question (Davenport & Prusak, 2000, p. 10).

In addition, judgment helps identify the problem severity and priority (Khan & Zhang, 2005, p. 92) and is indicative of analysis.

There exists a myth that *managerial judgment*, which is most relevant for strategy formulation, cannot be measured in view of its intangibility. Yet, managerial judgment is in fact quantified on a daily (even hourly) basis: by financial analysts, bankers, creditors, superiors, and subordinates. The effective results are achieved by the achievement of the enduring value of the shareholder’s investment and can therefore be easily improved (Sioma, 2000, p. 1).

4.1.1.10. Rules of Thumb

K works through rules of thumb: flexible guidelines to action evolved through trial and error and over long-term experience and observation. As a matter of fact, the term “rules of thumb” stand in the language of artificial-intelligence community for *shortcuts to solutions in new situations* when new problems resemble problems previously solved by more experienced workers. Rules of thumb help identify patterns in new situations, and thus respond more effectively. As a result, the solution should not be built from scratch every time. Hence, K expressed through rules of thumb offers **speed**. It allows its possessors to solve new situations faster and much more efficiently, even when it comes to rather complex issues (Davenport & Prusak, 2000, pp. 10-11; Nonaka & Takeuchi, 1995, p. 35). This, in turn, explains the relevance of training and practice to enable experience curves in organizational learning.

According to Roger Schank, a computer scientist at Northwestern University, such internalized responses are referred to as “*scripts*.” Like computer program codes, they serve as efficient guidelines to complex situations (Davenport & Prusak, 2000, p. 11).

Scripts are shortcuts through numerous alternatives that save managers and K workers the trouble of consciously analyzing every step of the solution. They may be played so quickly that one may not even be aware of them. Thus, the solution is arrived at in a rather intuitive way, without humans’ realizing how they got there. This automatic or unconscious problem-solving secures very high speed of execution (Davenport & Prusak, 2000, p. 11; Sioma, 1980, p. 62). According to Karl Weick, **intuition** is “**compressed expertise**” which implicates how K works and what it can do is very similar to rules of thumb (cited by Davenport & Prusak, 2000, p. 11).

As a vivid example serves the skill of an experienced driver who *knows* how to drive, does a series of complex actions automatically as compared to a beginner. Moreover, a veteran driver also develops an intuitive sense of *what to expect* on the road. It is experience that makes the experienced driver aware of minute signs that might be indicative of danger which a beginner driver, on the contrary, would normally miss, since they are too subtle to be very taught at a driving school. The same is true of an experienced businessperson who quickly, without going through a definable process or even being unable to explain his or her “reasoning,” evaluates the situation and makes his/her decision making (Davenport & Prusak, 2000, p. 11).

4.1.1.11. Values and Beliefs

According to Nonaka & Takeuchi (1995, p. 58), *“knowledge, unlike information, is about **beliefs** and commitment.”* Moreover, in the theory of organizational K creation, both academics adopt the traditional definition of K as *“**justified true belief.**”* As opposed to traditional epistemology which emphasizes the absolute, static, and non-human nature of K, typically expressed in formal logic, Nonaka & Takeuchi shifted the paradigm to the *“dynamic human process of justifying personal belief toward the **“truth.”**”*

Many people assume that organizations are objective and neutral and their purpose reduces to creating a product or a service. As a result, their goal may seem quite detached from values. Yet, according to Schein’s Model of Organizational Culture (2004) mentioned above, individuals’ values and beliefs have a tremendous impact on organizational culture (thus, K, in general), since organizations are made up of humans whose values and beliefs unconsciously impact their thoughts and actions. Moreover, organizations are characterized by histories, and stories told by employees or expressed through their actions and words, which, in turn, is indicative of the underlying corporate values and beliefs on the “artifacts” or physical level (Schein, 2004, p. 25; Davenport & Prusak, 2000, pp. 11-12; Leonard, 1995, p. 24).

A belief does nothing but vary the manner, in which people conceive an object. It can only provide an additional force and vivacity to their ideas (Russel et al., 1984, p. 137). As a matter of fact, values and beliefs are an integral part of K, thus, determining significantly what individuals sense, absorb, digest, and conclude from their observations. As a result, people with different values see one and the same situation or thing not identically, therefore, filtering the K through a personal prism of values and beliefs. A bustle of urban life may be regarded as energy and variety for someone who values it and as chaos and danger for somebody who prefers rural quiet. In business environment, different values and beliefs are translated into different degrees of risk taking (either as new opportunity or a threat) (Davenport & Prusak, 2000, p. 12).

Moreover, according to Edgar Schein (2004, p. 17), **organizational culture** is defined as *“[a] pattern of **shared basic assumptions** that was **learned** by a group as it solved its problems of **external adaptation** and **internal integration**, that has worked well enough to be **considered valid** and, therefore, to be taught to new members as the correct way you **perceive, think, and feel** in relation to those problems.”* The given definition underscores anew the primary importance of shared mental assumptions or shared values and beliefs as

basic determinants of judgment and behavior patterns that guide action and thought in organizations.

Moreover, according to Hill & Jones (2008, p. 11), culture change within an organization is impossible without a respective *accumulation of specific values and norms shared by the members of the same organization and which, in turn, will impact the members' interaction and behavior patterns both internally and externally*. Therefore, the infinite power of K to organize, select, create, learn, share, innovate, and judge comes from values and beliefs as much as from information and logic (Davenport & Prusak, 2000, p. 12).

Hence, **belief systems are of paramount importance** and which is still more crucial for a firm is to manage to properly communicate and internalize its corporate values and beliefs to its employees and have them further articulate its corporate belief system both to customers (through final products, skills, cooperation, etc.) and among themselves or other stakeholders, thus, fostering voluntary K sharing, and culture of learning and constant change built on trust and mutual support (Nonaka & Takeuchi, 1995; Leonard, 1995; Smith, 1990).

In view of the aforementioned, the author developed the following hypothesis:

Hypothesis (H) 1: As a result of the rapid globalization of technological standards (primarily enabled by the Internet and its ubiquity), the resultant convergence of markets as well as a relative high degree of homogeneity in customer preferences worldwide, **standardization** and **adaption** are basic strategies preferred when choosing a MEM.

H 2: Bidirectional flow of technology is a rare occasion in view of the cut-throat global competition and uncertainty as to the outflow of technological KH, which then could be easily purchased and/or imitated. Thus, in the case of technological KH, a WOS is preferred to a JV. As an insurance against KH outflow serves cross-licensing.

Managerial KH or tacit knowledge, on the contrary, is much more difficult to replicate. Therefore, franchising is the common MEM to capitalize on intellectual property.

H 3: Successful **experience** in using a certain MEM (e.g. JV) in the past enhances the company's inclination towards the preference of the same foreign MEM in future (JV). In other words, experience is a key determinant for the firm's further steps.

H 4: The choice of **WOS** vs. **IJV** as two basic strategic rivals depends primarily upon the company size, the degree of its multinational involvement, and R&D intensity.

H 5: During the current financial crisis, **outsourcing** is rapidly gaining pace. In addition, **M&A** are one of the most preferable MEM during recession.

5. Results

Globalization gains pace. Its coverage all over the globe helps not only parent companies to expand internationally, but improves host countries' total investment capacity due to increasing flows of finances from abroad. Foreign direct investment (FDI) (and MNCs as major FDI providers) is therefore the most interesting way of investment that influences both economies of home and host countries (Hilmi et al., 2007, p. 242). Different MEM have different performance outcomes: **WOS** should outperform **IJV**, and **IJV** should outperform **acquisitions**.

In view of current turbulent economy marked by the economic downturn, converging industries and cut-throat global competition driven by globalization processes, SA are gaining pace (ranging from a sub-supplier contract (outsourcing) to franchising and ILA, from R&D partnerships to IJV and consortia (exports and external loans)) (Pellicelli, 2003, pp. 1-2).

From the historical perspective, it should be pointed out that focus of companies' main factor and objective changed just as radically as technology and lifestyles.

Period	Main Factor	Main Objective
1970s	Product Performance	The best product, the lowest cost, the most recent technology
1980s	Position in the sector	Economies of scale and economies of scope
1990s	Capabilities and competences	Innovation, advantages through changing conditions and emerging opportunities
2000s	Knowledge	Acceleration of technological innovation, shortening of product life cycle, convergence of technologies, progress in IT, significant reduction in R&D costs, deregulation and globalization

Table 4: Historical Perspective (Source: Pellicelli, 2003, pp. 2-3)

Yet, just like in the old good times, SA manage (apart from efficiency issues, protection from competition and technology access) to set **new global standards** and **overcome protectionist barriers** (normally to secure subsequent M&A and the monopoly status by global market share) (e.g. *Nestle's* acquisition of *Haagen Dazs*).

In addition, in view of the long-term accumulation of K and experience, the optimal MEM depends to a certain degree upon the nature of the company's **distinctive competency**: either in **technological** KH or in **management** KH. In the case of technological KH where proprietary controls are a must, ILA and IJV are to be avoided to minimize the risk of losing control of the technology. Therefore, for a high-tech company a WOS is a much better choice (Hill & Jones, 2012, pp. 291-292).

On the other hand, ILA and IJV must be structured to maximally reduce risks of KH expropriation on the part of licensees or JV partners. Technology licensing is an insurance against imitations and as well as the establishment of own technology as a standard or dominant design (e.g. as *Matsushita* did with VHS format for VCRs securing ongoing royalty payments) (Hill & Jones, 2012, p. 292). Such actions are primarily taken to deter competitors from developing their own, possibly superior, technology. On the other hand, risks related to licensing outweigh risks of losing control of technology KH. Consequently, ILA should be applied with much caution.

Management KH, on the contrary, is more characteristic of service companies (e.g. *McDonalds* or *Hilton* hotels) (Hill & Jones, 2012, p. 292). In fact, management KH is tacit K and therefore much more difficult to replicate. Moreover, the most valuable asset in such cases is the company's brand names additionally protected by international laws pertaining to trademarks. Hence, the risk of losing control over management KH to franchisees or JV partners is relatively low.

In view of the aforementioned and while many issues related to technological KH do not appear in the case of management KH, numerous service companies prefer a combination of franchising and subsidiaries (WOS or JV) to control franchisees within a certain region or nation. From the political perspective, JV are favored more.

It goes without saying that globalization requires constant cost reduction. **Cost reduction** pressures lead, in turn, to the choice of a combination of **exporting** and **WOS**. Manufacturing facilities are then placed in the centralized locations where factor conditions are optimal, whereas via exporting to the rest of the world, a company manages to realize substantial economies of location and economies of scale. A number of marketing subsidiaries (WOS) may be based in various countries to overtake distribution in a particular region. Thus, marketing WOS are preferred more to a JV arrangement or services of a foreign marketing agent, since they secure tight control over marketing activities, thus, no loss of revenue and income potentials (Hill & Jones, 2012, p. 292).

Furthermore, tight control over local operations enable the corporation to use profits secured in one market to improve its competitive position in a different location. Therefore, companies pursuing global or transnational strategies favor the establishment of WOS in the overseas markets (Hill & Jones, 2012, p. 292).

The following table provides an overview of primary advantages and disadvantages of basic MEM.

Entry Mode	Advantages	Disadvantages
Exporting	Economies of location and economies of scale	High transport costs Trade barriers Problems with local marketing agents
Licensing	Low development costs and risks	Lack of control over technology No economies of location and economies of scale No global strategic coordination
Franchising	Low development costs and risks	Lack of control over quality No global strategic coordination
Joint Ventures	Access to local knowledge Shared development costs and risks Political dependency	Lack of control over technology No economies of location and economies of scale No global strategic coordination
Wholly Owned Subsidiaries	Control over technological KH Economies of location and economies of scale Global strategic coordination	High costs and risks

Table 5: Advantages and Disadvantages of Different Entry Modes

(Source: Hill & Jones, 2012, p. 166)

According to the World Bank's database, rapid globalization and aggressive competition on an international scale gradually lead to the complete exclusion of small-size players or newcomers from the global marketplace, thus, enabling the exclusive dominance of MNCs (80% of total exports). Radical cost reduction is extremely difficult to tackle for SMEs. About 57% of new entrants are forced to quit within the first year of entering the export market (Oluwarotimi, 2012). The figures speak for themselves.

Another table is an overview of market entry modes by industry.

Entry Mode	Industry	Reasons for Entry	Examples
Exporting	Manufacturing	Pressure for Cost Reduction	Avon
Licensing	Manufacturing	Technological Know-How Lack for Resources (SMEs)	Dolby
Franchising	Servicing (Fast-food) Clothing Distribution	Management Know-How	McDonalds Burger King
Turnkey Projects	Chemical, pharmaceutical, petroleum, mining industries	Technological Know-How Management Know-How	Numerous public housing projects
Outsourcing manufacturing	Production Information Technology	Pressure for Cost Reduction Skilled Workforce	IKEA
Management Contracting	Hotel Industry	Management Know-How	The Four Seasons Hotel
Strategic Alliances	Motor Vehicle Industry	Technological Know-How Management Know-How Pressure for Cost Reduction	Microsoft-Toshiba Cisco-Fujitsu
Mergers	Most industries	Technological Know-How Management Know-How	Boeing and McDonnell Douglas

		Pressure for Cost Reduction	
Acquisitions	Most industries	Technological Know-How Management Know-How Pressure for Cost Reduction	Pfizer acquired Warner-Lambert
Joint Ventures	Capital intensive industries (e.g. Electronics, Pharmaceuticals)	Technological Know-How Management Know-How	Fuji-Xerox
Wholly-Owned Subsidiaries	High Tech Electronics Pharmaceuticals	Technological Know-How Management Know-How Pressure for Cost Reduction	SAP

Table 6: Entry Mode Choice by Industry (Source: Own Work)

It goes without saying that K and experience gained from overseas operations are indispensable and be used as spillovers over the corporation's all WOS. Their impact is easily confirmed by contribution of K intensive business services (KIBS) to growth opportunities within EU (1995-2007).

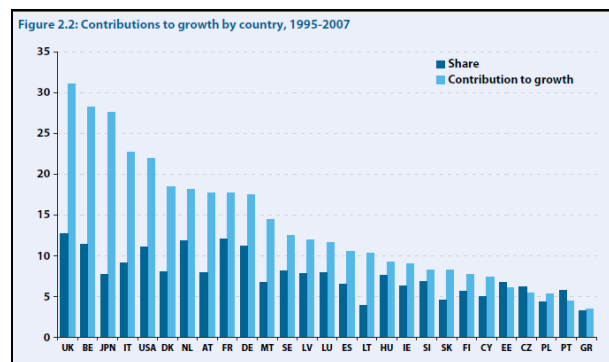


Figure 21: Contribution of KIBS to Growth by EU Country, 1995-2007 (European Competitiveness Report 2011, 2011, p. 59)

The above analysis of MEM results in the following conclusions:

H 1: Standardization and Adaptation

Increased globalization gradually leads marketplaces from national markets as distinct entities, isolated by trade barriers, and barriers of distance, time, culture, and religion towards one huge global marketplace (Levitt, 1984, p. 2). These converging markets completely reshape numerous industries. Standards in technology, customer preferences, and, thus, homogeneity in basic product offerings (e.g. global acceptance of *Coca-Cola*, *Sony PlayStation*, *McDonalds* hamburgers, the *Nokia* wireless phone, and *Microsoft's* Windows operating system) lead to the introduction of global (probably, sometimes still unofficial) technological standards (Hill & Jones, 2012, p. 147).

Moreover, the prevalence of multinationals in exporting further intensifies the relevance of cost effectiveness on an international scale, and, thus, the inevitability of standardization and specialization worldwide (Oluwarotimi, 2012).

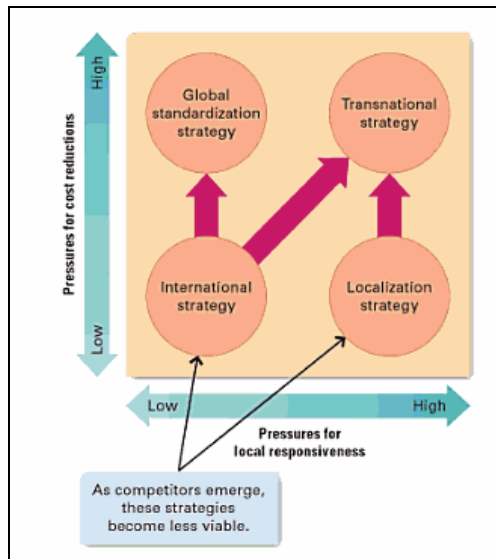


Figure 22: Changes over Time (Source: Hill & Jones, 2012, p. 285)

On the other hand, lack of proactive steps taken as to significant reduction of cost structures might turn out the Achilles heel also for current market leaders, since over time competitors *do* come, and then the company is doomed. A vivid example is world-known giant *Xerox*. Its competitors, Japanese companies like *Canon* managed to invent devices similar to *Xerox's* patents, but priced them below the innovator's products. As a consequence, *Xerox's* global market share was rapidly eroded by competitors. Thus, proactive reduction of the cost structure are the winners' strategy (Hill & Jones, 2012, p. 160).

On the other hand, disregarding certain issues (e.g. ethical or environmental problems caused by standardization and outsourcing in host countries) may partially or completely ruin the company's reputation. In the highly digitalized world of today (due to its ubiquitous Internet, social media, etc.), negative reputation may mean automatic loss of a huge piece of the global market pie. A world-known example is *Nike* and its "sweatshop" production in Asia (Morris & Lawrence, 2010, pp.946-947).

Adaptation to local peculiarities (cultural, religious differences) is evident, in view of the accelerated expansion into distant markets. E.g. in recent years, Western European, Japanese, and U.S. corporations increased their investments into nations of Eastern Europe, Latin America, and Southeast Asia (Hill & Jones, 2012, p. 148). Yet, in view of significant changes in customer preferences overseas, rapid capitalization on the advantages of growth opportunities in the above mentioned markets is possible only through adaptation to local requirements. Hence, H 1 was supported.

H 2: Bidirectional Flow of Technology

Personal analysis and literature review on the global expansion of SMEs and MNCs as well as their preferred choice of the MEM strategy reveal that very few sizable companies today have strictly regional markets. Many SMEs, start-ups, or even industries are born today with a global outlook. The establishment of overseas subsidiaries to serve local markets and to outsource manufacturing in order to take advantage of low-cost labor or highly skilled

workforce are primary scenarios preferred internationally (**Level 1, Assembly**, and **Level 2, Adaptation Strategies**) (Leonard, 1995, p. 257).

In the first line, this phenomenon is related to the uncertainty of losing technological KH, or tacit knowledge. Therefore, transferring capabilities at **Level 1** and/or **Level 2** boils down only to transferring compatible physical and management systems (or the mere duplication of technological capabilities of the original technology source in combination with training and spillovers). **Level 3 (Product Redesign)**, on the contrary, which necessitates significantly much more effort and attention to teaching a recipient company about the science that underlies the technology or company culture, is preferred exclusively in the case of **WOS** or **SA** aimed at securing technological KH (Leonard, 1995, p. 257; Liebeskind, 1996, p. 93; Hilmi et al., 2007, p. 246).

Level 4 (Independent Design), which implicates that the recipient country possesses exactly the same science base and is capable of interacting with the original source as an equal partner (**bidirectional technology flow**), seems, in all probability, to have been reached, only in very rare cases. Primarily because most innovations are controlled and strictly supervised by parent companies (or global market leaders) that attempt to prevent the outflow of technological KH by all means (Liebeskind, 1996, p. 93). Thus, the real relationship transformation from the parent-child to the parent-parent or equal creators (with cross-licensing as an insurance against technology outflow as an alternative solution) is rather a big rarity and is more indicative of SMEs, *not* MNCs (Pellicelli, 2003, p. 12).

In addition, two-way technology flows have strategic differences all over the globe. While developed nations attempt to control K creation, developing countries are still looking for technology access (Hilmi et al., 2007, p. 246). Industrial restructuring and updating towards higher value-adding activities (the resultant outcomes of FDI), on the contrary, are characteristic of both industrialized and emerging economies. Thus, in view of numerous synergy effects, FDI today are more complements (or enrichment) rather than mere substitutes of the obsolete (Hilmi et al., 2007, p. 247).

Another interesting revelation of the current research consists in the asymmetry of K distribution among nations. Most **future-oriented technologies** or **tacit knowledge** is located in **developed nations** (prevalence of experience, managerial and technological skills and KH, global brands, intellectual property), whereas **developing countries** are mainly characterized by production process capabilities, networks, and organizational structure (defensive strategy) (Hilmi et al., 2007, p. 243).

Still another interesting revelation consists in the fact that rapid growth of emerging nations is primarily enabled *not* only by their increased exports of raw materials but also by their focus on proper knowledge management and adaptation of education standards to global ones, constant technological updating and R&D. Hence, the gradual shift towards knowledge-intensive production is a global trend. Moreover, modern IT-based solutions, primarily the Internet with its digital and online libraries, distance learning opportunities as well as social media and communities of practice, serve as the infinite source of invaluable information which can secure quantum leaps towards innovation and sustainability both for developed and developing nations.

Culture change and **constant learning** are therefore indispensable prerequisites for securing growth in the globalized and digitalized world of today. As a vivid example serves Procter & Gamble and its Open Innovation which aim at unleashing global creativity and innovation to secure organic growth and sustainability (Huston & Sakkab, 2006, pp. 1-3). By the way, the P&G's Connect & Develop strategy is also widely used in the public sector. Primary knowledge-inhibiting (or sustainability-inhibiting) activities, on the contrary, include limited problem-solving influenced by only past solutions, inability to innovate using new methods and tools, limited experimentation, biased evaluation of external knowledge (new technology, customer feedback, etc.) (Leonard, 1995, pp. 35-41).

In the final analysis it should be pointed out that **one-way transfer** of K and technology is only a short-term solution to a long-term problem (competitors or innovators *will* come sooner or later). Consequently, technology outflow will remain one of the basic problems of WOS for generations to come (Leonard, 1995, p. 222). Proactive thinking, on the contrary, based upon technology share and co-creation are likely to secure more radical and more lucrative solutions. Thus, H. 2 was supported.

H 3: Experience

As a matter of fact, the choice of MEM was always heatedly discussed in literature. According to numerous research, companies tend to be reluctant to adopt a FDI mode, when they first enter a foreign country. Yet, as soon as the barriers of language and culture are overcome, the likelihood of FDI increases (Hill et al., 1990, p. 117). Expansion overseas could be compared to the following proverb: "*Get your toe wet first and see how cold the water is.*" The globalized world with its partially standardized preferences and expectations facilitates FDI significantly. Yet, experience with the host market remains of utmost relevance to the choice of MEM.

Just as mentioned above, the choice of MEM is always related to the company's *goals* (expansion, profitability, opportunity, and/or control), *risk perceived* (decision-making under uncertainty), and *contextual specificities* (unexpected outcomes enabled by *learning*, emergence of new ideas, insights, etc., and the *environmental opportunities* offered by the host country) (Hilmi et al., 2007, pp. 244-245). Yet, learning remains an indispensable determinant for securing success of a MEM.

According to the Internationalization Theory, *market uncertainty* shapes the firm's strategy for an international expansion because of lack of experience, demand, competition and the market itself, thus, the inability to estimate the present and future market factors. As a result, corporations prefer a more conservative or learning approach (Johanson & Vahle, 1977). In terms of entry modes, firms normally prefer exporting at the stage as opposed to the later stage of the product life cycle (Johanson & Vahle, 1977).

Moreover, literature overview shows that MNCs which enter overseas markets pursuing the IJV strategy outperform those that enter foreign markets by WOS (in whole). This, in turn, confirms the relevance of **experience** or gradual accumulation of K (and, assuredly, capital) in overseas markets as well as knowledge of customer preferences, customer and supplier databases, etc. (Chan, 1995, p. 39).

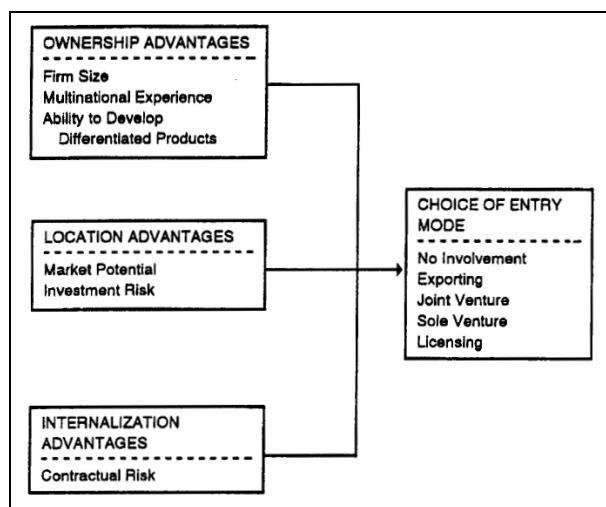


Figure 23: Entry Choice Factors (Source: Agarwal & Ramaswami, 1992, p. 5)

In addition, substantial extension or rethinking of the overall international strategy is a must, primarily because of the necessity to consider organizational learning as one of the basic sources of new insights into organizational functioning or efficacy of internal K transfer (Eisenhardt & Santos, 2000, pp. 1, 25) as well as the relevance of searching for and coordination of capabilities dispersed throughout the larger social and economic systems to capitalize on benefits of global specialization (Garzarelli, 2006, p. 15). As opposed to developed countries which primarily target strategic asset acquisition (brand names, new

technologies and ideas), developing countries aim at technology-sourcing and learning (Hilmi et al., 2007, p. 246).

Yet, K (market K, in particular) and market experience are sometimes very difficult and expensive to obtain (Lymbersky, 2008, p. 25). Therefore, K should be necessarily embedded not only in people as primary carriers and creators of intellectual property, but also in business processes, methods and technology to enable easy access to invaluable insights and capacity for growth. As a result, an integrated approach towards K, organizational resources and organizational capabilities and processes is the outcome of dynamic adaptation on a global scale, K remaining the company's primary strategic asset underlying existing and would-be products. Experience as part of K manifested through physical ability to act and accomplish problem-solving tasks applying a required set of skills and insights, is, consequently, an indispensable prerequisite to secure success of the ME choice. Thus, H. 4 was supported.

H 4: WOS vs. IJV

First and foremost, relentless onslaught of globalization, and liberalization of world trade intensify the competing potential between the two primarily, but strategically fundamental options – WOS and IJV. Each of the two has both advantages and disadvantages as to the degree of control over operations, resource commitment, and risks to bear (Chan, 1995, p. 37; Onkvisit & Shaw, 2008, p. 267).

According to results of numerous empirical and statistical research, **the size of the corporation** as well as its **multinational involvement** are critical factors for choosing either a WOS or IJV. The size of the corporation is normally indicative of its potential to cover transaction costs (Madhok, 1998, p. 260). Thus, only MNCs dare to enter the global arena considering a WOS or an IJV.

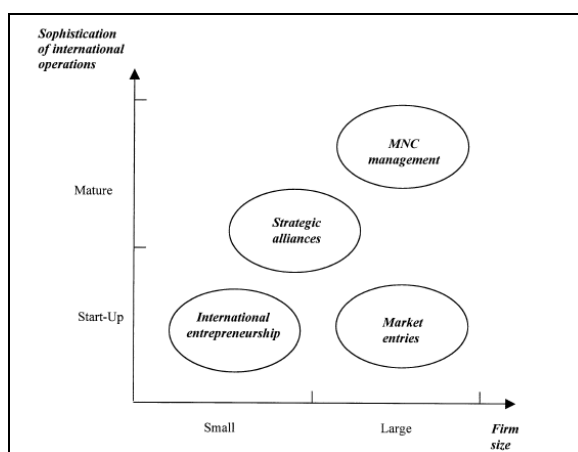


Figure 24: International Operation by Company Size (Peng, 2001, p. 810)

In addition, SA based on contracts have different scenario outcomes as opposed to those based on ownership of capital, whereas the typical value chain of the local firm may be effected by foreign capital only in part (R&D, production, marketing and sales) (Pellicelli, 2003, p. 7). Thus, confirming the importance of company size for the choice of MEM.

Yet, despite all the benefits of 100% ownership, control and higher profitability ratios of the WOS strategy, the IJV strategy may equally perform as its primary counterpart. According to Lei & Slocum (1992, p. 81), IJV is the most appropriate strategy for entering foreign markets, primarily because of political and legal uncertainty and risks. In addition, it is also confirmed by the historical choice of MEM in cooperation with the communist world or other nations with political instability (Pellicelli, 2003, p. 10).

On the other hand, the principal drawback of IJV is, assuredly, the “melting pot” of managers with different nationalities, backgrounds, experiences, practices, priorities, abilities, and even objectives who attempt to combine joint resources and management approaches to reach common goals. These discrepancies (asset management, asset separability, and asset appropriation risks) entail not only a long negotiation, coordination and planning process, but also problems in daily operations, thus, causing adverse effects on performance indicators (and not only at the initial stage of joint operations) (Chan, 1995, p. 42; Pellicelli, 2003, p. 10).

Nevertheless, when it comes to using IJV for the first MEM, most of MNCs *do* succeed applying this strategy. Yet, upon gaining sufficient experience abroad, most companies terminate their IJV operations (Chowdhury, 1992, p. 115; Hilmi et al., 2007, p. 244). Therefore, the IJV strategy is primarily intended for a *newcomer* and as a *limited duration* (or rather short-term) strategy to promote the firm’s brand name and learn from partners, competitors, and customers (small-scale entry) before upgrading the ownership status (M&A as a post-entry strategy) or exiting the market (Peng, 2001, p. 814). WOS, on the contrary, is indicative of competitive capabilities and surmounted market barriers, thus, experienced players.

The results of the above mentioned analysis are summarized in the following tables.

	Modes of Entry				
	Exporting	Contractual Agreement	Joint Venture	Acquisition	Greenfield Investment
RISK	Low	Low	Moderate	High	High
RETURN	Low	Low	Moderate	High	High
CONTROL	Moderate	Low	Moderate	High	High
INTEGRATION	Negligible	Negligible	Low	Moderate	High

Table 7: Risk/Return/Control/Integration (Source: Kumar & Subramaniam, 1997)

In view of their relative high levels of outcomes (high return, high control and moderate integration), IJV are gaining much popularity. E.g. one third of all fast-growing companies are involved in IJV today (Kotelnikov, 2001). Moreover, IJV prove an effective MEM also for SMMs with insufficient finance and management skills to gain access to supplies of raw materials, local production facilities, technology, local expertise, and distribution channels.

Of late, temporary IJV with host governments (state-owned or national companies) have gained relevance (e.g. civil engineering projects, new global technological ventures, etc.). Government restrictions (thus, lack of control, high risk and uncertainty) also prevent some potential investors from exporting and establishing a WOS. Therefore, supply of KH through IJV is a viable way of obtaining an equity stake in a foreign market (Kotelnikov, 2001).

On the other hand, IJV are very difficult to integrate on a *global* scale, which, in turn, requires substantial cross-border trading and the resultant problems related to inward and outward transfer pricing and the sourcing of exports. Further issues include guidelines on cash and working capital, management of exchange rate and remittable profits (Guterman, 2002, pp. 45, 66, 182).

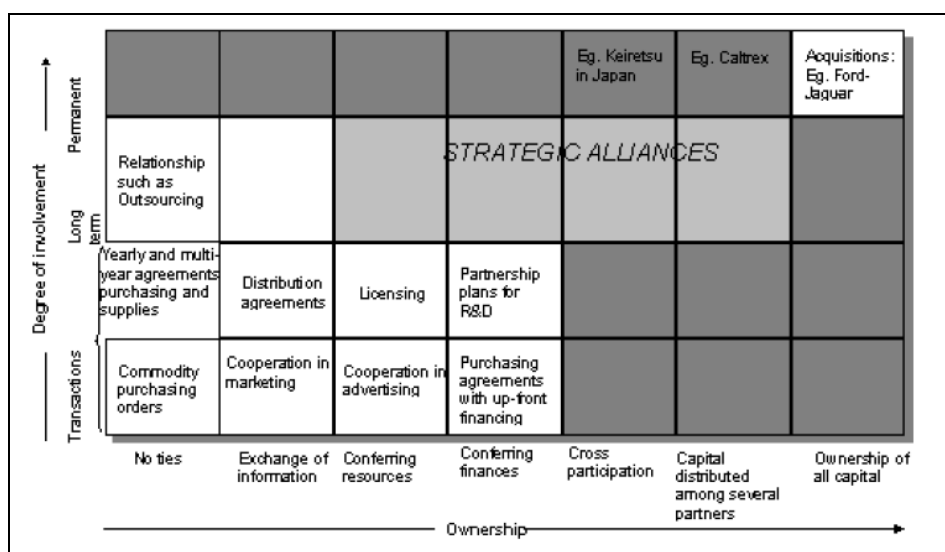


Figure 25: The Spectrum of Agreements (Source: Pellicelli, 2003, p. 9)

M&A, on the contrary, are characteristic of firms with valuable strategic assets which intend to increase their efficiency quickly (large-scale entry, or first-mover advantage) (Hill & Jones, 2012, p. 311). Yet, this strategy is, on the one hand, relatively costly, and is therefore more relevant for MNCs (Hilmi et al., 2007, pp. 248-249). On the other hand, in view of complexity of internal processes, primarily integration and coordination, as opposed to external benefits such as cost efficiency and a greater market power, M&A have a rather high

rate of failures. Consequently, a gradual transition through the IJV is a much more reasonable and realistic scenario.

In addition, the results of numerous research indicate that MNCs that chose the IJV strategy were larger than those that chose WOS. Moreover, those corporations that chose IJVs have a significantly larger number of WOS than those that used the pure WOS strategy (Chan, 1995, p. 41). In other words, multinationals with a high degree of multinational involvement tended to choose the IJV strategy as the strategy for multiple entering overseas markets instead of opening up WOSs (potential acquisition targets and IJV opportunities vs. GFI) (Raff et al., 2007, p. 1). In addition IJV, SA, IJV in particular, served as a transitional stage from partial liability (IJV) to 100% ownership (WOS) through acquisition (e.g. *Ford's* acquisition of *Jaguar*) (Pellicelli, 2003, p. 9).

Consequently, a particular MEM should *not* be view in isolation. It is also necessarily related to the overall strategic position of the corporation. Moreover, multiple entries help build core capabilities and learn from previous entry experience from various countries simultaneously, thus, multiplying the corporation's tacit K or its basic strategic asset (Peng, 2001, p. 813). Moreover, R&D-focused entries provide access to innovations resident in host countries, thus, generating information spillovers that can be further used as opportunities for organizational learning and growth in the parent corporation as well (both "pushed" by firm-specific advantages and "pulled" by resources and capabilities of the target market to develop new advantages) (Peng & Wang, 2000, p. 80; Peng, 2001, p. 814).

In view of the complexity and cost-effective nature of SA, the latter are primarily characteristic of firms in ***industrialized nations, short-term durations*** of contracts as well as ***creation of new products or technologies*** as opposed to the distribution of the existing ones (Bartett, 2009, p. 107). Moreover, SA are an excellent alternative to bypass constraints to cross-border M&A in specific industry sectors. Elimination of restrictions normally leads to the full-scale integration (Kotelnikov, 2001).

On the other hand, SA are a must for some industries, since major innovations and breakthroughs are grounded on interdisciplinary or even inter-industrial advances. Hence, critical resources and capabilities to conduct its own effective ***R&D*** are extremely difficult to secure by one single firm, even if it is a market leader globally (Huston & Sakkab, 2006, p. 6). Moreover, ***product life cycles*** have shrunk significantly of late. Therefore, in order to stay competitive, an innovation is a must. SA are very typical for *telecommunications, information technology, electronics, specialty chemicals and pharmaceuticals* (transfer of technology). In addition, pooling resources also secures not only ES, but also significantly reduces risk.

Consequently, SA are extremely advantageous for high-risk and high-cost projects (primarily, when it comes to R&D) (Kotelnikov, 2001).

On the other hand, **R&D intensity** is a less relevant issue for MNCs choosing between the WOS or IJV strategy (Chan, 1995, p. 37). In general, WOS showed higher R&D intensity than in the case of IJV. Yet, in view of rising Open Innovation opportunities coupled with rather insignificant changes in the respective values resultant from numerous research, the author cannot conclude that the IJV strategy requires lower R&D intensity than WOS (Chan, 1995, p. 41). Thus, H 4 was supported only partially.

H 5: Outsourcing

During the current financial crisis, cost-effectiveness plays a major role. The premium sector, on the contrary, remains as always less susceptible to economic fluctuations (Spiller, 2010, p. 38). Yet, just as mentioned above, to compete on a global level, companies have to proactively (thus, constantly) reduce costs. The *Boeing* Company, e.g. uses 132,000 engineered parts that are produced by 545 suppliers from all over the globe. In general, 30% of its 777 commercial jet aircraft (by value) is built overseas. Moreover, for the production of its most recent jet airliner, the 787, *Boeing* scheduled to outsource 65% of the total value of the jet (Hill & Jones, 2012, p. 147).

IKEA, a proactive global leader, aims at reducing the price of its offerings by 2%-3% per annum, which implicates constant cost cutting, and, thus, outsourcing *each* item (Hill & Jones, 2012, p. 170). Therefore, the highest profitability of the final product enabled by the best outsourcing suppliers from all over the world implicates both the optimal cost-effectiveness and high quality ratio for the above mentioned global leaders.

Nevertheless, just as indicated above, the linear model of innovation (internal R&D) is now being gradually replaced by Open Innovation, i.e. innovation through collaboration and co-creation of all stakeholders (both internal and external) (global outsourcing of R&D, so to say). This strategy is used to significantly reduce time for new product development intensified by shortened product life cycles. As an illustrative example serves the above mentioned *P&G* and its *Connect & Divide Strategy* or the “*proudly found elsewhere*” approach which secured 35% of the corporation’s innovations from outside the company (Huston & Sakkab, 2006, p. 2).

In particular, the corporation acquires strategic assets (*licenses* and *patents*, as a key indicator of K) from all over the globe and normally from already existing solutions from other industries: independent inventors, lead users, communities of practice, etc. (Huston &

Sakkab, 2006, p. 4). As a result, R&D costs are reduced significantly, products are up-to-date and in conformity with customer preferences, or easily adapted to local requirements (even customized, which is easily affordable for global market players).

In addition, apart from purchasing licenses and patents, modern innovation theory also considers *learning* as the primary source of innovation, K creation, thus, sustainability. This theory is based on the assumption that most innovations *do* exist already as finished solutions, but in different industries or spheres of life. The only thing that is required is to redesign or adapt existing forms of K to specific requirements. And this is exactly what P&G is doing: searching for creative and innovative solutions from different industries and, if required, adapting or refining them (Huston & Sakkab, 2006, pp. 8-9).

As a result, the role of R&D tends to be seen more as a *problem-solving activity* initiated from customer preferences and customer feedback (complaint management) rather than as a sheer act of discovery (Huston & Sakkab, 2006, p. 1). Hence, its primary task boils down to finding the best solutions, refining them and capitalizing on them. Moreover, the market of global talent or knowledge, *Innocentive*, aims at establishing the market of most valuable solutions (the most valuable marketplace for major global leaders), which further confirms the primary importance of K as strategic asset for securing success and sustainability in the globalized world of today (Huston & Sakkab, 2006, p. 6).

Consequently, market players are looking for new ideas or K (i.e. the source of sustainability), whereas startups or emerging companies are still seeking physical resources. Anyway, SMEs gain invaluable K when entering foreign markets. An alternative for acquiring this experience can be gained only from export intermediaries in order to facilitate the internationalization of smaller companies. Yet, “renting” K from others may again prove a rather risky enterprise (Peng, 2001, p. 814). On the other hand, capability-related issues (or experience, skills, and K) rather than the level of transaction costs and the efficiency of the transaction under the uncertainty of opportunism play a much more decisive role in the choice of MEM (Madhok, 1998, p. 259).

Apart from outsourcing, M&A are thriving these days too. Generally speaking, acquisitions as a fast move strategy secure a fast and significant market presence, create value and increase profitability (Hill & Jones, 2012, p. 212). In such a way, domestic monopolistic restrictions are broken by international expansion. The ordinary scenario of M&A runs as follows: a traditional market research followed by the purchase of a startup or an emerging company with a promising product or technology, and its subsequent integration in one’s own

portfolio (*Cisco*), or, alternatively, diversification into new industries (*Google*, *Walmart*) (Kotelnikov, 2001; Hill & Jones, 2012, p. 176).

Yet, the current trend is, assuredly, related primarily to the recessive economy in most countries of the world. It is obvious that in view of the difficult financial situation all over the globe, only market leaders, or cost leader strategists, may afford both to survive and even to thrive (Böhner et al., 2008, p. 16).

In particular, the global crisis makes equity affordable for much-much less, which intensifies the strategic relevance of M&A. Bankruptcy of numerous SMEs worldwide lead to repossessions and industry restructuring. Therefore, strategic purchases aimed at increasing market power (even globally), which might have been extremely difficult to afford a few years ago, become a real bargain. E.g. *Adidas* attempted to purchase *Ashworth Golf* to strengthen its golf product line for years. The company's dream came true only back in 2008 and at the price twice as low as two months before the actual purchase. Two other examples are: *Unilever* and its acquisition of *Tigi* (2009) and *P&G* and *Art of Shaving* (premium segment) (Böhner et al., 2008, p. 16).

Consequently, the recession made clear: *winners are winners even in difficult times*, and primarily because of their strategic approach towards K, KM, acquisition of KH and other strategic assets, as well as adequate market research on a global scale. Thus, H 5 was supported.

6. Conclusion

In the final analysis, it should be pointed out that in the knowledge-based society of tomorrow with its primary focus on knowledge, *not tangible assets*, as strategic assets and knowledge workers as carriers and creators of strategic intellectual property, MEM will be primarily reduced to K transfer or acquisition of strategic assets (primarily, invaluable K), whereas physical assets, machinery and equipment, which were prioritized by the industrially-based economy, will become only second-rate.

Proper leverage on intangible assets will make countries or individual companies more knowledge-competitive on an international scale. In addition, this development will eradicate asymmetries in distribution of strategic physical assets between developed and developing countries, thus, intensifying global competition, making K the primary (*or even only*) currency in business environment.

Thus, within the framework of globalization, the classical question *to buy or to build* acquired a new dimension: a complementary “merger” or “SA” of both: *to buy* and *to build*. Hence, a typical scenario for MNCs is: (1) to start with the IJV strategy (the intermediary MEM), jointly develop new products, acquire host market K, new experience and connections, and use the residual capital for securing cost effectiveness through production outsourcing and specialization all over the globe, (2) parallel expansion through exporting enabled by economies of scale and scope (complementary strategies), (3) to merge or acquire the IJV partner and further expand its influence abroad through changing its proprietary status, and so forth (naturalization of the subsidiary). Thus, a unified modal choice proves always much more beneficial.

In view of limited resources, asymmetric information, and lack of competitive advantage, SMEs are forced to start with exporting. Their further development depends primarily upon the manager’s insights into the market dynamics, global trends and opportunities and the ability to capitalize on capabilities.

Yet, in both cases, constant change management (learning and adaptation to dynamic environmental changes) is the only source of SCA. Furthermore, globalization, ubiquitous Internet access, and international Internet marketing, in particular, will further intensify the relevance or even necessity of foreign MEM, making it the only viable growth option as compared to the mere presence on the regional level. The key challenge of foreign MEM will be then associated with adding value to already existing products (both tangible and intangible) through proper management of K assets as well as creation and implementation of novel ways of K transformation.

As a consequence, K, the primarily source of wealth and upliftment for millennia, will be dependent only upon brainpower, *not machine power*, as its strategic resource. Therefore, cooperation, not competition, is likely to be the most viable solution of tomorrow that will not only reshape entire industries, global economy, politics, and social structures, but will also secure organic growth, sustainability, emergence of innovative approaches towards creation and share based on democratic principles, human values to solve primary socio-economic issues such as well-being and happiness.

7. Further Research

The emergence of the global electronic marketplace as well as its ubiquitous presence, gave birth both to new challenges and numerous risks. Explorations of these issues in the context of unsurpassed characteristics and capabilities of this unique marketplace as well as unique K creation and K transfer opportunities are a rather promising venue for further research.

On the other hand, the importance of the physical location of firms should not be overlooked. Although the Internet enables markets to be increasingly interconnected and easily accessed, the dominance of the traditional geography-related clusters remains undisputable. Therefore, a double strategy (physical and digital) is a must. The Internet should help markets expand faster and provide market players all over the world with all the relevant market K to secure easier, more effective and multiple choice of MEM. Thus, K spillovers secured by communities of practice, actions of competitors and/or other stakeholders (that are, by the way, so easily traced in the Internet) could be used as the source of non-codifiable information. Moreover, the scope of this K increases exponentially and simultaneously all over the globe. The big challenge is, thus, reliable sources of information and/or fast information processing.

On the other hand, the ability to codify technological KH or invaluable insights becomes a real problem of the knowledge-based society. Consequently, further research is required in this field too.

In addition, the emergence of K as the primary strategic asset of a company and the relevance of Open Innovation and communities of practice lead to the supposition that K might soon turn into a new currency. According to Thomas A. Stewart, progenitor of the intellectual approach to managing products, processes and people, and his concept of intellectual capital, money will soon disappear and is likely to be substituted by information or intangible capital (Stewart, 2001). Even accounting or buying-selling transactions will be effected for information or intangible assets, not for money.

In the Information Age, the era of constant change, wealth will be created as the product of K (probably even in the forms not known today). Thus, K as the source of organic growth and sustainability will have to circulate at every level of a business to secure permanent improvement of HC, structural capital (packaged HC or the organizational capabilities), and customer capital. As a result, the relevance of search for talents and K transfer coordination as well as experimentation with novel ways of K share and K creation could be considered as topics for future research.

Yet, business environment of tomorrow is being shaped *today*, primarily by proactive managers and lead users (Pötz, 2005). The solutions of the past become, therefore, in most cases obsolete. Hence, the importance of organizational learning (participation and co-creation) enabled by IT-based solutions coupled with the intellectual capital approach to managing K are indispensable to understand the company's bottlenecks and attempt to find creative alternatives (Wigg, 1995).

As a matter of fact, K creation "*is still at an infant state*" (Nonaka & Nishiguchi, 2000, p. 3). Consequently, it requires more creativity and more innovative approaches towards solving every-day business problems (the choice of MEM, in particular). As a result, product development and product-based competition turns into a second-rate goal (Leonard, 1995, p. 3). The company's progress and sustainability depend, on the contrary, upon ongoing refinement and development of K creation processes as well as advancements towards thinking not in terms of money or products, but in terms of *knowledge* and *quality transfer*. Yet, it is probably the task still for generations to come...

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Anhang 1: Abstract

The main issue of the paper is to prove that these days the Knowledge is a strategic asset in choosing a market entry mode.

In the rapidly growing, globalized, and partly digitalized economy of today, some organizations are forced to expand. The world is constantly changing; therefore the organizations have to move with the stream. If firms decide to move abroad, the decisions concern the following aspects: the size of the foreign market (present vs. potential), the purchasing power of the target market (present vs. future wealth), and the suitability of the product for the chosen market, nature of indigenous competition (Koltenikov, 2001).

Before the final decision is made, it is necessary that the ME concept contains numerous issues, challenges and problems. The selection of the target market and the product for sales constitutes the first stage of exploring a new market. It is based on internal and external analysis (SWOT): information on customer preferences and social structure of the target market, potential competitors (especially, the presence of global players), suppliers, scarcity vs. abundance of resources, political regulations, trade barriers, etc. Subsequently, a respective market entry mode (MEM) is chosen (Kotelnikov, 2001; Kotler & Armstrong, 2009).

Section 2 deals with different Forms of market entry, based on different market entry strategies, it shows which MEM is suitable.

These days the Knowledge is seen as a source, the key driver and new product (Leonard, 1995, p. 3). Knowledge helps the get fast access to new chances to eradicate poverty, to secure organic growth and constant development, economic stability, and sustainability (Dahlman & Utz, 2004, p. 10).

In fact, only constant learning and striving for perfection secured by K assets may lead to fundamental improvements (effectiveness, efficiency, and top quality). The time of the “Working Smarter”, not the “Working Harder” Strategy finally arrived (Caballero & Hammour, 1994, pp. 1350-1351).

The main issue is to learn how to search, store, create, share and use knowledge properly.

There exist numerous classifications of knowledge: Nonaka & Takeuchi, 1995, p. 59 discriminate between fundamental types of Knowledge: tacit (stored only in the heads of people) and explicit (stored in books, CD's, etc.).

In addition, Knowledge can also be viewed from the following perspectives: Resource Based Theory, Organizational Capability Theory and Knowledge Based Theory (Leonard, 1995).

These theories serve as the research foundation for the current thesis, the author applies the premises of the aforementioned theories to investigate the following issue: Can Knowledge be regarded as a company's strategic asset?

Section 4 deals with different classifications of Knowledge, which are detailed analyzed and it is shown what their contribution for choosing a market entry mode is.

Anhang 2: Zusammenfassung

Die Arbeit behandelt das Thema „Knowledge as strategic asset in choosing a market entry mode“ – „Wissen als ein strategischer Zug im Auswahl der Markteintrittsform“.

In dieser schnell wachsenden, globalen und digitalen Wirtschaft sind Unternehmen gezwungen zu expandieren. Die Welt verändert sich konstant und somit müssen sich die Unternehmer diesem Lauf anpassen. Krause, 2010, s. 9 hat gesagt, dass nichts außer Veränderung konstant ist. Wenn Firmen sich für neuen Markteintritt entscheiden, müssen die folgende Punkte beachten: die Größe des Zielmarktes (gegenwärtiger vs. potentieller), die Kaufkraft des Zielmarktes (gegenwärtige vs. zukünftige Kraft), Produktanpassung im Zielmarkt und die vorhandene Konkurrenz (Kotelnikov, 2001).

Vor der endgültigen Wahl des Zielmarktes muss der Markteintrittskonzept viele Faktoren, Herausforderungen und Probleme beinhalten die berücksichtigt werden müssen. In erster Linie muss der Zielmarkt erforscht werden, basierend auf der internen und externen SWOT Analyse: Kaufkraft, soziale Struktur, potentielle Konkurrenz, Lieferanten, Ressourcenknappheit, politische Regelungen, etc.

Im zweiten Teil der Arbeit werden elf verschiedene Markteintrittsformen erklärt und verglichen. Basierend auf vier verschiedenen Markteintrittsstrategien wird dargestellt, welche Formen für welche Firmen in Betracht gezogen werden.

Abgesehen von all diesen Faktoren wird der heutigen Zeit Wissen als die Quelle, der Schlüssel und das neue unentbehrliche Produkt gesehen (Leonard, 1995, s. 3). Wissen ermöglicht schnellen Zugang zu neuen Chancen die Armut zu bekämpfen, Organisationswachstum und konstante Entwicklung zu sichern und ökonomische und wirtschaftliche Stabilität zu gewährleisten (Dahlman & Utz, 2004, s. 10). Das ständige Lernen und Perfektion gewährleistet durch das Wissen, führen zu einer fundamentalen Verbesserung (Effektivität, Effizienz und Qualität). Die Zeit der intellektuellen Arbeit statt schwerer Arbeit ist gekommen (Caballero & Hammour, 1994, ss. 1350-1351).

Das Wichtigste ist: Wissen zu suchen, zu erhalten, zu entwickeln, zu teilen und richtig anwenden.

Es bestehen viele Klassifikationen von Wissen. Nonaka & Takeuchi, 1995, s. 59, unterscheiden zwischen dem stillschweigendem (nur in den Köpfen vorhanden) und dem explizitem Wissen (in den Büchern, auf den CD's, etc. vorhanden).

Wissen wird auch von den folgenden Perspektiven betrachtet: Ressourcen basierende Theorie, Organisatorische Fähigkeitstheorie und Wissen basierende Theorie (Leonard, 1995). Diese

drei Theorien dienen als Forschungsfundament für diese Arbeit. Die Frage: Kann Wissen als strategischer Zug für Unternehmer gesehen werden, ist untersucht.

Im vierten Teil der Arbeit sind elf verschiedene Schlüsselfaktoren des Wissens vorgestellt, detailliert analysiert und es wird gezeigt was ihr Beitrag für die Wahl der Markteintrittsform ist.

Anhang 3: Curriculum Vitae

PERSÖNLICHE DATEN

Name:	Ivana Music
Geburtsdatum, -ort:	13.03.1980 in Bosnien und Herzegowina
Staatsangehörigkeit:	Österreich

BILDUNGSWEG

2002-2012	Universität Wien, Studienrichtung: Internationale Betriebswirtschaft in Wien 1210 Spezialisierung: ✓ HR Management ✓ Organisation und Personal ✓ Internationale Unternehmensführung
1999-2002	HAK Aufbaulehrgang BFI in Wien 1050 Diplomabschluss
1996-1999	Fachschule für wirtschaftliche Berufe in Wien 1170 mit Abschluss
1995-1996	Polytechnischer Lehrgang in Wien 1030
1991-1995	Hauptschule in Bosnien und Herzegowina
1987-1991	Volksschule in Bosnien und Herzegowina

BESONDERE KENNTNISSE

Sprachen:	Kroatisch (Muttersprache) Deutsch (2. Muttersprache) Englisch (In Wort und Schrift) Serbisch/Bosnisch (In Wort und Schrift) Französisch (Grundkenntnisse) Spanisch (Fortgeschrittene Grundkenntnisse)
EDV:	ECDL-Zertifikat SAP (gute Anwenderkenntnisse) Internet, Outlook (Sehr gut) 10 Fingersystem (Sehr gut)

Wien, im Jahr 2012