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- encouraging and assisting basic and applied research activities that advance knowledge of global business
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- facilitating the interdisciplinary dialogue concerning global business and global entrepreneurship issues as they relate to academic, business and government sectors.

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Physical Vanity across Cultures: Measurement and Validation

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Abstract: Physical vanity relates to a person’s, often excessive, concern for physical appearance and/or positive view of appearance. Netemeyer, Burton, and Lichtenstein (1995) developed a scale to measure such a physical vanity dimension. The study presented attempted to establish measurement invariance of this physical vanity scale across three extremely diverse cultures with samples from China (N= 502), India (N= 156) and the USA (N= 338). The results from a series of confirmatory factor analyses indicate that the physical vanity scale is applicable to culturally differing countries. Implications of findings are also discussed.

Introduction

It is generally believed that Western culture is dominated by an obsession with physical appearance and beauty (Netemeyer, Burton, and Lichtenstein 1995). However, the concept of vanity is neither new nor limited to Western culture. There is evidence to suggest that the use of products to enhance beauty and discussion about beauty among philosophers goes back to historical times and spans across cultures. Egyptians who lived 4,000 years BC are reported to be the first users of cosmetic products (Dureja et al. 2005). Archeological discoveries dating from between 2,000 BC and 1,200 BC as well as those from the second century AD suggest both ancient Egyptians and Romans commonly used cosmetic products to enhance beauty (Evershed et al. 2004, Walter et al. 1999). Western philosophers like Aristotle and Hume have commented upon vanity (Watson, Rayner, Lysonski, and Durvasula 1999); at the same time ancient Indian system of medicine, Aryuveda, has specific reference to herbs and formulations that can be used to enhance beauty. The common adage that beauty is in the eyes of beholder suggests that the concept of beauty is more than just a universal perception. What is considered beautiful might depend on or reflect culture-specific preferences. For instance, can we accept that the concern for physical appearance and beauty is likely to be a major driver of consumer behavior in cultures that differ greatly from each other in terms of history, ethnic mix, economics, religion and philosophy? This concern probably is also responsible for present-day success of beauty industries in the countries surveyed in this study (China, India, and the US). Differences in physical beauty perception impact such
industries like: perfume, fashion, cosmetics, weight control, and in the last quarter century cosmetic surgeries, that cater to widely differing beauty needs among consumers in various parts of the world.

On the other hand, with the globalization of markets, there is an increasing need for marketers to understand global consumers – their converging characteristics and preferences. While marketers seek to expand their reach into overseas markets, they find it increasingly difficult to build brand equity partially due to their lack of knowledge about consumer characteristics and preferences across cultures. Adding to such difficulties is the lack of appropriate theories, concepts, and measurement tools that can be used to better understand consumer characteristics across cultures (cf. Sekaran 1983). Given that modern consumer research and theory building have largely been conducted in the West, a recurring concern is the need to verify if the same theories and findings are applicable to other non-Western cultures. It is within this context that the present research seeks to examine measurement of physical vanity construct across three countries (China, India, and the US) to shed light on the validity of the Netemeyer, et al. (1995) scale and to assess its appropriateness in capturing true beauty perception difference across cultures.

Physical Vanity

Netemeyer et al. (1995) (NBL) define physical vanity as “an excessive concern for, and/or a positive (and perhaps inflated) view of, one’s physical appearance” (p. 612). And to measure this trait they developed the physical vanity scale and established both its reliability and validity. Yet, while pointing out that it still remains necessary to study vanity across cultures, they suggest that physical appearance and beauty is likely to be valued to a greater extent in Western societies (e.g. the US) when contrasted with non-Western Far Eastern societies, such as China and India.

While it can be argued that physical vanity represents an important universal consumer trait, research concerned with this construct is extremely limited (see Netemeyer, et al. 1995) even though the importance of this consumer trait is demonstrated by the role it plays in driving beauty related consumer behavior. That marketing practitioners recognized the construct’s importance and have long developed strategies based on vanity-related consumer behavior is obvious from the way major global industries in diverse vanity-related areas such as cosmetics (including perfume), fashion and sports apparel, as well as in medical related fields (e.g., weight loss, and cosmetic surgery), cater to the needs of consumers who seek to enhance, improve, and repair their looks and appearance. According to the 2002 Economic Census Americans spent $6.7 billions in cosmetic, beauty supply, and perfume stores in 2002 (U.S. Census Bureau 2004); this represents a 51.6% increase over the amount spent in 1997. Data released by the American Society for Aesthetic Plastic Surgery, suggests that in 2003 nearly 8.3 million cosmetic procedures were carried out in the U.S., this represents an increase of about 20% over the previous years (American Society for Aesthetic Plastic Surgery 2004). The data further indicate that liposuction was the most popular cosmetic procedure followed by breast augmentation, eyelid surgery, and rhinoplasty. According to a 2002 Roper
ASW survey, 62% of Baby Boomer women engage in some type of skin care on a daily basis; and half of that generation’s women say that they have used or intend to use skin care products so as to reduce wrinkles to help them look younger.

In a study examining the relationship between vanity and appearance-related advertising appeals, Watson et al. (1999) found a positive relationship between the two. The effect of vanity in consumer behavior is not limited to consumption of cosmetic and beauty products but encompasses a wide range of consumption behaviors as is evidenced by Hall, O’Mahony and Binney’s (2002) finding that vanity is significantly related to food-purchasing behavior as well.

Measurement Invariance Across Cultures

The first step in studying consumer behavior across cultures in a comparative context involves establishing that concepts and traits studied occur in a similar way across differing cultures and that the scales used to measure those concepts and traits are invariant across cultures. To help accomplish this, Steenkemp and Baumgartner (1998) (S & B) developed a procedure that establishes measurement invariance of scales across cultures. Mathur et al. (2001) report how valuable this procedure can be in the establishment of measurement invariance for a psychographic consumer trait such as cognitive age across diverse cultures (China, India, and Korea).

The S & B procedure requires carrying out a series of multiple-group confirmatory factor analyses with progressively more restrictive conditions. Each stage’s results dictate the actions to be taken at subsequent stages. The steps in the process are:

1. Check for equality of covariance matrices (Σs) and mean vectors (μs) across groups.
2. Establish full configural invariance, i.e., the pattern of non-zero and zero or close to zero factor loadings of the measurement instrument is identical across groups. If full configural invariance can not be established, test to see if partial configural invariance can be established, i.e., some of the loadings that were expected to be zero are in fact non-zero and/or some that were expected to be non-zero are in fact zero.
3. Establish full metric invariance, i.e., scale intervals across groups are equal. If this can not be fully established, test to assess if partial metric invariance can be established, i.e., some of the scale intervals across the groups being compared are different from others.
4. Test for full scalar invariance, i.e., measurement intercepts are equal across groups being compared. If full scalar invariance can not be established, test for partial scalar invariance, i.e., some of the measurement intercepts are not the same as those in other groups being compared.
5. Establish full factor covariance invariance. If full factor covariance can not be established, test for partial factor covariance invariance.
6. Establish full factor variance invariance. If full factor variance invariance can not be established, test if partial factor variance invariance exists.
7. Establish full error variance invariance. If full error variance invariance can not be established, test for partial error variance invariance.

In the first stage when equivalence of covariance matrices (Σs) and/or mean vectors (μs) are tested, check if covariance matrices are found to be equal, if equal there is no need to continue and go to a next stage. Equivalence in Σs across groups would imply that there are no differences and that data sets from different countries may be pooled for additional comparative analysis. However, Steenkamp and Baumgartner (1998) suggest that in most studies one might expect the cross-cultural data to show differences in covariance matrices (Σs) and/or mean vectors (μs). Therefore, one must follow the above outlined steps to establish measurement invariance.

The test for configural invariance is designed to examine the pattern of factor loadings across groups. Of all the subsequent tests in the series, the test for configural invariance has the least number of constraints. At each subsequent stage, the number of constraints imposed on the model becomes more restrictive. If at any stage full invariance can not be established across the groups being tested, the procedure calls for testing to assess if partial invariance can be established. Partial invariance is tested by freeing some of the parameters in the model. However, the selection of the parameter(s) to be set free for testing partial invariance must be guided by both empirical and theoretical considerations. Modification index (MI) is a good indicator that can be used to guide the selection of parameters to be set free at each stage as based on empirical consideration. The index shows how much the χ² will change and improve the overall fit of the model if that particular parameter is set free. Generally, parameter(s) showing large values of MI should be selected for this setting free process so as to test for partial invariance.

In addition to empirical consideration, theoretical implications should be considered in selecting appropriate parameter(s) that can be set free. Only those parameters that can theoretically be justified should be considered for setting free to test for partial invariance.

Method

Data Collection

Due to the exploratory nature of this research and lack of comparable resources (e.g. mailing lists), slightly different data collection methods were utilized in each of the three countries (China, India, and U.S.) studied. However, this should not diminish the value of this research since its primary objective was to ascertain the validity and reliability of the physical vanity construct across substantially differing Western and non-Western cultures.

China. The Circulation Bureau of the Postal Service of the Province of Shandong helped in the collection of data in China. Through their cooperation a list of magazine and newspaper subscribers was obtained and a sample of the subscribers were selected and contacted. A small monetary reward was offered to the participants (less than 1 U.S. dollar). Questionnaires were individually delivered and then returned through the Postal
Service by regular mail. In this manner, a total of 549 surveys were obtained of these 502 answered all items of the physical vanity scale and were usable.

**India.** Undergraduate and graduate university students in eastern India were recruited to assist in the data collection and instructed to ask one of their parents or another adult in their family to complete the survey questionnaire (collection of data was not a part of any class assignment). In addition, some university faculty and staff, as well as members of their family, were included in the respondent pool. Of the 195 completed questionnaires acquired in this way, 156 were usable for the present study.

**The United States.** Data collection was done by students from two universities in the greater New York metro area of the eastern United States. Questionnaires were hand-delivered by students to one of their parents, to other relatives, as well as to friends and co-workers of differing ages to ascertain participation of varying age-cohort groupings. While promised anonymity, to enable verification of the authenticity of the responses, respondents were requested to indicate their names and phone numbers on a separate sheet. Respondents were afterwards randomly contacted for verification of the authenticity of the information collected. After this verification, the identifying page was removed so as to provide respondents’ anonymity prior to any analysis being conducted (this method was consistent with the data collection method followed in India). In this manner a total of 359 questionnaires were obtained in the U.S., of these 338 were usable in the present study.

American and Indian respondents received the original English version of the survey instrument. Although English is not one of the many native Indian languages, it is nonetheless the language commonly used by those associated with higher education, both in universities, government, and business enterprises. Since Indian respondents typically belonged to families with higher education, use of an English language questionnaire did not pose any problem. Chinese respondents received a Mandarin Chinese version. Translation into Mandarin Chinese was carried out by bilingual professional translators. Back translation was used to cross check and validate translation accuracy. Disagreements between translators and back translators were resolved by mutual discussion.

**Measures**

We used the physical vanity scale developed and validated by Netemeyer et al. (1995). This construct comprises two component traits: Physical concern (PC) and Physical view (PV). Physical concern is measured by five statements (e.g., the way I look is extremely important to me) and the physical view trait is measured with six items (e.g., People notice how attractive I am). For both PC and PV, five-point Likert scales (strongly agree – strongly disagree) were used (see Table 1 for the eleven statements).
Analysis

A three-part procedure was employed to assess reliability and validity of the physical vanity scale across China, India, and the U.S. In the first part, traditional analysis comprising of traditional factor analysis, reliability measurement and correlation analysis were carried out to assess reliability of the scale within the three countries. In the second part multiple-step procedure using confirmatory analysis as recommended by Steenkemp and Baumgartner (1998) were employed to establish reliability of the two measures across societies. Finally, in the third stage correlation analyses were carried out, using other physical vanity related variables to further establish the validity of the measures across the three countries.

In the first part, exploratory factor analysis of the eleven items representing the two traits (physical concern and physical view) of the physical vanity construct were carried out separately in each of the three countries, and then done together for the total 3 country sample. In two of the three countries, two factor-solutions were extracted, each with its corresponding items as in the original scale. In case of India, the original principal component analysis extracted three factors that differed slightly from the two factor solution. A confirmatory factor analysis was carried out with a forced two-factor solution and oblique rotation. This analysis successfully reproduced the two factors (physical concern and physical view) as identified in the original scale. Factor loadings for the three countries and correlations between the two trait factors can be seen in Table 1 along with both reliability (alpha) and scale descriptive statistics. As shown in Table 1, PC and P View representing the two trait components of the physical vanity construct were comparable in all the three countries and had reliabilities ranging from .71 to .87. The mean and standard deviations of the physical concern scale were as follows: China, mean = 16.09, SD = 4.64; India, mean = 17.05, SD = 3.60; USA, mean = 17.49, SD = 3.87. The same descriptive statistics for the physical view scale were: China, mean = 16.60, SD = 5.26; India, mean = 17.29, SD = 3.94; USA, mean = 18.32, SD = 4.56.

Netemeyer et al. (1995) report that the two components of physical vanity: physical concern and physical view are related and that their correlation ranges from .02 to .54. In view of the wide variation in correlation between the two components of physical vanity, including one instance of non-significant correlation, it was decided to test the invariance of these two subscales across cultures independently. Also, NBL do not suggest assigning different weights to the various items included in their scale. Therefore, factor loadings were not constrained in any way (i.e. specific value or be equal). Thus, as long as all items loaded on the same factor being analyzed it was acceptable for these tests. Structural equation modeling program LISREL 8 (Joreskog and Sorbom 1993) was used to do the sequential confirmatory factor analyses outlined in the S & B procedure. The analytical procedure outlined by S & B was used to establish the measurement invariance of the two components of the physical vanity scale. In line with the general practice, the
overall fit of the model at each stage was assessed by using multiple indicators (Bagozzi and Yi 1988). Specifically, we used the same set of indicators used by Steenkemp and Baumgartner (1998), in addition to traditional indicators such as: $\chi^2$ and associated significance level, standardized root mean square residual (SRMR), root mean square of approximation (RMSEA), consistent Akaike information criterion (CAIC), comparative fit index (CFI), goodness of fit index (GFI), normed fit index (NFI), and non-normed fit index (NNFI). Generally, a value of 0.9 or above for CFI, GFI, NNFI, and NFI and a value of .05 or less for SRMR and RMSEA indicate a good fit of the model considered. Also, for situations involving comparisons, the lower the value for CAIC is the better the model considered better. Finally, since the samples were not matched and were not representative of respective populations, a comparison of latent means was not attempted in the present case.

**Measurement Invariance of Physical Concern Scale**

As shown in Table 2, the test for the equality of covariance matrix across the three countries ($\Sigma$s) produced a $\chi^2$ of 311.02 with 30 degrees of freedom ($p<.001$), a SRMR of 0.17, RMSEA of 0.15, CAIC of 501.60, CFI of 0.76, GFI of 0.76, NFI of 0.74, and NNFI of 0.76. These results show that the covariance matrices for the physical concern sub scale are not identical across the three countries and additional analyses should be carried out to establish measurement invariance.

The test for configural invariance was the first in the series of confirmatory factor analyses. Although the $\chi^2$ for this analysis was significant ($\chi^2 = 81.67$, df = 15), other indicators suggest an acceptable fit of the model (SRMR = 0.049, RMSEA = 0.12, CAIC = 440.58, CFI = 0.94, GFI = 0.96, NFI = 0.93, and NNFI = 0.89). Within country standardized factor loadings ranged from 0.43 to 0.97 and all of them were significant. Based on these results one can conclude that physical concern scale had the same factor configuration across the three countries.

The next step involved testing for full metric invariance. This was done by constraining the factor loadings to be invariant across countries. This model produced a $\chi^2$ of 118.26 (df = 23), SRMR = 0.078, RMSEA = 0.11, CAIC = 413.03, CFI = 0.92, GFI = 0.94, NFI = 0.90, and NNFI = 0.89. The increase in $\chi^2$ from the previous model was significant ($\chi^2 (8) = 36.59$, $p < .01$) although some other indicators suggest an improvement in the overall fit of the model. A review of the modification indices suggested that relaxing one constraint might improve the overall fit of the model. Therefore, a partial metric invariance model was tested by freeing one of the factor loadings for China (modification index = 31.65). This modified model produced a $\chi^2$ of 92.45 (df = 22), SRMR = 0.054, RMSEA = 0.10, CAIC = 395.44, CFI = 0.94, GFI = 0.96, NFI = 0.92, and NNFI = 0.92. A comparison of the partial metric invariance model with the configural invariance model shows an insignificant increase in $\chi^2$ ($\chi^2 (7) = 10.78$, ns). Other indicators suggest that

the partial metric invariance model had a better fit compared with the configural invariance model. As discussed previously, scalar invariance (comparison of the measurement intercepts) was not attempted because the samples in the three groups were not matched and any observed difference would be meaningless.

The next step in the process involved testing for full factor invariance. This was done by constraining factor variances to be the same across the three countries. However, this hypothesis could not be sustained because the change in $\chi^2$ from the previous model was significant ($\chi^2 (2) = 16.54, p < .01$). A review of the modification indices suggested that the overall fit of the model could be improved by setting the variance for the US sample to be free. This model improved the fit compared with the full factor invariance model ($\chi^2 = 101.91, df = 23$, SRMR = 0.053, RMSEA = 0.10, CAIC = 394.82, CFI = 0.93, GFI = 0.96, NFI = 0.92, and NNFI = 0.91). Indicators of the overall fit of the model suggest that the partial factor variance invariance model was comparable to the partial metric invariance model.

Finally, full error variance invariance model was tested by constraining the variance of error terms to be the same across the three groups. This model produced a $\chi^2$ of 355.77, df = 33, SRMR = 0.190, RMSEA = 0.16, CAIC = 520.99, CFI = 0.72, GFI = 0.77, NFI = 0.70, and NNFI = 0.75. All indicators of the overall fit of the model suggest that the full error variance model was not an improvement over the previous model. Based on a review of the modification indices four error terms (one at a time in sequential order) were set free to test for the partial error variance model. This model produced a $\chi^2$ of 149.06 (df = 29), SRMR = 0.072, RMSEA = 0.10, CAIC = 196.20, CFI = 0.90, GFI = 0.94, NFI = 0.88, and NNFI = 0.89. Although this model is an improvement over the previous model it is not a definite improvement over the partial metric invariance model or the partial factor variance invariance model, one can say that it has an acceptable fit.

Measurement Invariance of Physical View Scale

In this case too, the first step was to test for the equality of covariance matrix across the three countries ($\Sigma$s). As shown in Table 3, this test produced a $\chi^2$ of 313.84 with 42 degrees of freedom (p<.001), a SRMR of 0.12, RMSEA of 0.13, CAIC of 582.55, CFI of 0.87, GFI of 0.80, NFI of 0.85, and NNFI of 0.86. These results also show that the covariance matrices for the physical view trait items are not identical across the three countries and additional analyses should be carried out to establish measurement invariance.

The test for configural invariance was the first in the series of confirmatory factor analyses. Although the $\chi^2$ for this analysis was significant ($\chi^2 = 129.46, df = 27$), other indicators suggest an acceptable fit of the model (SRMR = 0.04, RMSEA = 0.10, CAIC = 552.10, CFI = 0.95, GFI = 0.95, NFI = 0.94, and NNFI = 0.92). Within country
standardized factor loadings ranged from 0.52 to 0.91 and all of them were significant. Based on these results one can conclude that physical view scale had that same factor configuration across the three countries.

In the next step factor loadings were constrained to be invariant across the three countries to test for full metric invariance. This model produced a $\chi^2$ of 147.84 (df = 37), SRMR = 0.06, RMSEA = 0.093, CAIC = 491.11, CFI = 0.95, GFI = 0.95, NFI = 0.93, and NNFI = 0.93. The increase in $\chi^2$ from the previous model was not significant ($\chi^2$ (10) = 17.38, ns). Also some other indicators suggest an improvement in the overall fit of the model. A review of the modification indices suggested that relaxing one constraint might improve the overall fit of the model. Therefore, a partial metric invariance model was tested by freeing one of the factor loadings for the US sample. This modified model produced a $\chi^2$ of 138.07 (df = 36), SRMR = 0.05, RMSEA = 0.091 CAIC = 489.36, CFI = 0.95, GFI = 0.95, NFI = 0.93, and NNFI = 0.94. A comparison of the partial metric invariance model to the configural invariance model shows an insignificant increase in $\chi^2$ ($\chi^2$ (9) = 8.61, ns). Other indicators suggest that the partial metric invariance model had a better fit compared with the configural invariance model. As discussed previously, scalar invariance (comparison of the measurement intercepts) was not attempted because the samples in the three groups were not matched and any observed difference would be meaningless.

The full factor invariance model was tested in the next step by constraining factor variances to be the same across the three countries. However, this hypothesis could not be sustained because the change in $\chi^2$ from the previous model was significant ($\chi^2$ (2) = 14.10, p < .01). A review of the modification indices suggested that the overall fit of the model could be improved by setting the variance for the Indian sample to be free. This model improved the fit compared with the full factor invariance model ($\chi^2$ = 139.54, df = 37, SRMR = 0.06, RMSEA = 0.089, CAIC = 482.78, CFI = 0.95, GFI = 0.95, NFI = 0.93, and NNFI = 0.94). Indicators of the overall fit of the model suggest that the partial factor variance invariance model was comparable to the partial metric invariance model.

Finally, full error variance invariance model was tested by constraining the variance of error terms to be the same across the three groups. This model produced a $\chi^2$ of 392.96, df = 49, SRMR = 0.13, RMSEA = 0.14, CAIC = 611.06, CFI = 0.83, GFI = 0.77, NFI = 0.81, and NNFI = 0.85. All indicators of the overall fit of the model suggest that the full error variance model was not an improvement over the previous model. Based on a review of the modification indices, six error terms (one at a time in sequential order) were set free to test for the partial error variance model. This model produced a $\chi^2$ of 168.48 (df = 43), SRMR = 0.07, RMSEA = 0.089, CAIC = 456.86, CFI = 0.94, GFI = 0.95, NFI = 0.92, and NNFI = 0.94. Although this model is an improvement over the previous model it is not a definite improvement over the partial metric invariance model or the partial factor variance invariance model once can say that it has an acceptable fit.

Overall, the results of the multiple step confirmatory factor analysis suggest that the two subscales of the physical vanity can be used to study consumers from diverse cultural backgrounds.
Discussion

The main objective of this research was to assess measurement invariance of the two subscales of physical vanity across three culturally diverse countries. Overall, data in this research support the notion that physical vanity is an important universal consumer construct and that can be applied in multiple cultural contexts. While the research found that not all measurement properties of the physical vanity scale match exactly across the three countries studied in this research, the value of the Physical Vanity scales in terms of reliability and validity is clearly demonstrated. Researchers studying vanity might therefore, find this scale to be useful when engaged in comparative analysis. Although the procedure recommended by S & B incorporates a test for the equivalence of mean of the latent construct across cultures, such a comparison was not attempted in the present research. Since the samples drawn from the three countries in our study were convenient samples and not representative of their respective populations, any comparison of latent mean would only provide superficial information. Yet, now that that applicability of the physical vanity scale has been demonstrated, future researchers might attempt to utilize representative samples across countries to study differences, and/or similarities, in vanity-driven behavior.

These findings have important implications for marketers of goods and services that focus on physical vanity factors. This is an important research tool in the hands of managers interested in learning about preferences of consumers across cultures.

References


### Table 1
**Factor Loadings**

<table>
<thead>
<tr>
<th></th>
<th>China</th>
<th></th>
<th>China</th>
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<th>USA</th>
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<tr>
<td></td>
<td>PC</td>
<td>PV</td>
<td>PC</td>
<td>PV</td>
<td>PC</td>
<td>PV</td>
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<tr>
<td>1. The way I look is extremely important to me</td>
<td>.632</td>
<td>.736</td>
<td>.845</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. I am very concerned about my appearance</td>
<td>.762</td>
<td>.704</td>
<td>.794</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. I would feel embarrassed if I was around people and did not look my best</td>
<td>.679</td>
<td>.488</td>
<td>.682</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. Looking my best is worth the effort</td>
<td>.607</td>
<td>.710</td>
<td>.660</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. It is important that I always look good</td>
<td>.785</td>
<td>.762</td>
<td>.740</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>6. People notice how attractive I am</td>
<td></td>
<td></td>
<td>.657</td>
<td>.730</td>
<td>.837</td>
<td></td>
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<tr>
<td>7. My looks are very appealing to others</td>
<td></td>
<td></td>
<td>.732</td>
<td>.755</td>
<td>.823</td>
<td></td>
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<tr>
<td>8. People are envious of my good looks</td>
<td></td>
<td></td>
<td>.787</td>
<td>.664</td>
<td>.713</td>
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<tr>
<td>9. I am a very good-looking individual</td>
<td></td>
<td></td>
<td>.770</td>
<td>.671</td>
<td>.788</td>
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<td>10. My body is sexually appealing</td>
<td></td>
<td></td>
<td>.703</td>
<td>.718</td>
<td>.764</td>
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<td>11. I have the type of body that people want to look at</td>
<td></td>
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<td>.697</td>
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<td>.762</td>
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<td>Mean</td>
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<td>17.05</td>
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<td>.73</td>
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<td>Correlations among the two traits</td>
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<td>.315</td>
<td></td>
<td>.294</td>
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<tr>
<td>N</td>
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<td></td>
<td>156</td>
<td></td>
<td>338</td>
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Note: PC = Physical concern trait; PV = Physical view trait
Table 2
Model Comparison for Physical Concern Trait

<table>
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<tr>
<th>Equality of $\Sigma^x$</th>
<th>$\chi^2$</th>
<th>$df$</th>
<th>SRMR</th>
<th>RMSEA</th>
<th>CAIC</th>
<th>CFI</th>
<th>GFI</th>
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<th>NNFI</th>
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<tr>
<td></td>
<td>311.02</td>
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<td>.17</td>
<td>.15</td>
<td>501.60</td>
<td>.76</td>
<td>.76</td>
<td>.74</td>
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<tr>
<td>Configural Invariance</td>
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<td>15</td>
<td>.049</td>
<td>.12</td>
<td>440.58</td>
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<td>.96</td>
<td>.93</td>
<td>.89</td>
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<tr>
<td>Full Metric Invariance</td>
<td>118.26</td>
<td>23</td>
<td>.078</td>
<td>.11</td>
<td>413.03</td>
<td>.92</td>
<td>.94</td>
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<td>.89</td>
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<tr>
<td>Partial Metric Invariance</td>
<td>92.45</td>
<td>22</td>
<td>.054</td>
<td>.10</td>
<td>395.44</td>
<td>.94</td>
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<td>.92</td>
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<td>Full Factor Variance Invariance</td>
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<td>.053</td>
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<td>355.77</td>
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### Table 3
Model Comparison for Physical View Trait

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<td>.86</td>
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<td>552.10</td>
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<td>456.86</td>
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## Corporate Social Capital as a Competitive Advantage in Determining a Company’s Capacity to Recognize Trends and Innovation Opportunities

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### Abstract:
Embedded in a globalized environment characterized by an increasing expansion and density of economic and social interactions, recognizing and improving a company’s capacity to recognize trends early and to innovate has become a critical success factor. A better understanding and management of a company’s innovation capacity implies the in-depth analysis of its conditions and drivers, as well as the identification of those internal and external actors and relationships with the highest potential for network-related innovation effects. Based upon an integral corporate value concept encompassing corporate financial, human and social capital, the purpose of this paper is to provide a conceptual framework which gives reason for adding the construct of social capital to the field of marketing strategy.

### Keywords:
Corporate Value, Innovation Management, Human and Social Capital

### Introduction

During recent years, the topic of social capital in general and in the context of organizations has gained growing interest in the strategic management literature. Existing studies (e.g., Adler & Kwon 2002; Nahapiet & Ghoshal 1998; Tsai 2000; Tsai & Ghoshal 1998) point out the fact that social capital is positively related to a company’s long-term competitive advantages and is an essential element of corporate value contributing to corporate success in a number of important organizational activities like inter-unit and inter-firm resource exchange, the creation of intellectual capital, inter-firm learning, supplier relationships, product innovation and entrepreneurship.

In global markets, the development and more effective, efficient and realistic management of social capital have gained special attention. To access adequate resources (e.g., information, technology, knowledge, access to distribution networks, etc.) and compete effectively in a globalized environment, companies are embedded in networks of business and social relationships that operate across national borders. With an increasing expansion and density of these local and global economic and social relations, the
dynamic interplay of international and global aspects of social capital becomes critical on a global level.

Embedded in a networked world characterized by compression of time and space where survival is particularly connected with a company’s capacity to sustainably out-learn and out-innovate its competitors (McElroy 2001), the production and integration of new knowledge as well as the recognition and improvement of the rate and quality of innovation capacity and innovation output is of particular importance. Apart from financial and human resources, knowledge and skills, a company’s natural ability to self-organize around innovation on an overall enterprise level – the social capacity to innovate in a company – should also be seen as a significant source of competitive advantage.

To date, only little research has addressed the topic of developing an integrated view of a company’s innovation capacity, especially incorporating the concept of social capital. To advance existing knowledge in the field of social capital, it might be an appropriate approach to start with the development of a theory based framework which contains basic hypotheses concerning the impact of relevant factors of social capital as well as human and financial capital on establishing high innovation capacity. Such a framework might, of course, be a little generic or abstract in structure and content. However, it is a good starting point to make sure that further conceptualization and especially operationalization will be appropriate. In this respect, the framework presented in this paper is only a first step of our future research trying to conceptualize the key dimensions of social capital as well as human capital, and to identify relevant impacts of these dimensions on the innovation capacity of (multinational) companies.

This paper is structured into three main sections. First, considering all different aspects of corporate capital to the company’s success, this paper aims at developing a multi-dimensional conceptualization of corporate value which encompasses corporate financial, human and social capital. Our conceptual model leads us to believe that human and social capital are the major determinants of innovation capacity. Second, two sets of propositions are developed: the first deriving from the perspective that knowledge and skills of individuals within the company impact innovation capacity (human capital), and the second deriving from the perspective that innovation capacity is tied to the characteristics of the social network in which the company is embedded (social capital). Third, the model and propositions are discussed with reference to their managerial and research implications.

**Construct Definition and Literature Review: Components of Corporate Value**

A comprehensive understanding of corporate value integrates all relevant actual and potential value sources and effects to the company’s success into one single model. In our socially constituted world it is worthwhile to go beyond the traditional economic view of the relationship between capital and firm performance. For the purposes of this paper, regarding all prospective and directly attributable in- and outpayments, corporate value can be – according to Bourdieu’s (1986) capital theory proposing economic, cultural and social capital – segmented into three highly interrelated forms of capital: financial, human and social. Each form is, at some point, convertible into money.
**Corporate Financial Capital:**

Corporate Financial Capital is immediately and directly convertible into money. It addresses direct monetary aspects and man-made aids to production owned by the company such as turnover, revenue, machines, land and equipment.

**Corporate Human Capital:**

Including indirect-monetary contributions from individuals within the company, the Corporate Human Capital focuses on the value of personality, knowledge, skills, experiences and abilities possessed by the company through its individual members.

**Corporate Social Capital:**

Social Capital – an umbrella concept used in a variety of disciplines to describe resources embedded within social networks (Adler & Kwon 2002) – can be defined as (a) “the aggregate of the actual or potential resources which are linked to possession of a durable network of more or less institutionalized relationships of mutual acquaintance or recognition” (Bourdieu 1985, p. 248), (b) “the sum of the actual and potential resources embedded within, available through, and derived from the network of relationships possessed by an individual or an social unit” (Nahapiet & Ghoshal 1998, p. 243), (c) “the capacity of individuals to employ (scarce) resources such as information, contacts and money because they are participants and members in social networks” (Faist 1995, p. 4), or (d) “the existence of a certain set of informal values or norms shared among members of a group that permit cooperation among them” (Fukuyama 1997). Referring “to friends, colleagues, and more general contacts through whom you receive opportunities to use your financial and human capital” (Burt 1992, p. 9) and “to connections among individuals, social networks and the norms of reciprocity and trustworthiness that arise from them” (Putnam 2000, p. 19), social capital is “a product of embeddedness” (Portes 1995, p. 13), which “inheres in the structure of relations between persons and among persons” (Coleman 1990, p. 302), and whose “effects flow from the information, influence, and solidarity it makes available to the actor” (Adler & Kwon 2002, p. 23).

With reference to organizations and their members, to a combination of firm specific and personal relations, corporate social capital can be defined as “the set of resources, tangible or virtual, that accrue to a corporate player through the player's social relationships, facilitating the attainment of goals” (Gabbay & Leenders 1999, p. 3). As a unique organizational resource, that is difficult to acquire and imperfectly tradable, corporate social capital is strongly associated to network structure and the value inherent in long-term relationships between individual employees, teams, departments and companies. Regarding multinational firms, corporate social capital is vitally important since they have to effectively integrate internal business units across geographic (e.g., country) boundaries, as well as manage relationships within a large external network of firms (Bartlett & Ghoshal 1998).

Generally spoken, embedded within a profound understanding of corporate value and referring to the connections that exist within and outside of the company on individual as well as on organizational level, corporate social capital encompasses both, the existence of a durable network of more or less institutionalized relationships as well as the sum of
actual and potential resources that might be available through and derive from that network.

**Conceptualization and Propositions:**

**Corporate Human and Social Capital as determinants of Innovation Capacity**

Economic survival in a globally networked world increasingly depends upon the company’s “widespread innovative capacity” (Bellandi 1989) and a continuous stream of new innovations, new patents, new ideas, new insights, and new bases of competitive advantage (McElroy 2001).

A company’s capacity to innovate – its ability to perceive opportunities and use internal and external information to develop or adopt innovative products or production processes – is undoubtedly based on a company’s financial (e.g., money, equipment, materials) and human resources (e.g., employees’ knowledge, education level, attitudes and values, innovativeness and creativity). However, as innovations often require a new set of resources not employed in the current production, the capacity to innovate also depends on the nature of the social environment in which a company is embedded. In our knowledge-based economy, innovations are no longer conceived as a specific result of individual actions, but more as an interactive social process of learning and exchange involving relationships between firms with different actors (Kline & Rosenberg 1986). Since interdependence between actors generates an innovative system or an innovation cluster (e.g., Edquist 1997; Landry & Amara 1988; Acs 2000; Porter 1999; Porter 2000), the local and global context of a company exerts a significant influence on the nature and extent of innovative activities (Gertler et al. 1998, 2000).

In view of the fact that diverse forms of social capital influence the innovation capacity of a company, corporate social capital can be – beyond corporate financial and human capital dimensions – considered as a necessary precondition (or antecedent) to a company’s collective capacity to collaborate around the production of new knowledge and all forms of innovation. Following a more interactionist instead of a conventional individualistic perspective (Schneider 1983) acknowledging the importance of social relationships and the social capital therein, “the combination of high-quality human capital and high-quality social capital is key to competitive advantage in the knowledge economy” (Lengnick-Hall & Lengnick-Hall 2003, p. 62).

Considering this background, it is important to identify, manage and control the influence of corporate human capital dimensions (i.e., employees’ capacity to acquire and apply effectively new knowledge, capabilities and skills) as well as social capital dimensions (i.e., the quality of social relationships – enabling employees to communicate useful knowledge) on a company’s innovation capacity. The research question is: Do human and social capital determine innovation in multinational companies, and if so, to what extent?

*Figure 1* shows the proposed conceptual model to investigate how far the capacity to innovate in a company is – apart from financial conditions – more closely tied to human or social capital dimensions.
Human Capital Dimensions

Focused on knowledge and innovation management, much research has concentrated on human resources, personal characteristics and development (e.g., Eagly & Chaiken 1993; Allen et al. 1992; Mayo & Marks 1990; Bearden et al. 1986; Hirschman 1980), proposing that contemporary firm’s core competencies lie more in its intellectual base than its hard assets (Quinn 1992). The intellectual base of a company “represents a valuable resource and a capability for action based on knowledge and knowing” (Nahapet & Ghoshal 1998, p. 245)

Aside from the dimensions we will concentrate on here, aspects like education level, attitudes, values, creativity, professional experiences and objectives, knowledge sharing potential willingness, cross-functional team working skills and collaborative spirit (Robertson & O’Malley Hammersley 2000; Swart & Kinnie 2003) are important to mention.

Expertise and Knowledge:

Expertise and knowledge in the forms of employees’ know-what and know-how (Quinn 1992), are important presuppositions of a company’s capacity to innovate and the most valuable assets of a 21st century company. Forming the basis for individual and organizational competence (Hayek 1945; Penrose 1959), knowledge includes various elements: (a) facts, truths or principles, (b) ideas validated by various tests, (c) findings of research, as well as (d) understandings derived from experience (Merton 1973; Souder & Moenaert 1992).

In this context it is important to mention, that innovation may arise from internal or external sources of knowledge (Dogson 1991) and a company’s own knowledge is a function of the knowledge that it has access to (Orr 1990). While employees can be viewed as “the ultimate knowledge creators and bearers” (Oltra 2003, p. 2), knowledge is a dynamic and complex system that changes as it interacts with the environment and can be defined as “a fluid mix of framed experience, values, contextual information, and expert insight that provides a framework for evaluating and incorporating new experiences and information. It originates and is applied in the minds of knowers” (Davenport & Prusak 1998, p.5). Since failures often occur when individual actors may lack knowledge, or a project team does not include people with the required expertise in problem solving (Weick & Roberts 1993), innovation can only result from an effective knowledge management processes (Rosemberg 1982). A company should realize the range as well as the boundaries of its internal knowledge, recognize what is not known within its own field and to whom it can turn for the certain expertise that is needed (Pinkus et al. 1997).

This leads us to our first proposition,

\[ P_{1a} : \text{Expertise and knowledge in terms of internal and external know-what and know-how are important preconditions of a company’s capacity to innovate.} \]
**Motivation and Involvement:**

The confidence to create ideas that are novel and useful, the willingness to adopt the sense of the need to change in the workplace and the ability to implement those ideas to develop new products, services or processes as well as an innovative organizational culture that is supportive of these efforts are core contributors to creative outputs. Employee commitment, job satisfaction and the level of involvement within a particular issue area may increase the motivation to innovate or to disseminate information about a "product," as well as reduce the cognitive costs associated with processing new information, allowing for a greater accumulation of knowledge over time (Bloch & Richins 1983). In fact, even employees with exceptional talent and know-how will not be able to develop potential without the adequate motivation (Twining 1991).

Consequently,

**P1b:** The employee’s individual motivation to innovate and the level of involvement within the innovation process determine the innovation capacity of a company.

**Innovativeness:**

Employees with a certain personal characteristic known as “innovativeness”, the predisposition to engage in creativity and experimentation through the introduction of new products, services as well as new processes, are among the first to support innovative efforts and new products. When they feel safe to innovate and perceive that their innovativeness contributes to the growth and profit of the company, employees are more likely to act innovatively and to experiment with new combinations of resources (Trice & Beyer 1993). Providing a forum that fosters employee innovativeness as the ability to create new solutions and not just relying on existing practices and models creates a basis for differentiation and competitive advantage (Zahra 1991). To enhance the innovativeness of employees, organizations should provide opportunities for development and training that facilitate creative decision-making, promote creativity and thus innovation (Sherman 1984; Cornwall & Perlman 1990).

Therefore, our next proposition follows:

**P1c:** Employee innovativeness and the willingness to support innovative efforts and new products contribute to a company’s capacity to innovate.

**Social Capital Dimensions**

While the first set of propositions addresses attributes of corporate human capital that contribute to innovation capacity, the second set demonstrates that corporate social capital plays a key role in determining the capacity to innovate in a company.
In the interest of moving towards measuring corporate social capital, it is useful to distinguish the sources of social capital along three dimensions: structural (e.g., network links), relational (e.g., trust) and cognitive (e.g., shared goals, shared paradigms) (Nahapiet & Ghoshal 1998; Tsai & Ghoshal 1998; Bourdieu 1986). Each having two common characteristics (Coleman 1990), as they constitute some aspect of the social structure, and facilitate the actions of individuals or organizations within the structure, the three dimensions are highly interrelated: Through social interaction (structural), individuals or groups develop trusting relationships (relational) and common goals and values (cognitive) (Tsai & Ghoshal 1998).

The Structural Dimension of Social Capital:

Viewing social relationships through the lenses of social network theorists (e.g., Burt 1992; Granovetter 1973; Hansen 1999; Wasserman & Faust 1994) the structural dimension of social capital deals with the pattern, configuration, and purpose of social interactions. Analyzing cliques, communication roles (e.g., liaisons, bridges, isolates), and structural indexes (e.g., connectedness, integration, diversity, openness) (Rogers & Kincaid 1981), structural capital considers the existence of connections between actors, the proximity of connections to the major powerful players, the diversity of the connections and the network position of an actor relative to other network players and investigates how the overall network configuration assists or hinders the flow of resources within the network.

The structural properties of social relationships such as centrality and betweenness are crucial in generating ideas and in coordinating expert knowledge in social networks and play an important role on how different actors can access resources from within the network. The position of a network actor or rather a business unit in a network significantly influences the capacity to innovate in this organization (Tsai 2001), companies with a central position in collaboration networks have a higher output of patents than less central firms (Powell et al. 1999). The availability of more potential exchange partners generate benefits deriving from the access to useful knowledge and to valuable and early information (Nahapiet & Ghoshal 1998). The number of network relations – so called network ties – influences and is proportional to the ability to acquire relevant information (Tsai & Ghoshal 1998).

Thus, the structure of social networks and the access to potential exchange partners can be regarded as important sources of new, external knowledge (Inkpen & Dinur 1998) and valuable channels for information benefits and knowledge diffusion and transformation, since knowledge is more easily transferred among networks partners than through market mechanisms (Shenkar & Li 1999).

Indicating an individual actor’s position within a network of relations, the structural dimension of social capital refers to the formation and the structure of ties between individuals in terms of density, connectivity or hierarchy (Burt 1992, 1997; Coleman 1988; Granovetter 1973; Hansen 1999). Structurally categorized as strong or weak, the strength of a tie (Granovetter 1973) is characterized by a combination of the duration, emotional intensity, intimacy, and reciprocity of interactions. Networks of largely strong ties – established through intense and repeated interaction – enable effective and efficient communication and are important for sharing and transferring more complex information...
and knowledge that is sticky by nature, i.e. highly context dependent, confidential or complex (Hansen 1999; Larson 1992; Levin et al. 2002). However, due to their clique-like structure, strong tie networks may suffer from redundant contacts and may decrease innovativeness because of rigidity caused by excessive amounts of normative cohesiveness. In contrast, weak ties, bridging structural holes (Burt 1992) between disparate social units, enable accessing a diverse range of other actors in terms of actor characteristics, available information, and perceptual scope (Burt 1997). From the novel and non-redundant information and opportunities that weak ties make available, value can be derived (BarNir & Smith 2002).

The existence of strong and weak ties impacts the potential innovation capacity of a company. Rather than being at the centre of a network, opinion brokers (Burt 1999) are located at the edge of several heterogeneous networks and play a key role in the flow of information because of existing social capital. Since they have relationships to members outside of the group that other group members lack, they span ”structural holes” and possess unique access to potentially valuable information. They can act as a bridge between different networks, which gives them their ‘Social Capital’ and status as a local missionary or maybe a role model within the group. Looking for ideas outside their immediate community (Rogers 1995), opinion brokers activate their bridging weak ties to well-connected actors who are perceived to have some expertise (Bansal & Voyer 2000; Gatignon & Robertson 1986), receive potentially valuable, new information and then influence other strong tie-related actors (Weimann 1982). Consequently, having such a central brokering position enables the access to second-order resources, i.e. the resources that are not one’s own but that are embedded in and mobilizable through social networks, like the knowledge of one’s friends (Bourdieu 1980; Lin 1999), and the combination of these resources into new entrepreneurial activities (Burt 1992).

This leads us to our next proposition,

P2a: The structural properties of social capital – the availability of potential exchange partners and the access to external expert knowledge – represent the opportunity to share information and knowledge and are important preconditions of a company’s capacity to innovate.

The Relational Dimension of Social Capital:

Whereas the structural dimension of social capital refers to the presence or absence of relations between actors, yet, cannot fully describe the ability of an individual or organization to be able to access social resources, the relational source dimension of social capital focuses on the quality and content, rather than the structure, of social relationships. Apart from the access to potential exchange partners and resources, innovations require relational aspects such as openness, willingness to take risks, and trust, which is built up over years of informal interactions between company members (Axelrod 1984; Krackhardt 1992; Oliver 1997; von Hippel 1988).

Relational social capital, as prerequisite for the formation of effective and stable relationships, encompasses the emotional aspects of relationships (Naude & Buttle 2000) – group process phenomenon like shared norms and values, interpersonal obligations and expectations, reciprocal obligation, mutual identification, commitment, understanding,
honesty and trust which organizations or groups of individuals have developed with each other through a history of social interactions (Nahapiet & Ghoshal 1998).

The relational dimension of social capital, as measured by trust, trustworthiness and commitment, allows actors to determine the amount of capital and level of risk when exchanging resources and will increase strength of preference for a particular exchange partner (Gwinner et al. 1998). Trust as “the willingness to be vulnerable to the actions of another party” (Mayer et al. 1995, p. 712), and trustworthiness as “the quality of the trusted party that makes the trustor willing to be vulnerable” (Levin et al. 2002) are among the most important facets of relational social capital. The existence of high trust in a relationship is proportional to the ability to freely share information, to take risks and innovate and to acquire information from this tie as well as to the credibility of information (Fukuyama 1995; Ring & van de Ven 1992, 1994) and produces certain outcomes such as cooperation and sensitive information exchange (Mayer & Davis 1999). Without high levels of trust and mutual solidarity, individuals or organizations are not going to establish and maintain interorganizational relations or give other actors access to useful knowledge or confidential information (Gherardi & Masiero 1990; Krackhardt 1992; Oliver 1997; Staber 1994; van de Meer & Calori 1989). Shared trust (or lack of it) influences the extent of information exchanged, the scope of search for and the commitment of managers to implement solutions and is considered as a significant determinant of managerial effectiveness (Zand 1972).

According to the closeness and the quality of a firm’s inter-organizational linkages, the tie strength has been found to be one of the most significant factors to explain the influence of network relations, their overall success and the value created (Ghoshal & Bartlett 1990). Research has examined the effects of the strength of ties on knowledge transfer and innovation (e.g., Hansen 1999; Uzzi 1996, 1997, 1999). Stronger ties may bring increased trust, prospective reciprocity, and commitment (Krackhardt & Stern 1988; Uzzi 1997; Gabbay 1997; Gabbay & Stein 1999) and are more likely to be activated than weak ties as sources of information and are perceived as more credible (Rogers 1995) and more influential (Brown & Reingen 1987; Reingen & Kernan 1986; Bansal & Voyer 2000). Further, stronger ties are typically more easily available (Granovetter 1982) and favor mutual interaction and feedback loops between the sender and the recipient (Leonard-Barton 1993) – an important aspect in the process of innovation (Kline & Rosenberg 1986; Rothwell 1992).

However, weak-tie information sources – not being limited to the social circle of the individual or organization – are more numerous, promote generation of new ideas and opportunities and offer varied and better information (Duhan et al. 1997). Moreover, weak ties may bring information on distinct social circles (Granovetter 1973), are more likely than strong ties to facilitate knowledge and referral flows (Brown & Reingen 1987), and play a crucial role in the diffusion of innovations (Rogers 1995).

In conclusion, in situations where information should circulate at a high speed and a high degree of trust, confidence and intimacy is required, strong tie-sources will be more influential and reveal rich exchanges of information and proprietary "know-how". However, when information relate to generation of new ideas and opportunities, weak tie-sources with a wide-ranging knowledge level are likely to have more influence.
Therefore, we propose that:

\[ P_{2b}: \] The relational properties of social capital – the level of trust and the strength of preference for a particular exchange partner – represent the *willingness and motivation* to share information and knowledge and determine a company’s innovation capacity.

**The Cognitive Dimension of Social Capital:**

The cognitive dimension of social capital – one of the least discussed dimensions when referring to social capital (Nahapiet & Ghoshal 1998) – addresses the need for a common understanding or “vocabulary” to build social capital. Related to the relational dimension, it will increase the strength of preference for a potential exchange partner, since similarity (i.e., shared norms and values) tends to influence relationships (Cialdini 1993).

Through its *shared meanings, language, symbols and codes*, the cognitive dimension facilitates the sharing of information and knowledge (Weber & Camerer 2003), which is necessarily important since innovation process involves the exchange of codified and tacit knowledge (e.g., Patel & Pavitt 1994; Winter 1987). The existence of shared language and codes is vital for efficient knowledge transfer and integration among individuals or groups and act as vehicles for integrating individual understandings and experiences. Thus, only if they share a common language, knowledge can be transferred and different companies can interact and gain access to people and their information about the other company.

While the cognitive dimension of social capital does not have any affect on the overall resource exchange and combination of resources (Tsai & Ghoshal 1998), “organization members who share a vision will be more likely to become partners sharing or exchanging their resources” (Tsai & Ghoshal 1998, p. 467). The cognitive dimension allows network actors to determine common patterns of behavior, develop expectations on what future patterns of behavior will occur and understand when new knowledge or information is brought into the network, to learn from new information and develop new knowledge which can then be transmitted through the network. Cognitive social capital is vitally important to multinational companies to integrate business units operating in multiple and diverse country markets and cultures – by shared values, goals, a mutual understanding and global vision, they can be bound together, solve possible bottlenecks, and fine-tune their decision-making.

Overall, the cognitive dimension of social capital describes the ability of network actors to create understandings of network behavior and facilitates the flow of valuable information and knowledge.

Consequently, the following proposition emerges:

\[ P_{2c}: \] The cognitive properties of social capital – a common understanding and the level of shared norms, values and beliefs – represent the *ability* to share information and knowledge and affect the innovation capacity of a company.
Even though we have just made a very first step to conceptualize innovation capacity in view of identifying corporate value as an overall measure to focus managerial planning, our integrative framework sketched in figure 1 seems to be worth focusing in further research as well as in managerial practice.

Conclusion

Further Research Steps:

Focusing on the link between individual attributes and social resources, this paper has examined the role of social context in determining a company’s capacity to innovate. We suggest that innovation capacity is rooted in the presence of a certain set of individual characteristics and in the social environment in which a (multinational) company is embedded.

Of course, our model is only a first step and should be further developed in different ways. First, the different propositions sketched above will have to be elaborated more into depth. Second, in the next step of developing hypotheses, we should as well emphasize the interplay between the different variables. This will have to lead to a proper causal modeling of effects between the dimensions of human and social capital and their impact on a company’s capacity to innovate. In this context we will also have to add the conceptualization of different forms of innovation capacity and their explanation in view of human and social capital impacts. As important the generation of such an extended model might be, we believe that first of all, we should try to empirically find out the relevancy of different variables measuring human and social capital to portray high corporate value in a more aggregated sense. Against this background we might concentrate a more advanced causal modeling on important variables. Such a procedure seems to be important insofar as the amount of variables and relationships between them is so high that one would run the risk “getting lost in complexity”.

Preparing the empirical test of our model the dimensions of human and social capital need to be operationalized. In some cases we already can fall back on already existing and somewhat tested measures, in other cases we will have to start from scratch. Especially in view of the different dimensions of social capital it might be worth starting with exploratory interviews with innovative local and global network members that are likely to yield further items. Further steps of the empirical work have, of course, to meet the state of the art of the use of sophisticated multivariate methods. For example, it might be useful to compare different approaches of formative and reflexive construct development and testing (Diamantopoulos & Winklhofer 2001; Jarvis et al. 2003), and, due to the fact that we cannot assume linear relationships between the different variables, we should also draw on nonlinear causal modeling (cf. also using neural networks).

Despite the limitations and necessary steps in future research, the primary contribution of our framework lies in developing and explaining a model of innovation capacity integrating the concept of social capital. The social capital dimensions could be used as a basis to develop a more robust measurement instrument to measure and manage a company’s capacity to innovate.
Managerial Implications:
Having more robust measures of innovation capacity is of course as well a key for managerial practice. In view of our propositions concerning the impact of social capital on the company’s innovation capacity, managers might discover the existence and relevancy of internal and external information, knowledge and other resources in their local and global business network which are either already available or easily accessible. Overall, taking the interplay between human and social capital into account our framework already might lead to the opportunity of a better understanding of the conditions and drivers of a company’s capacity to innovate and to come to a broadened view of corporate value. This will of course enlarge the efficiency of identifying and selecting different employee groups and of encouraging appropriate key employees or business units to leverage and use their innovation potentials.

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Figure 1

The Conceptual Model
The Relation between Environmental and Financial Performance Contingent on Industry Risk

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Abstract: This study extends previous research on the relation between different measures of environmental and financial performance by introducing moderating effects of inherent environmental industry risk. We provide empirical evidence from the MSCI World Index U.S. companies by using the GES Investment Services® risk rating for the period 2003-2006. The inherent environmental industry risk has a significant moderating effect on the form of the relation between environmental preparedness/performance and operating performance of the companies. In high risk or polluting industries, environmental management is costly and reduces the operating performance of companies. In low risk sectors, such as banking and insurance, leading companies on environmental management are also more profitable. The paper makes a distinction between the reputational benefits of environmental preparedness and the operational gains of environmental performance when studying the effects on market value. A significant direct effect of environmental preparedness on the market value of the companies is present, while the relation between environmental performance and market value is stronger in low risk industries than in high risk industries. In low risk industries, the market value of the companies is also on average higher and more attuned to benefits to environmental performance than in high risk industries.

1. Introduction

There is a long-standing debate in the academic literature on the relation between environmental and financial performance of companies and the outcomes of studies are mixed and contradictory. The sceptical view is that companies that respond actively to environmental challenges incur extra costs and thus reduce their profits and shareholder value (Walley and Whitehead, 1994). A primary argument for the opposite view is that a company can improve its economic value by being the first-mover to exploit environmental opportunities by anticipating environmental regulation and standards. Leading companies could encounter higher costs, but according to Williams and Siegel

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(2001) and Lundgren (2007) their customers may be willing to pay higher prices. An environmentally pro-active leading company could therefore be more profitable, and additionally because of benefits to its reputation have a higher market value than environmentally lagging companies.

This paper is motivated by the fact that environmental regulations, restrictions, and concerns differ among industries, but the environmentally related industry risk effect has not explicitly been considered in earlier studies. Some research has investigated how industry differences affect the relations between environmental and financial performance. These studies argue that the findings of the direct effects are driven by the fact that a positive effect in one industry is balanced by a negative effect in another (Elsayed and Paton, 2005). An examination of the association between environmental performance and financial performance of companies belonging to different industries has been performed by including industry dummies (Konar and Cohen, 2001; Elsayed and Paton, 2005; Hassel et. al, 2005 and Semenova and Hassel, 2008). The purpose of this paper is to empirically examine if the environmental risk of the industry moderates the relation between environmental performance of the company and two financial performance measures, the operating performance of the company measured by Return on Assets and the market value of the company measured by Tobin’s Q.

The next section of the paper develops hypotheses for the moderating effects, presents the research method use, results and a final discussion of the results of study.

2. Hypotheses Development

This paper is based on the notion that the industry context determines the environmental profiles of the companies with resulting financial consequences for operating performance and market values (Semenova and Hassel, 2008). Polluting industries typically have higher environmental regulations and constraints than clean industries. Environmental regulation in polluting industries has been found to negatively affect productivity, increase the operating uncertainty and required rate of return for companies (Jaffe et al., 1995; Semenova and Hassel, 2008). By studying the industry effect, we separate the inherent environmental risk of the industry from the company-specific environmental risks and their relations to financial performance of companies. Company-specific environmental risks can be managed through environmental preparedness and performance. By introducing two dimensions of environmental performance, this study allows a separate examination of the reputational benefits of preparedness on market value and the operational benefits of environmental performance on operating performance. Following Guenster et al. (2006) we use Return on Assets (ROA) as a measure for operating performance, and Tobin’s Q (Q) as a proxy for the market value of the company’s shares. The two measures are complementary in that ROA measures the financial returns from the current assets employed by the company, while Q reflects the intangible value in the stock market beyond the book value of the company.

The theoretical underpinnings for the moderating effects of inherent environmental industry risk on the relations between environmental and financial performance are
scarce. At the same time, industries vary considerably in their environmental impacts, governmental regulatory standards, and technological opportunities (Griffin and Mahon, 1997). Further, there are differences among industries on both social/environmental performance and financial performance (Waddock and Graves, 1997, Semenova and Hassel, 2008). The study of Elsayed and Paton (2005) provides a foundation for that the impact of environmental performance on financial outcomes is different across industries. They found that environmental performance had a positive relation to return on assets for companies in the chemical and telecommunication industries, but a negative impact in the metals and motor vehicles industries. Konar and Cohen (2001) also show that the magnitude of the environmental effects varies across industries. The traditionally polluting industries, such as chemical, metals, manufacturing and papers accrue larger financial losses, while smaller losses are in food products, transportation equipment, and electric machinery industries. The studies show that there is a direct industry effect indicating that environmental performance is more costly in polluting industries or in industries with high inherent environmental risk. The moderating effects of the industry risk have, however, not been subject to a systematic study before.

Our initial hypothesis is that when the environmental risk of industry is high, companies operating in those industries incur higher costs and reduce their operating performance when they want to comply with stringent environmental standards and improve their environmental performance. We consider two dimensions of company-specific environmental opportunities which are environmental preparedness and environmental performance. Environmental preparedness includes environmental policies and programs, mandatory and voluntary environmental reporting, environmental certification and environmental screening of suppliers for companies to engage in order to improve their environmental profile. Freedman and Jaggi (1988) argued that companies in polluting industries made more extensive voluntary disclosures of environmental information. The demand to invest in a pollution prevention policy and clean technologies is costly for companies in polluting industries (Konar and Cohen, 2001). Contrary, companies in green industries encounter smaller expenditures when they want to improve their environmental preparedness and performance. New technologies and processes that are on the cutting edge of emission reductions cost more and the viability of new, clean technologies is unknown as well as the economic consequences of their use (Russo and Fouts, 1997). Walley and Whitehead (1994) posited that it is not easy to be ‘green’ because environmental challenges are costly for companies, especially in industries with high competition and overcapacity such as the petroleum and chemicals sectors. Henkel et al. (2001, p. 448) took a theoretical standpoint that polluting industries consist mostly of companies with high reforming costs, while clean industries consist of firms with lower costs of compliance. Russo and Fouts (1997) made a general argument that industry context moderates the influence of environmental/social performance on economic performance. From this follows the proposition that improving the environmental preparedness and performance in industries with high or low inherent-industry risk will have different effects on companies’ operating performance. A moderating effect with a difference in the form of the relationship (Sharma et al., 1981; Hartmann, 1999) is proposed:
H1: The relations between environmental preparedness / performance and operating performance are moderated by inherent-industry risk; when the inherent-industry risk is high (low) environmental preparedness/performance will have a negative (positive) effect on operating performance.

This paper develops two separate hypotheses for how the environmental risk of the industry relates to the market value of the company. Alessandri and Khan (2006) have explored the role of industry risk and suggested that companies would be penalized if they deviate from the industry risk norms. The nature of the industry and the type of the risk norm were found to be important in company valuation. Elsayed and Paton (2005) report industry differences in the impact of environmental performance on operating performance, but not on market value. Konar and Cohen (2001) found that the magnitude of the market value loss is different across industries.

Prior research has more consistently been able to establish a positive relation between policies and programs to meet environmental demands and the share price of the company. Also, the Swedish Society of Financial Analysts (SFF) has highlighted the importance of information about a company’s environmental concerns and performance to the investors. Their recommendation, Environmental Information for Financial Analysts, states: ‘For an increasing number of companies a positive environmental profile has become an important element in their marketing strategy of the company and a lack of such a profile constitutes a risk factor’ (SFF, 2000, p. 58; authors’ translation). Reputational benefits can be related to the environmental profile. Dowell et al. (2000) showed that companies that go beyond global environmental standards in the manufacturing and mining industries have higher market values than companies that barely meet the standards. Konar and Cohen (2001) found support for the proposition that companies with few or no law suits have higher market values. Klassen and McLaughlin (1996) found a positive effect on market values of companies that received environmental achievement rewards, while negative news led to decrease in market value. Companies with low environmental preparedness can potentially encounter the same environmental violations that were found by Karpoff et al. (2005) to lead to reputational penalties. This study suggests that high environmental preparedness will bring a positive environmental profile to companies. Environmental preparedness may not have a positive impact on future cash flows, but improved reputation, followed by lower company-specific risk, leads to a lower discount rate and potentially higher present market value. Spicer (1978) saw the risk in that the capital market impute a higher risk factor resulting in a lower present value if the company fail to respond to environmental expectations. The following hypothesis proposes a positive relation between a company’s environmental preparedness and the market value:

H2a: There is a direct positive relationship between environmental preparedness and market value of the company.

The most consistent support in prior research has been found for the relation between environmental performance and company value. Prior studies, however, use some composite measure of environmental performance which makes it difficult to judge
whether the positive effects on value come from reputational benefits or changes in net cash flows. Konar and Cohen (2001) have demonstrated that environmental performance correlates with intangible asset values (Tobin’s Q) in high risk industries. King and Lennox (2002) found an indication of the ‘it pays to be green’ effect, but they were unable to separate industry and company effects. Hassel et al. (2005) used an abnormal earnings model with non-financial environmental performance as a driver of future earnings and found an incremental negative effect on market value added. Guenster et al. (2006) found a positive relation between best-in-class eco-efficiency and Tobin’s Q. The relation strengthened over time indicating that the market value effect of environmental performance was priced with a drift. The difference in market values of low and high eco-efficient companies increased over time indicating especially that the lagging companies were penalized.

Polluting industries are more regulated than clean industries and they have more stringent environmental constraints on company operations. Pollution abatement to comply with stricter environmental standards requires larger capital cost that decrease market value (Konar and Cohen, 2001; King and Lenox, 2001; Semenova and Hassel, 2008). Financial markets can, according to Klassen and McLaughlin (1996) react differently to industries that are environmentally clean and polluting. Improved environmental performance of companies in polluting industries, such as petroleum, may be viewed with scepticism leading to that financial markets initially reward environmental performance only in clean industries. Companies in green industries with low compliance and regulatory costs that improve their environmental performance will have higher market returns than companies in polluting industries. We propose that the strength of the relation (Sharma et al., 1981; Hartmann, 1999) between environmental performance and market value is moderated by industry risk.

H2b: The relation between environmental performance and market value is more positive under low than high inherent environmental industry risk

This study additionally controls for a number of company-specific variables that in previous empirical research were related to operating performance and company value (Konar and Cohen, 2001; Guenster et al., 2006). The control variables are included in table 1.

3. Methodology and Data

We examine three environmental-related measures for each of the companies that affect financial performance: preparedness, performance, and industry risk. Our environmental measures have several notable advantages. Traditional environmental proxies, such as absolute pollution levels and eco-efficiency consider either a single dimension of a company’s environmental performance that reflects historical environmental events or embody both current and forward-looking information into one multi-dimensional measure. Our extension is that environmental opportunities, namely environmental preparedness and performance allow us to separately consider reputational and operational benefits from environmental management. In contrast to current studies,
which analyse the impact environmental performance on firm performance across different industries by using the dummy variables for each primary two-digit standard industrial classification (Elsayed and Paton, 2005), this study investigates the influence of an industry-specific variable and provides a broader environmental risk and opportunity approach.

The issue of whether the impact of environmental opportunities on financial performance varies across different industries is explored using moderated regression analysis (Lance, 1988; Sharma et al., 1981; McClelland and Judd, 1993; Jaccard, 1990). We assume that environmental inherent-industry risk moderates the relations and specify three models (see table 1), which are based on one-way and two-ways interactions.

In examining the relationship between variables, we use the pooled cross-section time-series data analysis. The advantage of this approach is that the sample is much larger than when only time-series or cross-sectional methods are employed. Consequently, the precision in estimation of the regression parameters will increase. We recognize that pooling six time periods of data for each company requires us to control for a correlation in the error term of the regression models over time for a given company (Cameron and Trivedi, 2005; Petersen, 2007). Ignoring this panel data problem would lead to underestimated standard errors and inflated t-statistics. In this study, the parameters of the models (2)-(4) are computed by using the pooled OLS estimator with panel-robust standard errors that correct serial correlation and heteroskedasticity. The White heteroskedasticity-consistent estimator is applied to obtain the panel-robust standard errors adjusted for intra-cluster correlation (White, 1980). For the short panels used, this approach does not require specifying the models for individual-specific effects, assuming independence and identical distribution over cross-sectional units and no fixed effects (Cameron and Trivedi, 2005). We control for correlation across time of Tobin’s Q and ROA by including time dummies. Including the industry dummies and company-specific controls allow us capture unobserved industry and company-specific effects. Throughout the study, the number of observations varies depending upon which variables have missing data points. To avoid the effect of missing data, we apply the all-available or the replace value imputation methods.

The data used in this study comes from two main sources. Financial information, i.e., ROA, market value, and a set of control variables, were obtained from Thomson Financial DataStream. The data set consists of quarterly reports for 563 U.S. companies from the last quarter of 2002 through the last quarter of 2006, and covers all key accounting indicators essential for constructing our research measures. For environmental information, multiple data sources have been used in recent quantitative research, e.g. the Fortune survey, the KLD index, the Toxics Release Inventory, the Franklin Research and Development Corporation, and the Innovest Strategic Value Advisors’ eco-efficiency ratings (Griffin and Mahon, 1997; Russo and Fouts, 1997; Guenster et al., 2006). The environmental measures were obtained from the Global Ethical Standard (GES) Investment Services® Risk Rating. The strength of the GES Investment Services database is that it provides evaluations of both environmental risk and opportunity of the MSCI World Index companies. The environmental rating includes the inherent industry risk level and the company-specific risk level. The company-specific risk is based on two
sub-scores of companies’ opportunities, namely performance and preparedness. Preparedness represents reputational benefits from a company’s environmental policy, management systems, and regular reporting. Performance covers the pro-active operational ability of the company to handle environmental impacts and risks, such as product performance, energy use, GHG and VOC emissions, waste treatment, and other initiatives. Altogether the GES systematic screening evaluates companies’ present environmental status and readiness for the future. Environmental measures are intended to embody both ex post and ex ante dimensions of corporate risk and opportunity.

4. Results

Table 1 provides the results of regression models based on equations (2) through (4) for environmental risk and opportunity scores. Columns of the panels report coefficients on dependent variables ROA and Q and their one-tailed tests of significance. Note that the coefficients estimated for company-specific control variables are consistent with those reported by Guenster et al. (2006), and by Waddock and Graves (1997). Industry and time dummy controls are included but suppressed in the tables.

The first column of Table 1 shows the results of the tests for the main effects of environmental opportunities on financial outcomes. Both environmental preparedness and performance are significantly positively related to company ROA and Q. As shown in the second column of Table 1, the industry risk has a significantly positive relation to operating performance and a significantly negative relation to the market value of the companies. The influence of inherent-industry risk on the relationship between environmental opportunities and financial outcomes is explored by including the two-way interaction term in equation (3). For ROA the interaction terms for both environmental preparedness and environmental performance are significantly negative ($\beta_3 = -0.09, t$-value $=-2.73$; $\beta_3 = -0.09, t$-value $=-1.97$), suggesting that the relationships are modified by inherent-industry risk. Including the two-way interaction term in the regression equation increases $R^2$ from 0.1354 to 0.1402 ($p<0.01$). When Q is dependent variable, the interaction term for environmental performance is significant ($\beta_3 = -0.005, t$-value $=-1.43$) and increases $R^2$ from 0.2997 to 0.3004 ($p<0.01$).

Hypothesis 2b suggested that the strength of the relationship between environmental performance and market value (Q) would be different under high and low environmental risk and the interaction term was found to be significant. We conclude that the strength of the relation is moderated by industry risk. The results indicate the fact that better environmental performers in green industries get significantly higher market valuation that their counterparts in polluting industries. Additional test shows that in polluting industries only companies with high operating performance can significantly improve their market value through environmental performance.

---

1 The companies are grouped in the high industry risk sample at the median value of inherent-industry risk (2.33) and then the sample are divided into high and low operating performance sub-sets at the median value of ROA (8.08). The findings indicate that environmental performance has a significantly positive
Thus, all tests indicate that environmental industry risk moderates the form of the relationship between environmental preparedness/performance and operating performance (ROA), and modifies the strength of the relation between environmental preparedness and market value (Q). Finally, the direct relation between environmental preparedness and market value are significant and companies under high risk trade at a significant discount. Overall, we find empirical support for hypothesis H1, and support for the moderating effects hypotheses H2a and H2b.

5. Conclusions

This study extends previous research on the direct relation between environmental and financial performance by introducing both form and strength as moderating effects of the industry risk. The motivation to study the industry effect is that polluting industries are more regulated than clean industries and they have differing environmental constraints on company operations that directly or indirectly affect the economic value of companies. Previous studies have either been restricted to polluting industries (Freedman and Jaggi, 1988; Dowell et al., 2000; Konar and Cohen, 2001) because the environmental performance measured used were tuned to polluting industries only, or when industry wide performance measures were used, the environmental profiles of the industries were not explicitly under study (Guenster et al., 2006). We use the industry ratings by the GES Investment Services to explicitly capture the inherent environmental risks in a wide range of industries.

The empirical results of the study are in line with the proposed hypotheses for the financial outcomes of the moderating industry risk effects. The study we decomposes the environmental opportunities of the companies into two dimensions of environmental preparedness and environmental performance. The two opportunity dimensions allow us to separate the reputational benefits on market value (Q) from the operational benefits on operating performance (ROA). Restrictions in environmental performance constructs have not in earlier studies allowed a multi-dimensional view. The first dimension, environmental preparedness is expected to bring reputational benefits to the company. Leading companies can gain higher market values than lagging companies. The operational costs can, however, outweigh the benefits and the outcomes on operating performance can be either positive or negative. We proposed that environmental preparedness does not bring incremental changes in the internal performance of companies with operational benefits, as also suggested by the pro-active view of Clarksson et al. (2006). Preparedness can especially be costly in high environmental risk industries where the companies have to live up to constraining environmental standards. The second dimension, environmental performance can capture the comparative operational benefits that lead to both higher operating performance and market values in leading companies compared to lagging companies. This eco-efficiency paradigm was supported by the Guenster et al. (2006) study.

Impact on Tobin’s Q ($\beta_1 = 0.06$, t-value = 3.12) for those companies that have high profitability in polluting industries and environmental performance has an insignificant impact on Tobin’s Q ($\beta_1 = -0.002$, t-value = -0.15) for the companies with low profitability in polluting industries.
Additionally, the inherent risk of the industry is has a direct positive relation to the operating performance and direct negative relation to the market values of U.S. companies when controlling for company-specific characteristics in a multi-variate setting. The findings are also supported by uni-variate tests that the mean ROA (Q) is significantly higher (lower) in industries rated in the two highest risk classes of industries than in the two lowest rated industries.

The complexity in the relations is demonstrated by both differences in forms and strengths of relations due to industry risk moderators. Operating performance can be improved by both environmental preparedness and performance only in low risk industries. The effect of environmental performance on market value is stronger in low risk industries. Environmental preparedness brings reputational benefits to market value in both low and high risk industries. Thus, this is the first study to provide evidence on the financial outcomes of the moderating industry effect that the GES Investment Services® risk ratings provided a basis for.

References


Hamilton J. 1995. Pollution as News: Media and Stock Market Reactions to the Toxics Release Inventory


Table 1. Regression results of sample companies

The table shows the outcome of estimating linear panel data regressions of financial performance on environmental risk and opportunities with inherent-industry risk as moderator. The unbalanced panel contains 534 companies constituting 3204 company-year observations over the period 2003-2006. The table reports pooled OLS coefficients with the panel-robust t-statistic (in parentheses) based on White (1980) standard errors. The environmental risk, preparedness and performance scores are centered in equations 2-3. Significance at the 1%, 5% and 10% level is indicated by ***, **, and *, respectively (one-tailed tests).

<table>
<thead>
<tr>
<th>Variable</th>
<th>Equation (2)</th>
<th>Equation (3)</th>
<th>Equation (4)</th>
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<td></td>
<td>ROA</td>
<td>Q</td>
<td>ROA</td>
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<td>Intercept</td>
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<td>3.61***</td>
<td>11.23***</td>
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<td>(6.96)</td>
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<td>(6.99)</td>
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<td><strong>0.017</strong>*</td>
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<td>(2.83)</td>
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<td>(0.35)</td>
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<tr>
<td>Performance</td>
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<td><strong>0.013</strong>*</td>
<td>0.03</td>
</tr>
<tr>
<td></td>
<td>(2.13)</td>
<td>(1.47)</td>
<td>(0.28)</td>
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<tr>
<td>Industry Risk</td>
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<td><strong>-0.030</strong>*</td>
<td><strong>0.51</strong>*</td>
</tr>
<tr>
<td></td>
<td>(5.86)</td>
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<td>(6.30)</td>
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<tr>
<td></td>
<td>(-2.73)</td>
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<td>0.04***</td>
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An Arabian Subcontracting Study in Business Development and the Alliance Life Cycle

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Abstract: The alliance life cycle concept applied to entrepreneurial business development presents an observation of business practice from which principles can be derived. A review of the literature was undertaken primarily from Western sources to explain SME business behaviour in the absence of research-based literature about the life cycle of the SME firm in the business of subcontracting directly relating to Arab GCC countries or other Arabian countries. The research presented in this paper investigated some of the forces of development of subcontracting businesses in the clothing and textile industries of Tunisia. By comparison with the traditional product life cycle a development cycle of the firm was created from the changes and dynamics of the relationships between the contractors and the subcontractors. The stages of the cycle are clearly demonstrated and empirically derived. The paper concludes that the Tunisian study could provide future research directions from which to examine the importance and differences of business culture in the contractor-subcontractor relationships within other spheres in Arab GCC countries and the West.

Keywords: alliance life cycle, business development, theory of the firm, entrepreneurial and marketing insights, strategy, Tunisian contractors-subcontracting relationships

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Introduction

Sub-contracting is about the engagement of another person or firm, normally as a third party to perform part or all of the business related activities for a contractor, the second party, where the contractor already has an original contract with another entity, the first party. So in the usual processes of inter-firms’ business relationships the production of goods and services can become complicated. One contractor can have several SME subcontractors. The study in this paper showed that sub-contractors were limited in marketing and in opportunities for business development when as suppliers their activities were concentrated in production while marketing became a powerful tool for the contractor in touch with the retailers and end users. In the Gulf GCC states where the indigenous populations are small compared to other countries such as China or India, subcontracting has become an important mainstay for their economies due to the need to import the necessary skills to sustain economic growth. The SME subcontracting firms in developing countries, such as Tunisia, needed to be developing business to business activities as changes in their marketing environments brought in greater competition into their domestic markets. Subcontracting was seen by the SMEs in the Tunisian study as a form of cross border vertical integration from neighbouring countries bringing in further pressures on their markets. Access to European markets through subcontracting relationships with European firms had also exposed the subcontracting producers to the broader range of international market competition.

A way to limit this problem might be to develop marketing activities through the alliance life cycle so that a small subcontractor could learn from the contractor within a relationship characterized by four major stages i.e. embryo, growth, maturity and decline. This development within the business relationship would help the subcontractor to engender significant competences by learning from their partners. Qualitative research was carried out to explore such activities with seven subcontracting firms and the main results demonstrated that the life cycle stages of the subcontracting firms reflected Schumpeter’s creation and destruction cycle of innovation. For example, in the declining phase the findings from the in-depth interviews showed that some firms had become more successful than others in avoiding signs of ageing in the Tunisian clothing and textile industries. The implications from this were that the subcontracting firms could learn from their activities with their business customers to engender marketing competences earlier on in their innovative processes.

2 Nature and diversity of alliances

The cooperation model of the Japanese Keiretsu of the 19th century is an example of an old alliance phenomenon which formed the backbone of the beginning of the growth of Japanese advances into international markets and the resulting expansion of Japanese firms. In the 1990s these alliances reached an annual growth average of 25% (Inkpen, 1998). There has been a multiplication of alliances in the last three decades as a response to the increasing complexity of the environment. Digging into the plurality of firms’ relationships one could detect other explanatory principles in these organisational changes which were purely capital intensive. Based on organisational theory (Coase, 1987; Coriat et al, 1999; Williamson, 2002), alliances can be explained by the
triptych: constraint theory, demand characteristic and the market contestable theory. The triptych will be further examined in the paper. From the history of organisational alliances firms would be keener to cooperate in order to overcome supply and demand difficulties. Risk avoidance was an explanation in the literature for the diversity of alliances as firms cooperated in sharing their skills and resources to further their market gains.

In Tunisia the experiment of alliances between firms started in the early seventies, in particular with the promulgation of a 72/38 law essentially concerning the manufacturing firms. Commonly known as the 72 law it gave majority advantages to those firms that were labour intensive and exporting companies. This allowed Tunisian companies the opportunities to compete with others in the world. This period was a protectionist period for the Tunisian clothing and textile industries. The sector production reached 5,433 million dinars in 2004 compared to 4,647 million dinars in 2000. Investment within the sector was valued at 106 million dinars in 2005 (FIPA 2005) with foreign direct investment in Tunisia constituting 61.6 million Tunisian Dinars (FIPA, Tunisia 2005). Labour cost remained the major factor embracing the Tunisian clothing and textile industries. Tunisia has been a signatory to several agreements, such as the association and free trade agreement with the EU, bilateral agreements instituting progressively a free trade zone with several Arab countries and an agreement with EFTA countries. Easing investment in textile and clothing industries included giving the possibility to foreign investors to hold up to 100% of capital in an undertaking without authorization, the facility of the procedures for setting up a business and the investment incentives code in order to reinforce the competitive position of Tunisia. The end of the Multi Fibre Arrangement (MFA) 1st January 2005 where Tunisia lost its favoured export market status in the European Union exposed Tunisian clothing and textile firms to the vagaries of international market competition and impacted on the country’s foreign exchange earnings and job creation. Without protection the industries faced intensified competition in the post-MFA era e.g. from China, India and other important producers, who free of quantitative limitations, could increase their production and exports.

So there is a case for SMEs to go for alliances, essentially in partnership relationships. On 29th March 1995 Tunisia became Being a member of the World Trade Organisation since 29th March 1995 has not buffeted Tunisian industries from the effects of globalisation, the credit crunch and worldwide competition. In 2001 the sector represented a world volume of exchanges of more than 350 billion Dinars (CEPEX 2003). Tunisia is facing problems in its infrastructure with the scarcity of raw materials and sophisticated equipment even though it is labour intensive. The textile industry is deeply grounded in Tunisian habit and culture. Nowadays, the textile industry constitutes an important source of currencies, that is, at a rate of about 40% of the total of exports over the period of 1999-2003 (CEPEX 2003). The industry includes more than 2000 companies including at least 700 firms in subcontracting partnerships with foreign firms.

From the literature concerning alliances relevant explanations are proposed. Based on these explanations, we will try to understand the marketing changes under the angle of a triptych: competences marketing, adherence to the marketing concept and the integration level of the marketing function within the organisation (Achrol et al, 1999) with regard to the study reported in this paper. This is because such triptych changes may have strategic
implications on the alliance life cycle leading to another organisational innovation and thus to a new organisational form (Webster, 1992, Spekman et al, 1998). Subcontracting as an inter-firm alliance contributed to advance common members’ interests (Merriam-Webster's 1995). As any inter-firm alliances were effectively innovations for firms they could have varying forms, with a limited life, dependant on the objectives of the partners. The use of the life cycle concept, already widely used in research in management and, in particular, in marketing could be an interesting approach to distinguish marketing competences’ changes through the constitutive stages of the alliance life cycle. In practice, if it is difficult to distinguish between these stages, the life cycle approach would allow suitable strategic choices in the level of each stage.

3 Developing competences

A classification of the different subcontractor types based on criteria such as technical autonomy, relationship duration and the aim of collaboration is provided by Aoki (1988). This gave a framework in which a subcontractor could develop distinguishable competences. The implications were mainly on technology development and diffusion (Wong 1991). Langlois and Robertson (1995) classified firms’ networks according to the degree of coordination integration and the degree of possession integration. Firms’ networks operating in the textile and clothing industry were, according to this classification, "industrial districts" characterized by a high degree of coordination among the members of the networks. The level of competition was relatively high and the barriers to entry and exit were low. In addition, distinctive competences were at the heart of the performances of firms within the networks. Competition was limited to certain activities where firms concentrated on engendering distinctive competences (Lazerson, 1988, Malerba, 1995).

The theory of the firm within the literature has been the subject of critical interpretations of innovations and of the development of marketing within the organisation. For example, the neoclassical firm offered little potential for the development of marketing skills because competition was basically led by production. If all what was produced was bought by the end consumer there would be little need for marketing investment. The transaction costs theory gave a theoretical model explaining inter-firm links. According to Williamson (1995) the use of alliances would be an interesting illustration of transactional cost theory. Firms contracted alliances when neither the market nor the organization of transactions within the firm was able to minimize the total cost of production and transaction. Alliances were an option when an organization might suffer from the opportunism of its partner if it decided to use the market to buy a component and when production costs and organizational costs were internally very important. This theory gave a new dimension to marketing within the firm. Under the alliance-hybrid form of organization, the main issue was to coordinate the activities of two organizations in a way to minimize production and transaction costs. The role of information in coordinating activities between the two partners became very important. It reduces the problem of uncertainty and complexity. It partly minimizes the opportunism of the co-contractors. Marketing draws from this reasoning of legitimacy because although it has no direct connection with production it provides important relevant information, reduces
the problems of coordination of activities regarding opportunism and risks due to uncertainty issues.

According to the Schumpeterian economic evolution (1939) the organisation becomes the result of successive innovations (see also Munier, 1999). Thus the subcontracting firm is an organisational innovation and a type of inter-firm alliance. Breshi et al (2000) stated that a technological regime can be explained as a combination of specific technological opportunities given the suitability of innovations, technical advances and a knowledge base. The particular pattern of innovative activities in an industry could then be explained as ‘the outcome of different technological (learning) regimes’. Schumpeter’s cycles are based on processes of economic transformation consisting of growth and non-growth phases. The internal change which characterizes the economic evolution is caused by innovations concerning products, production and marketing methods, new markets, new raw materials or semi-finished products.

Founded by R.R. Nelson and S.G. Winter (1982) the evolutionary theory of the firm suggests a general theory of change in the economy offering an analysis based on the behaviour of economic agents drawn from the concept of biological evolution. The evolutionists consider that any theory of the firm must meet two basic issues: the firm’s internal constitution and its dynamic external nature. The evolutionists put emphasis on the aspects of cognition and learning as key determinants of the behaviour of the firm. They draw from Williamson’s analysis, but retain from the Schumpeterian approach to economic change the cyclical nature and its volatility. The evolutionist firm’s boundaries consist of an optimum of skills combination leading to the best strategy choice. The firm optimizes the strategy option by looking for skills inside and outside its organisation. The irreducible form of the firm would then be the result of an optimal mix of skills specific to the company and its external environment (Ejermo, 2005; Evangelista et al, 2006; Lin, 2008).

Through Schumpeter’s ideas evolutionists explain organisational innovation as a new combination of existing organizational routines, or as the introduction of new routines. This new combination determines the firm’s boundaries. Breshi et al (2000) in their study gave supporting empirical estimates of indicators to the Schumpeterian patterns of innovation such as the ‘concentration of innovative activities, stability in the hierarchy of innovators, importance of new innovators and other variables explaining technological outcomes.

For Amit and Schoemaker (1992) and Langlois (1994) adaptation to the environment requires a reconfiguration of a firm’s assets and the ability of the company to learn and develop skills. This requires constant monitoring of markets, continuous monitoring technology and the will to adopt best practices. This often causes enormous costs for the company.

The monitoring of markets and technological developments require the ability to quickly identify changes in the environment, assess the impact on the markets and to anticipate competitors by appropriate adaptation. Doz et al (1987) and Mody (1993) highlighted the collaboration and partnership as supports for new organizational learning to cope with the constraints of the environment. The alliance framework provided allowed the firm to complement missing skills and competences that were necessary to cope with environmental constraints. The alliance is a strategy that could be considered as
distinctive competences, a routine, facilitating organizational learning and development of new routines through a partner’s effort and synergy. Organizational behavior was also regarded as an important consideration (e.g. (e.g. Spekman et al 1998).

4 A life cycle approach

The life cycle approach has already been adopted in the field of marketing (the product life cycle and the market life cycle). Recently many researchers tried to apply this concept in researches with firms in marketing (Hill et al, 2002) and in the alliance context. The alliance in this context becomes a created living entity that grows, reaches maturity then disappears. Several approaches have been proposed to distinguish between the alliance life-cycle stages. Some refer to the "wedding" institution and compare the relationship cycle between a man and a woman namely, the encounter, courtship period, getting married and breakdown (Moss, 1994). Others refer to the governance mode within organizations to distinguish between stages (e.g. Heide, 1994). R&D and innovation stages are also contributory factors to the behaviour of firms (Wright and Nancarrow, 2001). In reality an alliance may finish at any stage and even if the relationship continues, it is often too difficult to distinguish between the different stages. Innovation considered in a broad sense, appears as a first step, spread, stabilizes, declines and is subsequently replaced by another phase of new innovation. The concept of the cycle was also in the following disciplines: research and development, organization evolution and growth, production processes, personal relationships and marketing. The theories placed the innovation process at the heart of the cyclical changes. Marketing often connected by literature to innovation plays an essential role in this process (Day 2000). It therefore has a strong relationship with the concept of life cycle of the alliance. The firm thus became a place where several processes meet, shaping the inter-relationships’ structure and the industrial structure. To determine the different life-cycle stages of the alliance is not an end in itself. The purpose is to allow practitioners to make the appropriate strategic choice at each stage.

Moss (1994) compared the inter-firm alliance to a romantic relationship between two persons. Five main stages were considered: courtship, partner’s engagement, living together, reconciliation and maturity. Jolly (2001) proposed four stages in the alliance life cycle as cooperation, the prenuptial processes of courtship and engagement, implementation of the alliance or marriage and the breakdown of the relationship. Heide (1994) focused on the firm’s governance mode to establish three stages of the alliance life cycle: for initiation, to maintain and for ending. Such approaches were in contradiction with McDonald’s (2007) approach to business for which there was no love or hate in contracts since agreement for one party to do something for another party was due to the acceptance of payment.

5 Research approach

An inductive reasoning approach was implemented through qualitative research based on examining the SMEs on a case by case basis reflected through the ethnographic lens. The aim of inductive reasoning is to lead to statements founded upon objective observations (Wright, 2008). The ethnographic approach enabled interpretation of the observable and learned pattern of the subcontractor’s behaviour towards the contractors. This immersive
method led to a better understanding of how key people in each studied company consider the contractor during all the time they have been dealing with it. Besides, this method allowed observation of employees’ behaviour and to have in-depth interviews with them to highlight each contractor’s oriented culture. Secondly, case studies were used in order to build a scenario to tell an account, a narrative or story involving various people and their roles, contributing to learning about a particular situation giving detailed information gathered.

Initially, qualitative research was conducted using in-depth interviews carried out with a sample of eight companies and with at least three key individuals in each company operating in the Tunisian textile sector. This method allowed empirical research to collect a quantity of information on marketing changes within the studied organisations. The advantage of this method was in-depth exploring of the universe i.e. of the decision making persons in companies through the language, the words and expressions which they use. This gave empirical validation through the control of two practical investigations.

Seven case studies using such in-depth interviews were, therefore, conducted with the agreement of these firms which allowed exploration of causality between the alliance life cycle and marketing development. Within the framework of this method we used several tools of collection of information: repeated interviews, observation, questionnaire and secondary research. Within each company, repeated interviews were carried out with at least three key people, the head of the marketing and sales department when he was available in the company, the company’s chief executive and the head of the operational and production department. Besides, in each company, at least two employees were interviewed creating a sample size of 35. A detailed questionnaire was constructed in order to reveal through the alliance lifecycle the implementation and the development of marketing activities within the subcontractor’s organisation. The approach adopted was similar to the marketing audit approach. The marketing performance of the subcontractors was the result of organisational learning through the different partnerships created with contractors with whom they were in the maturity or growth stages. It also took account of the results of previous subcontracting relationships which had terminated.

The in-depth interviews collected rich data about the cases of the selected companies which covered various situations according to their company sizes and relationships with their partners. External validity of the results was assured since they match the kind of information accepted by other people working within the industry. The results received confirmation from more then one information source, such as subcontracting firms, trade associations and government agencies. Besides, the cross-referencing of the research findings through several case studies highlighted the reliability of the results. In this research, triangulation was assured through the combination of several research methods i.e. in-depth interviews, observation, secondary research and a questionnaire used to reach our research objectives.
6 Subcontractors’ description

The above triangulation related to both players and firms. For instance, observation related to interpersonal exchanges in the context of marketing activities, marketing skills and the processes of individual learning. For firms, observation related to policy makers in marketing and those involved in the partnership process. The marketing function was, therefore, observed in detail with the use of the questionnaire undertaken with respondents. Table 1 showed the cases studied. Among the eight subcontractors listed from A to H, seven subcontractors accepted to go through the research process for the interviews. Subcontractor H did not allow us to spend time in the firm and talk to employees. The chief executives of each company were asked to choose a partner with whom they were at least in a mature stage of a relationship.

Table 1: Case studies

<table>
<thead>
<tr>
<th>Firms (Cases)</th>
<th>Starting date</th>
<th>Products</th>
<th>Number of employees</th>
<th>Main partners</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>1983</td>
<td>Denim trousers, suit trousers</td>
<td>1500</td>
<td>Ober</td>
</tr>
<tr>
<td>B</td>
<td>1982</td>
<td>Denim trousers, suit trousers</td>
<td>2000</td>
<td>Est/West</td>
</tr>
<tr>
<td>C</td>
<td>1996</td>
<td>Under wear Clothes</td>
<td>300</td>
<td>X</td>
</tr>
<tr>
<td>D</td>
<td>2001</td>
<td>Small mesh</td>
<td>300</td>
<td>Livet</td>
</tr>
<tr>
<td>E</td>
<td>1982</td>
<td>Suit trousers, men suits, men and women clothes.</td>
<td>2000</td>
<td>Weil</td>
</tr>
<tr>
<td>F</td>
<td>1992</td>
<td>Suit trousers, men suits, men and women clothes.</td>
<td>700</td>
<td>Marzotto</td>
</tr>
<tr>
<td>G</td>
<td>2003</td>
<td>Clothes</td>
<td>200</td>
<td>123</td>
</tr>
<tr>
<td>H</td>
<td>1996</td>
<td>Lingerie</td>
<td>150</td>
<td>Charlotte</td>
</tr>
</tbody>
</table>

7 Findings

The findings demonstrated several stages in the subcontractor and partner relationship. These stages differed in terms of the added value to a partner’s interdependence level, specific assets allocated to the relationship, the relationship quality and the partner’s behaviour. The emerging subcontracting life cycle as drawn from the studied firms more or less confirmed what was stated in the literature, where firms needed the switch to a
stronger partnership model of relationship. Five main stages were evidenced in the empirical research: Negotiation or embryonic stage, subcontracting stage, “control ready to wear” stage, “ready to wear” stage, end consumer approach and selling to the end consumer. We kept the subcontractors’ words to characterize the different stages. During the first stage all of the subcontractors studied showed an emphasis on negotiation with the contractor. Generally, it took two seasons to establish and implement a relationship. That was nearly the equivalent of six months, but there were four main seasons in the clothing and textile industries: summer, fall, winter and spring. During the second stage all of the subcontractors studied complied with subcontracting in its narrow meaning. They produce products according to specifications given by the contractors who paid money in exchange. The firms did not show any sign of initiative in the production process during this stage. They were specialized in production activities and were not interested in developing any other activities. After several years the relationship moved to another stage commonly called “control ready to wear”. The subcontractors were closer to their contractors while at the same time they felt more confident in introducing other activities in the company, such as product design. But the contractors still controlled the major activity of overall control of the products and retained oversight towards them. In the fourth stage they were more confident and had learnt from their previous experience with the contractor. Four of the cases studied showed marketing capabilities learned through organisational interaction. They became even more efficient then their contractors, which they called partners at this stage, for some of the activities e.g. logistics.

Through the subcontracting life cycle, marketing could play a major role in both senses: marketing could be a facilitator for this life cycle process and marketing improvements could result from the evolution of step to the other, but the experience could also be shortened. As an example, Firm B felt mature enough to concentrate directly on the final consumer, but this experience lasted for one year only. Firm B decided to sell its product (denim trousers) to the French consumer choosing a French city as a test market. After one year the firm had earned enough profit to state that the experience was positive. But the chief executive decided that this experience should be suspended because he felt there was no reason to disperse the firm activity at that moment. He said “after one year we had made enough profit from this venture to say that it was a success, but we have decided to suspend this exercise as we do not wish to dilute our business at this time. We may seek to look again at this business opportunity in the near future when we will feel it will suit our business”.

The contribution of marketing to the subcontracting organization was considerable. We can assess these contributions through the organisational level of involvement with the marketing concept, the organisational marketing competences and through the marketing function’s integration within the organisation. The following table showed differences in performing marketing activities in both maturity and growth stage of the relationship from the percentages of occurrence in the 35 interviewees’ discourses, as given. From the growth stage to the maturity stage the percentages highlighted a bigger emphasis on marketing in the maturity stage. In the maturity stage the studied organisation had learnt from interaction with their subcontractors to develop marketing activities.
Table 2: Stages of growth versus maturity

<table>
<thead>
<tr>
<th></th>
<th>Growth stage</th>
<th>Maturity stage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales department in the organisation</td>
<td>87.5%</td>
<td>50%</td>
</tr>
<tr>
<td>Marketing department in the organisation</td>
<td>12.5%</td>
<td>37.5%</td>
</tr>
<tr>
<td>Use of secondary information/specialised information providers</td>
<td>12.5%</td>
<td>25%</td>
</tr>
<tr>
<td>Use of informal information sources</td>
<td>87.5%</td>
<td>37.5%</td>
</tr>
<tr>
<td>Relying on communication by word of mouth</td>
<td>50%</td>
<td>37.5%</td>
</tr>
<tr>
<td>Information &amp; communication technologies</td>
<td>12.5%</td>
<td>25%</td>
</tr>
<tr>
<td>Contractor=Client</td>
<td>75%</td>
<td>25%</td>
</tr>
<tr>
<td>Contractor=Partner</td>
<td>37.5%</td>
<td>62.5%</td>
</tr>
<tr>
<td>«Travail à façon »: the narrow meaning of subcontracting</td>
<td>87.5%</td>
<td>37.5%</td>
</tr>
<tr>
<td>Finished Product</td>
<td>12.5%</td>
<td>62.5%</td>
</tr>
</tbody>
</table>

8 From embryonic to maturity stages

Table 3 reflected the research results to show the degree of evolvement and integration level leading to the development of competences during the alliance life cycle stages.

Degree of evolvement to the marketing concept

Embryonic stage: SME firms had been introduced to their contractors either through public institutions such as the Ministry of Commerce or through other members of the supply channel. In Tunisia the cheap labour costs provided the country with a high level of demand for manufactured clothes. Subcontractors had no need to perform activities in order to find customers. Finding capital for their manufacturing activities was their problem. Only one firm (G) among those studied started with marketing. The chief executive stated “our key role was to satisfy our customers with an appropriate offer. Understanding the behaviour of the end consumer towards current and future fashions was crucial to our future marketing strategy”. This firm had a marketing department linked directly to the top management. The other firms did not have a marketing department during this stage. The senior managers of A, B, D and F stated that the reason was the lack of marketing competences and the lack of resources. For firm C the head manager explained that marketing was not necessary and the firm’s objective was to
enhance productivity. He said “our main activities and investments were focused on productivity and not marketing as we do not think it is a necessity”.

Table 3: Marketing evolvement, integration and competences in the alliance life cycle

<table>
<thead>
<tr>
<th>Life cycle stage</th>
<th>Degree of evolvement to the marketing concept</th>
<th>Integration level of the marketing function into the organisation</th>
<th>Competences in marketing</th>
</tr>
</thead>
<tbody>
<tr>
<td>Embryonic stage</td>
<td>For all the enterprises, but not G:</td>
<td>For all the enterprises but not G:</td>
<td>For all the enterprises, but not G:</td>
</tr>
<tr>
<td></td>
<td>The companies initially sought to find customers for their offer of “travail à façon”.</td>
<td>Marketing activities were reliant on the company head.</td>
<td>Low level of competences regarding awareness about the market place. Communication action through word of mouth and identity media were important</td>
</tr>
<tr>
<td>Growth stage</td>
<td>For all the enterprises, but not G:</td>
<td>For C and D:</td>
<td>For A, B, C, D, E, and F:</td>
</tr>
<tr>
<td></td>
<td>Companies concentrated on their immediate customers and learnt how to satisfy their needs and expectations.</td>
<td>- Marketing activities were reliant on the company head. For F:</td>
<td>- more interaction with partners</td>
</tr>
<tr>
<td></td>
<td>- Difficult confrontation with the conditions of costs of quality and timing.</td>
<td>For F: - Sales department</td>
<td>- strict meaning of subcontracting</td>
</tr>
<tr>
<td></td>
<td>- Contractor = customer</td>
<td>For G:</td>
<td>- Identification of the sources of competitive advantage (price, quality, respect of the deadlines)</td>
</tr>
<tr>
<td></td>
<td>For A, B, C, D, E, and F:</td>
<td>For C and D:</td>
<td>- Competences related to the actions within the market place</td>
</tr>
<tr>
<td></td>
<td>To satisfy customers targeted by an adapted offer.</td>
<td>For F:</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>For G, A, B, and E:</td>
<td></td>
</tr>
<tr>
<td>Maturity stage</td>
<td>For C:</td>
<td>For C and D:</td>
<td></td>
</tr>
<tr>
<td></td>
<td>The subcontractor concentrated on the immediate customers and learnt how to satisfy their needs and expectations.</td>
<td>- Marketing activities are reliant on the company head. For F:</td>
<td>- Competences relating to the action within the market place (weak)</td>
</tr>
<tr>
<td></td>
<td>- Rather difficult due to confrontation resulting from the conditions of costs of quality and times.</td>
<td>For F: - Sales department</td>
<td>- Competences relating to awareness about the market place(weak)</td>
</tr>
<tr>
<td></td>
<td>- Contractor = customer</td>
<td>For G, A, B, and E:</td>
<td></td>
</tr>
<tr>
<td></td>
<td>For A, B, E, G, and F:</td>
<td>- Marketing department</td>
<td></td>
</tr>
</tbody>
</table>

**Growth stage**: During this stage firms concentrated on their immediate customers. They gradually learned how to satisfy their customers’ needs and expectations. However, contractors were considered as customers. They imposed on subcontractors the manufacturing specifications. The first subcontractor’s objective was to comply with
these specifications. Interactions with the contractors progressively led the organisations to integrate. This interrelated their decision making processes. The firms studied showed development of special capabilities in coping with the contractors’ specifications and expectations.

**Maturity stage:** During this stage the level of interdependence of companies increased. This was noted in the following partnerships: A/Ober, B/Est Ouest, E/ERFO and F/Marzotto. For firm C the contractor was considered as a customer even in the maturity stage. The first implication of this specific case was that maturity doesn’t necessarily mean closer relationship. From the analysis of secondary data this firm was found to have a specific duration in its relationship with all its previous contractors which did not exceed five years. The chief executive/head manager of this company which was majored in textile engineering was not aware about the importance of marketing activities within the organisation. For firm D marketing activities were not performed within the organisation because of the lack of resources.

**Integration level of the marketing function into the organisation**

*Embryonic stage:* G was the unique company which started with marketing department. The other companies did not have this department during this stage mainly because of two reasons: the lack of financial resources and the managers’ lack of awareness. Often, marketing activities were consciously or unconsciously deployed within the organisation by the head manager or by the senior sales manager.

*Growth stage:* Interaction with the contractor consists of repeated transactions. Gradually the subcontractor showed increasing ability to implement business strategies. This led the subcontractor to use methods related to sales management. The organisations showed at this stage “a sales department “, using the proper terms of the respondents, rather than a “marketing department” dealing with the contractor’s needs. Firms A, B, E and F were in this situation. For C and D managers were struggling with the contractors’ needs. Firm G had its marketing department created at the beginning of the relationship with the contractor.

*Maturity stage:* Reaching this stage companies A and B created their marketing departments in order to study the partner’s needs and to better satisfy them. These companies had enough financial resources to implement the final consumer oriented strategies. C and D did not set up their marketing department at this stage. For A and B the integration level of marketing within the organisation was higher. The managers’ awareness as well as the financial resources were the main reasons.

**Competences in marketing**

*Embryonic stage:* Subcontractors’ inside-out competences were not important at this stage. The relationship between both organisations was not effective at this negotiation stage. The companies studied evaluated the client/contractor needs and confronted them with their own manufacturing capabilities, such as their production capacities and their employees’ know how. The studied cases showed however, that the more the subcontractor multiplied his customers, the more he acquired an ability to negotiate more effectively with clients. The companies’ communication strategies, except for G, were
mainly by word of mouth. Nevertheless, all of them paid special attention to the identity media such as employees’ business cards, in-house financial documents, employees’ uniform and the buildings they occupied. The contractors evaluated the subcontractor’s image and willingness through these elements.

**Growth stage:** At this stage the subcontractors effectively started to learn about their contractors and to meet their needs. The more they interacted with the contractors the more they developed the ability to satisfy customers’ expectations. As a result they were able to identify different sources of competitive advantage. During this stage the subcontractors worked according to the narrow meaning of subcontracting. They manufactured products according to specifications imposed and controlled by the client. Mistrust and hesitation were characteristics of the relationship between both actors during this stage e.g. the contractor could try to exacerbate competition between the subcontractors in order to have the best prices. Marketing competences were limited. In the long run this situation could marginalize the companies because they were likely to be entirely kept apart from what was happening in the market place and the firm’s external environment.

**Maturity stage:** The multiplication of the transactions led the subcontractors being better able to control the relationship with its partner. In the maturity stage the companies developed external competences leading them to a better understanding of market expectations. They also developed monitoring processes over the external and internal processes. Furthermore, the relationship between parties evolved towards closer partnership. Those interviewed qualified their contractors as partners and not as clients. The organisational learning allowed the studied companies, particularly A, B, E, and G to reinforce their marketing competences. Some of them developed further activities towards the final consumer. To a certain extent these companies showed the ability to develop other marketing strategies. They showed signs of aging in the subcontracting life cycle and have subsequently to be in a better position in their international markets.

9 **Conclusions**

The results emerging from the case studies showed that choices by the firms depended on their ability to identify the transformation processes (e.g. marketing processes) taking place in the organization. The more aware the company was of these processes, the more the company was able to redeploy its activities. The corporate networks within the textile and clothing industry included several stakeholders’ activities as a result of the addition of several relationships between firms. Each member of the network could choose between two strategic options: integration or operating within the network. According to both transaction cost theory and evolutionary theory of the firm, the choice depended on the arbitration between the costs of coordination and the costs of adaptation to the marketplace at one side while on the other side this choice was influenced by marketing competences missing in the firms and their need to compete in the marketplace.

Organizational learning and the business culture go hand in hand. Future research could examine the importance and differences of business culture in the contractor-subcontractor relationships within other industries in Arab GCC countries and the West.
The alliance lifecycle concept is relevant where enterprises need to have stability to engender growth and continuity. The study could provide a framework for comparative research in the GCC countries to examine how organizational learning and motivation to form alliances can lead to building marketing competences. There is support in the literature for the evolutionary theory of the firm as a strategy, “a routine” developed by an organization which would lead to the development of other routines through the organisational learning process. These would lead to other strategic choices for firm and the development of new routines. It would be interesting to see how marketing competences developed during the stages of life stages can become distinctive routines, inducing competitive advantages for smaller entrepreneurial firms in the GCC states.

The literature review and the study showed important considerations about the subcontracting activity for firms in general moving through the stages of maturity and to strategic redeployment. As the current financial crisis emanating from the USA and affecting many countries have shown there are many vagaries in the international business environments facing many enterprises. Even oil rich Arab GCC countries were not immune to the problems of reduced demand in international markets as the financial crisis affected markets from West to East in 2008 with forecasts of increasing recession in 2009. However, the nature of skills deployment in partnership arrangements and the building of closer business relationships could be a source for future study to examine growth, regeneration and the continuing existence of greater diversity in businesses for the GCC countries in a global era.

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Sales Optimisation in Key Accounts

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Abstract: This research plans to show differences between sales negotiators and researchers about key accounts. This study evaluates the state of the art in key accounts and shows analysis differences for quantitative work to come.

Key words: key accounts, sales, sales negotiation, salespeople.

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Introduction:

Sample.
Research on key accounts was initiated with 20 companies belonging to the fields of industry (world leaders of gas, technology, phone, railway transportation, data processing, aeronautics, glass), services (advertising and promotion agencies) and mass consumer products (animal food, detergents) selected in Bournois, Rojot and Scaringella (2003) and Lacoste (2006). The objective was to find a better understanding of negotiation by key accounts salespeople.

Methods.

People in charge of key accounts were interviewed with open questions with the assistance of a guidebook. Companies preferred confidentiality in order to be able to answer honestly, without fear that the answers given could be detrimental to their activity or risky for their strategy.
The questions related to our research, i.e. to what point the realities observed by key accounts salesmen correspond to the theoretical approaches of researchers, are:

Do the needs expressed by companies match to the client’s strategic axis? How is it possible to improve this trend? Do organizations make it possible to optimize sales effectiveness? What is the impact of salespeople, lobbies, hierarchical commitment?
in the success of the operations? What is the key accounts managers’ mode of evaluation? How can projects progress in Europe or internationally?

We examine how to develop needs in favor of clients.

1. Optimization of need assessment.

The process of negotiation introduces, according to the group of experts, a distinction between assessment of needs for traditional offers and for complex sales tenders.

1.1. Search for solutions
The search for solutions is analyzed differently according to researchers and negotiators.

1.1.1. Work of researchers
A sales offer answers a clear request for a product or service. It is accessible through the call of a salesperson, Internet browsing (Méot 2008, Aimetti, 1997, Aimetti in Bloch and Macquin, 2001) the reading of a catalogue reading or calls to a local distributor.

As an answer, key accounts salespeople will be brought, (Page, 2002), to build a specific solution. It must satisfy client’s expectations by proposing a competitive, different and strategic recommendation with respect to competitors. Negotiators will look for, according to Lascoumes, Bourhis, (1997) processes of decision-making, stakes, purchasing policies and strategic sales plans. They may also develop good relations and try to discover significant personalities in decision maker teams according to Wysocki, (2001) and Hambrick (2001), Blanc-Le Gall (2006).

1.1.2. Key accounts Negotiators.
According to telecommunications and advertising-promotional agencies key accounts managers’ needs are not clearly expressed and/or not thought of in an explicit way by clients. The latter are limiting their scope to their own problems and do not take into account other possible factors or alternatives. The selling company, however, will help its client to position its questions under a clearer point of view.

In the field of chemistry, need assessment is built around good transversal relations between partners intervening at various stages of products design and development. These good relations help to obtain strategic information through rather friendly relationship. They grow around task forces teams, which help to discover the more influential members of organizations.

In the field of data processing, the development of solutions generally leads to a strategic partnership, considering the visibility of specific needs as well as the availability of information, software and tools used by Management.

This knowledge of business by key account salespeople goes well beyond expressed needs. It offers a view of a whole team, including its leaders. This people’s approach widens the points of view and produces new needs.

The measurement of customer requirements, all fields considered, shows the importance of a partnership between various people intervening in the negotiation process. Key account salespeople show their strategic dimension when starting a negotiation. In
general, authors are more interested in organization and clients than of an integrated process. In the following paragraph we concentrate our analysis on management of tenders in the following paragraph.

1.2. Management of tenders

The response to tender is broken up, according to experts, into two distinct parts: the initial expertise and the preparatory project.

1.2.1. Initial expertise

1.2.1.1. Work of researchers
Contributing greatly in this field, Colla (2001), underlines the new cooperative relations of suppliers and draws our attention to “category managers”, real key account salespeople working with and at distributor’s.

1.2.1.2. Negotiators point of view

Launching an initial expertise within the client’s company makes it possible to evaluate the costs of preparation and of marketing tests. It provides a good indication of investments by prospected clients. In the data-processing field, a company created a "sales plan" for every prospected company. This stage and the evaluation of the 3-to-5 year profitability was decisive in the making of a tender. One of the companies interviewed, which refused large industrial contracts not immediately profitable is today in liquidation in spite of products of international recognition. In the field of mass consumer products, answers underlined the price for referencing new products. Table 1 recapitulates these elements and shows that the financial aspect is a significant point.

Table 1: Management of tenders.

<table>
<thead>
<tr>
<th>Field of activity</th>
<th>Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gas</td>
<td>Expensive preparatory expenditure</td>
</tr>
<tr>
<td>Technology</td>
<td>Expensive preparatory expenditure</td>
</tr>
<tr>
<td>Chemistry</td>
<td>Expensive preparatory expenditure</td>
</tr>
<tr>
<td>Data processing</td>
<td>Sales plan</td>
</tr>
<tr>
<td>Consumption</td>
<td>Price of referencing</td>
</tr>
</tbody>
</table>

1.2.2. Preparatory project

According to key account managers (regardless of their activity), preparatory expenditure can be measured in millions of Euros or Dollars. The motorway program called Sirius in France, for example, built by the Direction de l’Equipement (Highway Company Management) received 3 companies as candidates, for this preparation. Two were not selected. This project required a heavy adaptation and preparatory work and a high cost, without guarantee of result. This effort is the result of a managerial implication, a success policy and the knowledge of the field by manufacturers. It also results from a good preparation upstream. Indeed, the drafting of specifications during the preparation phase...
20% of paid preparatory studies and 80% not paid) increased the likelihood of success during the launching of a tender.

Key account negotiators measure costs to be paid for negotiations. They help their clients to position themselves and develop partnerships. They also take part in drafting specifications for tests, pushing manufacturers to find a satisfactory/advantageous solution.

Theoretical studies rather highlights responsibilities for teams and influence of people in the negotiation processes.

We continue our study by measuring the added value in clients’ expectations.

2. Negotiation with added value: influence of clients’ expectations?

We shall examine these various points according to clients’ answers, prospects, creation of partnerships and source of efficient negotiation.

2.1. Simple questions for complex answers

2.1.1. Work of researchers

The price makes it possible to increase sales (Falque, Tshiember, 2001), Houver,Vandoeuvre (2006) and stresses the importance of the answers designed specifically to clients.

This is the reason why key account salespeople will try to build a project where their contribution will be recognized. Leroux (1993) and Stake (1988) confirmed this situation. They underline the effective implication of key account salespeople in the solution suggested by their company as one of their hidden dimensions in negotiation.

Negotiators associate simple processes and solutions. They build a link between company quality and policy, and capital evaluation (Hermel, Louppe, 2002) in order to improve their approach among company alternative purposes.

2.1.2. Negotiators point of view

In the industrial field, projects set up by suppliers are developed to better meet the expectations of client. They are different from the client’s initial interrogations and make it possible to better answer a client who may sometimes lack of perspective.

In the field of mass consumer products, simple questions often result in complex answers.

In the field of services, evolution towards more creative solutions increase the chances to retain client. When client perceives a solution as simple, they try to manage without a supplier. For this reason, key account salespeople will always build a project with a strong personal implication, which is essential for success.
Nevertheless key account managers do not merely function and lead their activity on complex projects. Table No. 2 stresses the importance of the links between a negotiator and his client.

Table no. 2: Negotiation with added value

<table>
<thead>
<tr>
<th>Field of activity</th>
<th>Organization</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gas, aeronautics, railway</td>
<td>Transverse organization</td>
</tr>
<tr>
<td>Telecom</td>
<td>Transverse organization</td>
</tr>
<tr>
<td>Agencies of promotion and publicity</td>
<td>Additional offer</td>
</tr>
<tr>
<td>Chemistry</td>
<td>Development strong partner</td>
</tr>
<tr>
<td>Data processing</td>
<td>Development strong partner</td>
</tr>
<tr>
<td>Consumption</td>
<td>Simple questions producing complex answers</td>
</tr>
<tr>
<td>Services</td>
<td>Search for creative solutions</td>
</tr>
</tbody>
</table>

Key account salespeople show a true capacity of reading strategic organizations. Authors would rather highlight company policies and hidden resources.

We continue the analysis with the management of prospection.

2.2. The management of prospection.

During the prospection phrase, key account salespeople will try to create a privileged relation, Thuderoz and Bourque (2002), from "how" (the way whose individuals are likely to negotiate) to "why" they negotiate.

This explains why salespeople become managers. With the image of “sailing ship skippers”, salespeople can motivate their clients (“team-members”) by “requiring always more” (Py, 2001) or “communicating better” (Salzer, Romano, 1991).

For this reason, a complete file on each client, before launching any operation, can supplement a list of prospective customers. Such detailed lists make it possible to start tests or develop research agreements. Suppliers can also make cultural and behavioral revolutions with their clients by developing huge training efforts.

Key account salespeople organize their operations in a dynamic sales development process. Researchers are more interested in communication between people and organizations. From this salespeople-and-client framework an association can be built on a strong partnership.

2.3. Development of a strong partnership

The development of a strong partnership makes it difficult to operate modifications and build a long term partnership. The presentation of an offer in the context of value chain gives a better indication to measurement of performances (Ittner, Larcher, 2001), accentuates understanding and develops added value. This increase of added value results gives a wider scope and an offer in line with strategy.
This dialogue between suppliers and customers highlights factors of differentiation, sources of increase in added values, as Macquin (1993) underlines when showing a composite sales team management including pure salespeople, sales services, and category managers.

*Complexity, enrichment of information, strong stakes, a more complete view, a strong dialogue support, and a better value added for clients help build a better relation with the client.*

A good negotiation will succeed if it is well organized. The following chapter shows the factors of organization of the negotiation.

3. An organized negotiation: does organization optimize sales effectiveness?

We will examine the organization of sales protocols and sales plans, then of the qualification of clients, finally of the client itself.

3.1. Tests, protocols, sales plans

*In the field of services,* the presence of competition on the field and a good knowledge of the deciders’ flow chart make it possible to start tests or protocols with prospective clients. They allow the evaluation strategies over a period of 5 to 6 months or more. Key account managers will anticipate and animate changes related to the client’s orientation. They operate quicker than others.

*Among every industry,* the negotiation is organized upstream around sales plans, in transversal workshops (where the schedules of conditions on component parts to implement are defined), whereas in *the processing industries,* there is no particular technique or methods of organization. Table 3 synthesizes these elements and shows the importance of up to date information and bilateral relations.

<table>
<thead>
<tr>
<th>Field of activity</th>
<th>Relational sales</th>
</tr>
</thead>
<tbody>
<tr>
<td>Services</td>
<td>Research of the most up to date flow chart.</td>
</tr>
<tr>
<td>Industry</td>
<td>Task force and workshop.</td>
</tr>
</tbody>
</table>

Key account *salespeople show their implication with clients and precision of their action when they intervene directly in supplying spare parts in “advanced workshops”.* *Researchers underline this proactivity.*

3.2. Qualification of clients

Key account salespeople consider that the qualification of a client is measured thanks to good feed back and information collected from different sources (through the crossing of information). This type of information can be also reviewed thanks to data collected by the client’s suppliers. They contribute to the quality of this information and give
indications about the influence of people when significant decisions are taken. Scheelen, Lévitte (2001), Platnic-Cohen (2005) define, for example, 8 types of personalities: driver, motivator, appraiser, promoter, supporter, organizer, facilitator and coordinator. They can help with a better classification.

This influence can be visualized by purchase process matrix for each company or service (Pardo, 1999). Key account salespeople also set up repertoires of most current methods in multinational groups or “costs and benefits estimation”. Dupont and Audebert (1994) raise some points in their professional applications of negotiation. Key account salespeople develop cognitive tools with their clients. Authors rather seek to classify various interlocutors.

We continue on the clients.

3.3. Clients

The satisfaction of client, control of costs and reactivity are regarded as important points (from the point of view of the client). Key account salespeople must also “surprise” their clients (Diridollou, Vincent, 2001) in order to innovate. To succeed here, according to the latter, it is advisable…

- …to improve key processes, constituting the heart of the trade rather than the only quality. This action rests mainly on people and their competences.
- …to modify the roles and attributions of the manager who becomes a "coach" actor in the promotion, animation and coherence of change.

The information available about prospective customers can also be organized by external companies specialized in key account follow-ups. These companies find names and purchaser functions as well as capitalization and deciders. They can usefully define operational strategies for ambitious suppliers.

Key account salespeople measure competitive efforts, plans of accounts, animation of workshops, access to information, purchase matrices, practices of groups and accurate costs estimation. It produces a better sales development. Researchers propose methods of success.

We examine the evaluation of sales activity.

4. An evaluated negotiation: results to last.

This evaluation is measured in time and according to the results.

4.1. Long term management.

Using the interviews of salespeople, key account salespeople know their clients or prospective customers very well and obtain better results. The people in charge of key accounts establish a management long-term plan (up to 10 years in gas
contracts, for example) by presenting a capital spending program and a profit and operating expenses matrix. The project is then discussed with CEO's.

4.2. A measurement of results

The evaluation of sales managers’ activity generally go through an external company analysis on the following points: competitive strengths, list of stakes over 5 years (in the industrial field) and development of "second sources" (alternative strategies in the changing environment of data processing). In the services activities “post operational measurement” is replaced by "in situ" actions (controls during operations). In the field of mass consumer products annual investigations are organized. Table 4 indicates the various modes of evaluation.

Table No. 4: Evaluated negotiation

<table>
<thead>
<tr>
<th>Field of activity</th>
<th>Evaluation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Industry</td>
<td>Measure of competitive strength. List stakes over 5 years.</td>
</tr>
<tr>
<td>Data processing</td>
<td>Development of second sources.</td>
</tr>
<tr>
<td>Services</td>
<td>Passage of the post operation towards in situ actions</td>
</tr>
<tr>
<td>Great consumption</td>
<td>Annual investigations</td>
</tr>
</tbody>
</table>

The evaluation takes into account a long-term plan, an analysis by external companies, second sources, annual investigations and competitive forces. These subjects are not investigated as much by researchers.


The success of the negotiation depends, according to the people in charge on their practice (in products, fields, companies) and competence - proven results - (fields of chemistry, production, technology and services agencies), of DN (Numerical Distribution, at Secodip meaning % share of products in front of market), DV (distribution Valeur, Secodip meaning % share of places selling products) for mass consumer products. It also depends on whether thenetworksare activated.

5.1. Lobbies

This activity requires information about decision makers, flow charts, contacts, legislative procedures and European investment (Zaragoza, 2001). The interviewed people make a difference between a lobbying of maintenance (management of existing clients) and development (management of prospective clients). A communication plan will show possible enemies (non favorable people) and "locked" personalities (people "held" by competitors) (Lacroix-Sablayrolles, 2002). Balanya (2000) presents three lobbies as examples:

- The 45 members of the “Round Table” (multinational business leaders) influence strongly decisions of European Commission;
The leaders of the largest European and American companies meet together regularly within the “Dialogue on Transatlantic Trade Commission”.

The access to European leaders by the Public Relations company called “Bursin-Marsteller”

Lobbying controlled by key account salespeople is based on influencing networks and grids at various levels (Mermet in Fradet, 2000) and using barter systems as marketing mix tool (Adetem 2002); whereas lobbying managed by the CEO’s transmit less information (strategic aspect does not escape careful managers) (Goupilleau, 2002).

We examine then networks of influence.

5.2. Networks of influence

In Europe, the networks of influence have an enormous weight on economics and politics (Capital 1998). They are organized around the Parliament and Ministries. These networks can be useful in countervailing powers and help to develop projects (Picardy, Adler, Bouvier 2000). The key account salespeople develop other forms of networks. They note that company personnel members belong to a large range of associations that are seldom orchestrated to help prospective research for key account managers (White, 1994). According to latters, the companies miss occasions to approach client on original subjects.

The other personnel members, ie. pensioners, are often a source of relational capital, which deserves to be better exploited. In the opinion of the key account salespeople, these types of speakers are interesting because they are less expensive and more effective than traditional systems of competitive follow up: one day of field analysis by such a personnel make it possible to have a better idea of the situation than a one day report written by external cabinets.

In spite of this situation, the companies spend heavy investments to detect deciders (by building matrix of organization) in order to make better allies (Khan, 2001). This information provides some orientations about business, needs, and mode of organization (centralized or decentralized).

Table n°5: Pro-active negotiation

<table>
<thead>
<tr>
<th>Field of activity</th>
<th>Sales tools</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chemistry</td>
<td>Experiment and competition</td>
</tr>
<tr>
<td>Technology</td>
<td>Experiment and competition</td>
</tr>
<tr>
<td>Services</td>
<td>Experiment and competition</td>
</tr>
<tr>
<td>Great consumption</td>
<td>DN, DV</td>
</tr>
</tbody>
</table>
The activity of key account salespeople during negotiation appears as a search for knowledge associated to markets, a healthy and simple economic approach and responsibility for activation of different networks. Researchers are interested in classification of counterparts, exchanges between partners and detection of favorable personalities.

We widen our work on the European level in what follows.

6. A European negotiation: from market to institutions.
Any European negotiation is working between the needs and constraints of the client (market) and those of the European Community.

6.1. Expectations of market facing European realities

- In Brussels and Strasbourg, the key account salespeople note the following points on decision makers:
  - The decision makers need lobbyists because they do not have time… They must adapt, act or react in front of the European decisions. They need a better definition of their objectives, a measurement of local and global strengths and a good communication (Clamen 2000). But expectations towards the Commission increase significantly between the companies (structured, organized and assisted) or consumers (more voluntary organization). The latter lack sometimes financial support (Alternatives economic, 2002).
  - The decision makers take thousands of different decisions that touch all activities. They take their decisions while resisting to pressures, tactics and strategies of contacts (Korda, 2000). They need European help about legal considerations, choices of objectives, respect of chronology, strategies of conviction (Clamen, 2002)
  - The decision makers group together a large range of information in order to take political decisions. The six studies of Louppe (2003) show through 6 different countries the importance of a common mode of action on various registers in order to reach an optimal effectiveness. The decision makers must also build technical dossiers in a transversal approach of a company, open on upstream (suppliers), intermediaries (European Commission) and downstream (consumers) (Batteux, Freitas, 2002)
  - The decision makers should know several European members of Parliament according to a deontology and a current methodology in the field of influence network (Derieux 2002). However these steps take months of actions and calls (Euroconfidentiel, 2002) in Commission lobby room.

Key account salespeople observe a reinforcement of the European activities and an increasingly large requirement of company partners. Can confrontation between expectations raised on the market and lengthening of procedures due to the 10 new members change the salespeople’s assignments?

6. “Relational engineering“.
The figures of the European Commission (2002) show a difficult task for negotiators:

- The key account salespeople negotiating with the European Commission deal with 3000 organizations, 10000 people (Vayssiere, 2002). The salespeople are led to work with the lobbyers: Belgian lawyers installed in Brussels, foreign lawyers, law firms and specialized organizations (Birkinshaw, 2001).
- Lobbying in Brussels creates a "relational engineering" which connects all activities. It gives a broader answer on industrial level and makes it possible to get interesting information on powerful shareholders, enlightened consumers and influencers often masked (Autret 2003). The data acquisition establishing comparison of 25 European countries gives a good measurement of decisions to be taken on the European level.

The key account salespeople note that the European Commission is an exchange information place between partners from all levels.

6.1. European Institutions.

European management involves managing the two traditional stages of the Commission and Parliament:

- The European Commission: lobbyers can influence, on behalf of a company supplier, in a few minutes, the ideas of European managers, (Guyader, Garcin, 2000), political groups, general secretary, European deputies, Council of European Union, European bank of investment, communauteary organizations, commissions and delegations, European Mediator, European Court of Justice (Trombinoscope of the European Union, 2003)
- The European Parliament: the members of the Parliament examine consistently a project if they watch a report on television, radio or can read the press about the subject studied (media contributing to "good information" of the European member of Parliament, imply a strong communication and action plans on the topics to be defended) (the European Commission DG XXII, 2001)

The communication is a powerful vector of success for the key account salespeople. It helps the companies to transmit more powerful messages.

6.2. International accounts.

The key accounts are defined by several companies like an entity joining together under the same name or different names, a significant number of interlocutors, different trades, multiple sites, signs, local or national, multinational marks or multi-continental for which only multipurpose teams can succeed.

The development of international accounts establishes a "sales and relational intimacy" with contacts immediately accessible in another part of the world. Goupilleau (2002) sweeps media techniques and gives priority to proximity in order to develop communication and allow small companies to improve their client relationships. For the large companies, Kotler (2003) recommends a more intensive development of relational networks and wonders about colossal advertising expenses with weak returns on investment.

6.3. Development of future research
The following points consider the people acting worldwide.

6.3.1. The measurement differential between European and world expectations: how to adapt communication and sales technique according to countries. Chevrier (2000) proposes a management strategy development and responsibility for international teams acting in intercultural diversities. Storti (2001) and Marx (2003) also highlight cultural differences from various types of interlocutors met by the key account salespeople.

- The potential role of European and world users: to develop a pedagogical culture. Alfrieda Daly (1998) underlines it as one of the significant elements in work organization worldwide.
- The development of innovating programs highlights investment to client. Dupriez, Simons (2002) show how to benefit from an innovative cultural diversity and Rapaille (2001) integrates the cultural differences in a marketing strategy.
- A "global" answer for total client (Moulinier 2000) can be managed country by country, ethnic group by ethnic group as Jolibert and Loo (2001) suggest it. Marquardt and Horvath (2001) show how to build confidence, motivate team members, develop and maintain a team direction, build a common vision by converting richness created by cultural diversity into action and innovating thought.
- The responsibility for identification of each member of the Business Unit in the world.
- The coordination of international accounts, with the local sales force in order to create and collect more client value (Rackham, Vincentis, 1999).
- The coordination and control of sales force activities by interface and a strategic sales plan (Gielgun, 2000).
- The responsibility of local communication when necessary for the local sales force (Thibaud, 2000).
- The management of international businesses under multicultural point of view, which introduces the COI (Cultural Orientations Inventory) giving a chance to identify the lack of international team competences (Walker, Walker, Schmitz, 2002).

The research of Jolibert (2001, 2001) (Deloffre (2000) bring good answers on these questions and sales behavior facing international offers: structure of economies, evolution of religions in the world, negotiations with Argentineans, Brazilians, what is recommended to exchange with to Israelis, to avoid with Australians, common points and differences in the approaches of negotiation between three ethnic groups (Malayan, Chinese and Indian) of Malaysia.

The key account salespeople know the difficulties of international trade and seek the answers in the local organizations within a world framework. Authors as Jolibert (2001) bring good practical answers.

The comparative data between the salespeople and researchers are summarized in the table No. 6 which underlines the very broad and exhaustive activity of negotiators and the frequent search of classification and typology of researchers.
Conclusion

The art of negotiation is built on a broad search of resources and expectations of clients. A good understanding of the situation amplifies its effectiveness. It produces a concerted and original solution, carrying strong added value and reactivity.

If we look for a link between reality of the sales activities and research undertaken by authors, the following points (summarized in table 1) appear:
The key account salespeople permanently seek new information about their partners, companies, and clients. They play an in-house advisory role as well as an external one. They detect innovations in complex organizations. They lead their activities with lobby support and world wide as well as European networks of influence.
The authors and researchers show the influence of human aspect in sales functions and the importance of reactivity. They underlined influence of communication with the clients and key account policies. They highlighted the classification of the salespeople and European institutions roles.

The task of the key account salespeople is broad and requires great qualities. Analyzing various sequences of sales activity, authors and researchers help to understand activities of salespeople.

Table 6: Synthesis comparing reports made by salesmen and subjects covered by authors and researchers.

<table>
<thead>
<tr>
<th></th>
<th>Key accounts salespeople</th>
<th>Authors and researchers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Need assessment</td>
<td>The key account negotiators help customers to position, develop partnerships, take part in the drafting of specifications for tests and bring the manufacturer to a solution.</td>
<td>Theoretical study rather highlights teams responsibility and the influence of people in the processes of negotiation.</td>
</tr>
<tr>
<td>Added value</td>
<td>The key account salesmen show their capacity to read strategies and organize in a dynamic process of sales development.</td>
<td>The researchers are interested by communication between people and organizations. They highlight the companies’ policies and hidden resources.</td>
</tr>
<tr>
<td>Customers</td>
<td>The key account salesmen show their implication and precision of their action when they intervene directly in parts spare supply in the advanced workshops.</td>
<td>Authors rather seek to classify the various interlocutors. The researchers underline the proactivity of the salesmen.</td>
</tr>
<tr>
<td>Evaluation</td>
<td>The evaluation takes into account a performance management in an average long term, an analysis by external cabinets, second sources, annual investigations and measure of competition.</td>
<td>Researchers cover these subjects less often.</td>
</tr>
<tr>
<td>Lobbying</td>
<td>A constant effort of lobbying, a research of information associated with the business</td>
<td>Researchers are interested in classification of interlocutors,</td>
</tr>
</tbody>
</table>
concerned, a healthy and simple economic approach, the responsibility of a practitioner to activate different networks. exchanges between partners and detection of favorable personalities.

<table>
<thead>
<tr>
<th>European accounts</th>
<th>The key account salesmen observe a reinforcement of European activities and an increasingly large requirement of companies’ partners. The researchers often privileged the presentation of European mechanisms.</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>International accounts</td>
<td>The key account salesmen know the difficulties of an international market and look for answers in terms of local organization. Authors like Jolibert bring practical answers.</td>
<td></td>
</tr>
</tbody>
</table>

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Evaluating the Relationship between Time-Based Manufacturing Competence and Overall Business Performance

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Craig C. Julian
Southern Cross University
Australia

Abstract: This study evaluates the relationship between time-based manufacturing competence and overall business performance of firms engaged in the steel mini mill industry in the United States of America. The primary data for the study were collected from a self-administered mail survey of 137 firms engaged in the manufacturing sector of the steel mini mill industry. The sample consisted of 71 firms indicating a response rate of 52% and was considered to be adequate. Statistically significant positive relationships were found between time-based manufacturing competence and performance. The surveyed plants were classified into two groups of high performers and low performers, and the means of their time-based manufacturing competence were compared. The results indicate that the high performers have a higher time-based manufacturing competence than the low performers. The findings confirm the assertion in the manufacturing strategy literature which states that time, as a strategic factor, is a source of competitive advantage.

Introduction

Today’s business environment is characterized by global competitive pressures. Traditional competitive factors such as cost and quality are no longer enough to sustain a competitive advantage. Firms must be aware of the many competitive dimensions in today’s market in order to achieve success, and they must be quick to introduce a variety of products, maintain low cost and high quality, and produce products in the least possible amount of time. This means that firms should adopt a multi-competitive advantage orientation which enables them to survive in today’s global competition.

In recent years, time has emerged as a significant competitive factor in almost every industry as few industries in today’s market seem to be immune to time competition. Blackburn (1991) reported that at least one firm in every industry leads in terms of speed of response to the market. As a result of their responsiveness, these time-based competitive firms are emerging as market leaders (Blackburn, 1991).

Time-based firms attempt to transform their entire delivery system into one which focuses on the total amount of time required to deliver a product or service. The key is “time compression,” which not only increases responsiveness, but also enables time-based firms to be more innovative and to produce more variety, with higher quality and lower costs. Thus, time-based firms do not ignore traditional competitive advantages...
such as cost and quality. Instead, they use time to obtain such competitive advantages (Stalk and Hout, 1990).

Flexible manufacturing technologies and time-based programs such as just-in-time and total quality control have been adopted by many firms. By adopting time-based operations without a strategic focus on time, firms will not achieve the objectives of a time-based competitive concept that focuses on the entire delivery system. Time-based operations must correspond to a business strategy that guides all the functions in the organization. Such a business strategy must emphasize time compression throughout the entire delivery system.

The objective of this study, therefore, is to examine the relationship between time-based manufacturing competence and business performance. In recent years, time has been a source of competitive advantage in manufacturing. Responsiveness, reduction in production cycles, and fast delivery are examples of what makes time a source of competitive advantage for firms in the 21st century.

Literature Review

In today’s world-class competition, U.S. firms must adopt a time-based business strategy and a time-based manufacturing strategy (Blackburn 1991). In the competitive environment of the last part of the twentieth century, innovations in competitive strategy have had life cycles of ten to fifteen years (Stalk and Hout, 1990).

Stalk and Hout (1990) traced the evolution of Japanese manufacturing competition, suggesting that Japanese companies’ best illustrate the stages of competition through which today’s leading companies have evolved to obtain multi-competitive advantages. Competition has evolved through several stages.

The first stage of competitive advantage was based on low wages after World War II, and the next stage was based on an economies of scale-based advantage. The source of competitive advantage was then shifted to focused factories. Finally, today’s competitive advantage is based on flexibility, variety, speed, and innovation (Stalk and Hout, 1990). These sources of competitive advantage represent the elements of responsive orientation to a customer’s needs. To meet the needs of today’s customers, competitive advantage has to rely on speed and responsiveness.

In the late 1970s, Japanese companies exploited the benefits of flexible manufacturing to the point that a new competitive thrust emerged, the variety war. During this period, the rate of change in products increased rapidly, and time emerged as a new source of competitive advantage (Stalk and Hout, 1990). Management’s recognition of time’s competitive value has been a key ingredient of Japan’s recent outstanding success in the manufacturing industry. Although time-based competition is a worldwide practice today, Japan continues to provide some of the most tangible and dramatic examples of its benefits which enable Japan to be a leading economic power in today’s global competition (Goldsbrough and Deane, 1988).
Time has become the new source of a sustainable competitive advantage. Today's new generation of competitors has an expanded pattern for corporate success. The traditional pattern provided the most value for the least cost; the expanded pattern provides the same, but in the least amount of time (Stalk and Hout, 1990). This suggests the elimination of trade-offs among competitive priorities. It suggests, too, that firms should focus on time as a means to achieve low cost, high quality, and fast delivery.

Although time is not a new factor in business, time-based management is a new philosophy. While early efficiency experts focused on the best way to do things, time-based competitors focus on the big picture, on the entire value-delivery system (Blackburn, 1991). The goal of time-based organizations is to reduce overall response time. Time-based firms attempt to transform an entire organization into one that is focused on the total amount of time required to deliver a product or service. Thus, time-based firms eliminate the task altogether or perform it in parallel with other tasks so that overall system response time is reduced or compressed (Blackburn, 1991; Stalk and Hout, 1990). Researchers have observed that attention is shifting to speed and time-based competition (Carter, Melnyk, and Handfield, 1995).

Time compression is the essence of time-based competition throughout the organization. The strategic implications of compressing time are significant. As time is compressed, the following changes occur: productivity is increased, prices are increased, risks are reduced, and market share is increased. Companies that build their strategy on flexible operations are more powerful competitors than are companies with traditional strategies that are based on low wages, scale, or focus (Stalk and Hout, 1990).

In most manufacturing facilities, cycle time is inversely proportional to work-in-process turns. As work-in-process turns increase, cycle times decrease. Also, as work-in-process turns increase, productivity increases (Stalk and Hout, 1990). Generally, for every halving of cycle times and doubling of work-in-process turns, productivity increases 20 to 70 percent. As the amount of time required to satisfy customer orders is compressed, prices can be increased also (Stalk and Hout, 1990).

As time is compressed, market risks are reduced. One business cost that is rarely made explicit is the cost of over- or under-forecasting demand. The farther into the future demand must be forecast, the greater the probability that it will be wrong at the time of the sale. High forecasts result in marked-down prices, and low forecasts produce opportunity costs (Stalk and Hout, 1990).

As time is compressed, market share increases. Many successful companies find themselves unable to grow in their historical markets using such traditional approaches as price cuts. These companies, however, can grow by improving the response time to their traditional markets (Stalk and Hout, 1990). Stalk and Hout (1990) assert that by reducing time consumption in every aspect of business, companies also reduce costs, improve quality, and stay close to their customers. In other words, time reduction throughout the
organization results in the realization of competitive advantages as well as the benefits of relationship marketing.

The success of Japanese car manufacturing in the 1970s has been attributed to the use of just-in-time (JIT) inventory management systems. The objective of JIT systems is to procure, transport, and produce the required items in very small quantities just in time for their consumption. The system was first developed by Toyota in an effort to react to customer demands with minimum delays (Schonberger, 1982).

Just-in-time, according to Blackburn (1991), is the genesis of time compression. It is a source of flexibility and speed. Using JIT as a tool merely to shorten manufacturing cycles is an underutilization of its full power. Blackburn (1991) asserts that JIT concepts are the keys to the time-compression process. Firms should develop JIT capabilities in non-manufacturing functions throughout the entire value delivery system (Blackburn, 1991).

There are different aspects of time-based competition, including fast-to-product and fast-to-market. Fast-to-product firms emphasize speed in terms of responding to customer demands for existing products (Dumaine, 1989). Fast-to-market firms enjoy first entrant advantages which include higher pricing, higher market share, improved customer service, and productivity improvement (Park, 1994).

An important aspect of time-based competition is identifying the areas in which time can be reduced (Patrick and Nigel, 1993). Patrick and Nigel (1993) identified five cycle-time loops where time can be managed to obtain higher performance. These five central cycle-time loops are the make/ship loop, the distribution loop, the supply loop, the new product introduction loop, and the strategic business development loop.

Additionally, the literature suggests that strategic focus on time enables firms to obtain sustainable competitive advantages (e.g., Blackburn, 1991). This assertion has been based on conceptual rather than empirical research. Most of the research to date has relied heavily on anecdotal evidence (Blackburn, 1991). Little research is based on empirical studies. For example, Valentino and Christ (1990), using a case study, explained that, through the cooperative approach, a time-based firm’s consumer division achieved 50 percent speed-up in development time, lower development costs, and dramatic improvements in product quality.

In the early 1980s, leading Japanese and some small North American and European companies demonstrated the power of two new dimensions of competitive advantage: low-cost variety and fast response time. These newly developed capabilities not only reduce costs, but they also enable firms to offer a broad product line, to cover more market segments, and to rapidly increase the technological sophistication of their products (Stalk and Hout, 1990).

Time has emerged as an effective tool in achieving lower costs and higher quality. It is a powerful concept because making a process faster and more responsive also reduces
costs, improves quality, and lowers inventory holding costs (Blackburn, 1991). Blackburn (1991) added that time compression also supports the currently popular admonition of getting closer to the customer. Demanding executives of aggressive companies are altering their measures of performance from competitive costs and quality to competitive costs, quality, and responsiveness (Stalk and Hout, 1990). Time compression allows firms to reduce costs, improve quality, increase productivity, offer variety, reduce innovation cycle times, and enhance responsiveness.

The value delivery system is the system that underlies the operations of every company. Each business operation is different, but all share one powerful common trait: all are systems for providing value to customers i.e. the value delivery systems. These systems facilitate the development of products, the delivery of products, and the making of decisions. Therefore, value delivery systems organize work and guide actions. Time, however, connects all of the parts of the value delivery system (Stalk and Hout, 1990).

Stalk and Hout (1990) attribute firm performance to the quality of their systems. According to Stalk and Hout (1990), firm performance is the direct result of how effectively the system is structured and managed. Better designed and better managed systems enable firms to operate more efficiently and responsively than their competitors. Thus, the quality of their systems is the basis for their sustainable competitive advantage, as are their technologies, products, or services.

To respond to customers’ needs is what motivates time-based corporate strategy. However, the key to becoming a time-based competitor lies within an organization. What matters to the customer is the total time required to deliver a product or service. Thus, time must be compressed in every function that affects the delivery of the product or service to the customer (Blackburn, 1991).

Many firms have reduced the time in their manufacturing processes. The just-in-time of the 1980s was successful. Manufacturing is just one link in the value delivery chain. Customers want instant gratification. Time must be reduced throughout the entire delivery process, otherwise customers will be unimpressed (Blackburn, 1991).

Time delays can appear anywhere in the value delivery system. Many U.S. firms have compressed time in one function, but few firms have successfully eliminated wasted time in all functions. The evidence strongly suggests that firms can find wide-open windows of opportunity for removing wasted time in every function (Blackburn, 1991).

The majority of time is typically consumed beyond the factory, by decision makers and information processors. At most factories consume less than 40 percent of the delivery time, and, in many cases, factories consume even less than 10 percent of the total delivery time (Stalk and Hout, 1990).

This observation reflects the importance of compressing time in functions other than manufacturing. Although manufacturing adds the most value, it consumes the least amount of time in the delivery cycle. Ultimately, in both manufacturing and service
firms, the entire value delivery system must be made flexible in order to consume the least amount of time. A responsive value delivery system must have flexible sales, order entry, procurement, and distribution systems as well as flexible factories (Stalk and Hout, 1990).

Given the issues raised in the literature relating to time-based manufacturing competence the following research question is offered for testing in relation to firms in the steel minimill industry in the United States of America:

RQ: To what extent does time-based manufacturing competence have a positive effect on overall business performance for firms in the steel mini mill industry in the United States of America?

Research Design

This study was based on an empirical investigation of manufacturing firms in the steel mini mill industry in the United States of America. The sample of firms was a census sample of firms in the steel mini mill industry and was provided by the U.S. Association of Iron and Steel Engineers. In order to obtain valid and reliable measures of the variables, previously validated scales were used to measure all variables (Kim and Arnold, 1992). All items were measured via seven-point bipolar scales (Kidder and Judd, 1986). The questionnaire was developed and pre-tested using a small sample of firms with the final instrument mailed to a census sample that included 137 firms who were ápriori identified as being involved in manufacturing in the steel mini mill industry, yielding 71 useable questionnaires being returned accounting for an effective response rate of 52 percent and considered to be adequate. This response rate is better than normal for most mail surveys (Groves, 1990; McDougall et al., 1994).

The instrument contained items identified by the literature intended to measure time-based manufacturing competency and performance. The instrument was designed to collect data about time-based competitive priorities and firm performance measures. The questionnaire was based on the 1994 Manufacturing Futures Survey conducted by Boston University’s Manufacturing Roundtable. An authorization was obtained from Boston University to use the section dealing with competitive priorities (see Kim and Arnold, 1992).

Based on the respondents’ perceptions, the respondents identified the degree of importance and the degree of strength of several time-based competitive priorities and manufacturing capabilities. In addition, the sample members’ provided their perceptions of their firms’ overall business performance (see Kidder and Judd, 1986).

Data Analysis

Prior to analyzing the data a check for non-response bias was conducted and a description of the sample is provided. An ‘extrapolation procedure’ technique was used to assess
non-response bias. This assumes that the groupings of actual respondents by an identified criterion are similar to the ‘theoretical’ non-respondents (Armstrong and Overton, 1977). Frequencies and independent t-tests were used to determine whether significant differences existed between the sample and the target population based on years of operation. No significant difference was identified between the sample and the target population for this classification variable. Therefore, as there appears to be no significant difference between respondents and non-respondents then the sample can be considered sufficient to draw conclusions about time-based manufacturing competency and performance for firms in the steel mini mill industry in the United States of America.

The sample consisted of 71 responding firms of which more than 66 percent of the plants reported they had been in operation for less than fifty years (see Table 1). Table 1 shows that a significant number of plants, more than 33 percent, have been in operation for more than fifty years. Mini mill operation is relatively new compared to the ages of firms shown in table 1. Most mini mill steel plants had been in the steel industry long before they adopted the mini mill operations when they were introduced to the industry.

<table>
<thead>
<tr>
<th>Years of operation</th>
<th>Frequency</th>
<th>Percentage</th>
<th>Cumulative percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 5 years</td>
<td>6</td>
<td>8.5</td>
<td>8.5</td>
</tr>
<tr>
<td>6 years to 20 years</td>
<td>16</td>
<td>22.5</td>
<td>31.0</td>
</tr>
<tr>
<td>21 years to 50 years</td>
<td>25</td>
<td>35.2</td>
<td>66.2</td>
</tr>
<tr>
<td>More than 50 years</td>
<td>24</td>
<td>33.8</td>
<td>100.0</td>
</tr>
<tr>
<td>Total</td>
<td>71</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>

The steel mini mill plants produce a vast variety of product lines, which are generally referred to as long products. The structure of the companies that participated in this study were either single plant or multiplant firms. Steel industry operations were based mainly on integrated systems until the 1980s, when businesses became more aware of the strategic role of the time factor, and it was then that the steel industry adopted mini mill operations. The integrated steel industry in the United States has suffered a decline in growth and global competitiveness, but plants that incorporated the mini mill process in their operations have achieved a remarkable growth in a declining industry. The mini mill process has been limited to plants with small capacity. The capacity of mini mill operations is relatively small compared to that of the integrated system. Table 2 indicates that the level of capacity for more than 88 percent of the participant plants is less than one million tons per year. In fact, more than half of the participant plants have a capacity of fewer than 400,000 tons per year.
Table 2.--Responding Plants by Capacity

<table>
<thead>
<tr>
<th>Capacity category</th>
<th>Frequency</th>
<th>Percentage</th>
<th>Cumulative Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 400,000 tons/year</td>
<td>42</td>
<td>59.2</td>
<td>59.2</td>
</tr>
<tr>
<td>400,000 - 800,000 tons/year</td>
<td>17</td>
<td>23.9</td>
<td>83.1</td>
</tr>
<tr>
<td>800,000 - 1,000,000 tons/year</td>
<td>4</td>
<td>5.6</td>
<td>88.7</td>
</tr>
<tr>
<td>More than 1,000,000 tons/year</td>
<td>8</td>
<td>11.3</td>
<td>100.00</td>
</tr>
<tr>
<td>Total</td>
<td>71</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>

The surveyed plants produce a variety of product lines and serve different market segments. They serve regional, national, or international markets, and, in addition to their geographic market variations, some plants focus on certain segments of the industry. Their share of the market is relative to the market in which they compete (see Table 3). Because mini mill plants have small capacity, they serve small segments of the market. As reflected in table 3, approximately 36 percent of the responding plants have a market share of less than 10 percent.

Table 3.--Market Share

<table>
<thead>
<tr>
<th>Market share category</th>
<th>Frequency</th>
<th>Percentage</th>
<th>Cumulative percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1% to 10%</td>
<td>26</td>
<td>36.6</td>
<td>36.6</td>
</tr>
<tr>
<td>11% to 25%</td>
<td>18</td>
<td>25.4</td>
<td>62.0</td>
</tr>
<tr>
<td>26% to 50%</td>
<td>15</td>
<td>21.1</td>
<td>83.1</td>
</tr>
<tr>
<td>More than 50%</td>
<td>6</td>
<td>8.5</td>
<td>91.6</td>
</tr>
<tr>
<td>Not available</td>
<td>6</td>
<td>8.5</td>
<td>100</td>
</tr>
<tr>
<td>Total</td>
<td>71</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

Based on the analysis of the data reported by the respondents the results suggest that there are positive relationships between all variables presented in Table 4. All the relationships presented in Table 4 have similar significant statistical results.

The data were analyzed using the correlation coefficient (Pearson’s $r$). The correlations between all the variables are reported in Table 4 and all relationships are statistically significant.
Table 4.-Time-based and Performance Hypotheses

<table>
<thead>
<tr>
<th>Variables</th>
<th>r-value</th>
<th>p-value</th>
<th>t-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Time-based competitiveness and manufacturing performance.</td>
<td>.22</td>
<td>.035</td>
<td>1.860</td>
</tr>
<tr>
<td>Time-based competitiveness and business performance.</td>
<td>.28</td>
<td>.010</td>
<td>2.405</td>
</tr>
<tr>
<td>Time-based manufacturing capability and manufacturing performance.</td>
<td>.67</td>
<td>.000</td>
<td>7.442</td>
</tr>
<tr>
<td>Time-based manufacturing capability and business performance.</td>
<td>.57</td>
<td>.000</td>
<td>5.721</td>
</tr>
<tr>
<td>Manufacturing performance and business performance.</td>
<td>.63</td>
<td>.000</td>
<td>6.690</td>
</tr>
<tr>
<td>Time-based manufacturing competence and manufacturing performance.</td>
<td>.34</td>
<td>.002</td>
<td>3.069</td>
</tr>
<tr>
<td>Time-based manufacturing competence and business performance.</td>
<td>.31</td>
<td>.004</td>
<td>2.689</td>
</tr>
</tbody>
</table>

\( \alpha = .05, \ df = 70, \) one tailed t-critical = 1.667

**Discussion**

The findings from this study indicate a significant positive relationship between time-based manufacturing competence and business performance. The most salient notion in strategy research is that business strategy guides manufacturing strategy (Anderson, Cleveland, and Schroeder 1989). The positive relationship between time-based competitiveness and time-based manufacturing capability supports this notion. The degree of importance of competitive priorities has a positive relationship with the degree of the strength in the manufacturing capabilities. This supports the assertion that time is an important strategic factor. In light of this result, time must be emphasized at the business strategy level in order to guide other functions to adopt it as a functional strategic element.

The role of establishing the strategic orientation by business strategy is evident in the finding which reflects the positive relationship between time-based competitiveness and manufacturing performance. Business strategy guides all the functional areas through its
dominant orientation (Hofer and Schendel 1978). Business performance is the result of the collective effort from all functional areas including manufacturing. The significant positive relationship between time-based competitiveness, which represents the business strategy orientation, and business performance reflects the important role that business strategy plays in guiding functional areas toward common goal of high performance and competitive position.

The positive relationship between time-based manufacturing capability and business performance supports the positive relationship in the manufacturing strategy literature between manufacturing strategy and performance (Williams et al. 1995). This reflects the value of the manufacturing function as a competitive factor.

The positive relationship between manufacturing performance and business performance reflects the concept of a multi-competitive advantage. Focus on time as a strategic factor enables firms to obtain a multi-competitive advantage. Firms will be able to provide customers with high-quality products at low cost and in a timely manner (Blackburn, 1991; Stalk and Hout, 1990). Manufacturing performance is represented by the factors that constitute the multi-competitive advantage, namely, cost, quality, cycle time, and flexibility. The positive relationship between manufacturing performance and business performance may lend the time element a significant role in creating a multi-competitive advantage.

One of the assumptions of this study is that time-based manufacturing competence is the force behind creating a multi-competitive advantage. Time-based manufacturing competence enables firms to offer high-quality products at low cost and in a timely manner. This reflects the value of the positive relationship between time-based manufacturing competence and business performance. The positive relationship between time-based manufacturing competence and manufacturing performance reflects the notion that time enables firms to lower costs, improve quality, and deliver products in a timely manner.

The positive relationship between manufacturing performance and business performance reflects the relationship between time-based manufacturing competence, multi-competitive advantage, and business performance. Manufacturing performance that consists of four competitive advantages (cost, quality, short cycle, and flexibility) has a positive relationship with time-based constructs and at the same time has a positive relationship with business performance. This leads to the conclusion that time-based manufacturing competence enables firms to have a multi-competitive advantage, which enables firms to achieve a high level of manufacturing performance and, in turn, a high level of business performance. This explains the observation that attention is shifting to time-based competition (Carter, Melnyk, and Handfield 1995)

References


The Regionalization of Global Brands: Emerging Market Perspectives

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Abstract: This paper reports the findings of multi-country study which compared the relationship between country of origin and brand trust in several emerging market economies (Nepal, Poland and Bulgaria) and one fully-developed economy (the United States). The study measured the importance of buying a global brand in 23 different product categories and asked respondents to evaluate brand trust and country-of-origin across all categories. The product categories of interest ranged from high involvement, durable goods (refrigerators, washing machines) to low involvement, fast moving consumer goods (chocolate bars, yogurt, disposable batteries). Analysis of country-of-origin effects yielded the research’s most interesting finding: Global brands might have a regional, or meso level, component which consumer brand trust has uncovered for the first time.

Keywords: Country of origin effects, brand trust, regionalization, globalization, global brands

In his well-known and oft-quoted article, “The Globalization of Markets,” Theodore Levitt (1983) outlined the basic logic for a global brand: that as global markets converged, due to the unrelenting forces of globalization, consumers will want “standardized consumer products on a previously unimagined scale of magnitudes” (p. 20). Firms that developed global products would then benefit from significant economies of scale since “everywhere everything gets more and more like everything else as the world’s preference structure is relentlessly homogenized” (Levitt, 1983, p.24). Levitt’s article prompted an immediate response (Boddewyn, Soehl & Picard, 1986) and still continues to prompt research and discussion on the degree to which market, product and advertising strategies can be (or should be) globally standardized (Viswanathan & Dickson, 2007).

Levitt (1983), however, did get one thing right: Markets have globalized. One aspect of globalization has been to reduce the barrier of geographic distance for marketing purposes. This is “the death of distance” (Cairncross, 1995, p. 5) that is always associated with globalization. Products as well as brands can now “travel the world” in search of new markets and new consumers. This search for market opportunity coincides with changes in the level and pace of economic development in countries outside of the United States, Canada, Australia, New Zealand, Japan and Western Europe – so-called “emerging markets.” Emerging markets are increasingly attractive to companies based in...
fully-developed economies because of their substantial, latent consumer demand for branded, quality products (Xie & Boggs, 2006). Further, there is some evidence that some market segments are becoming increasingly homogenous at a global level. Stock and Tupot (2006) provided evidence for a “global youth” segment and Lascu (2008) posited a “global elite” segment as well. Underpinning both the global youth and the global elite segments are consistent preferences for a set of global brands (i.e., a brand that is marketed and positioned everywhere the same). An important issue thus becomes: In an era of globalization, just how global are global brands?

The research reported here extends the discussion about global brands by analyzing the relationship between country-of-origin (COO) and brand trust. While COO is a well-researched global marketing topic, the relationship of COO to brand trust is not. Further, this research adds consumer perception data from two areas underreported in the branding literature, Nepal and Eastern Europe, to data from primarily United States consumers. Lastly, the research takes a multiple category approach toward exploring the importance of global brands. We asked respondents to evaluate the importance of both COO and brand trust across 23 different product categories.

Global Brands

Many researchers use the term “global brand” without defining it (Kapferer, 2005: Holt, Quelch & Taylor, 2004; Nebenzahl & Jaffe, 1996; Pharr, 2005; Quelch, 1999; Tse & Gorn, 1993; van Gelder). “The stickiest problem...seems to be the difficulty of defining what is ‘global’ and what is not” (Johansson & Ronkainen, 2005, p. 340). Two definitional perspectives are found in the literature. One set of definitions takes a producer perspective, while the other takes a consumer perspective. Cateora and Graham’s (2007) definition clearly embodies the producer perspective. A global brand is “the worldwide use of name, term, sign, symbol (visual and/or auditory), design or combination therefore intended to identify goods or services of one seller and to differentiate them from those of competitors” (p. 360). For Cateora and Graham, a global brand is a product or service with uniform characteristics (name, sign, and symbol) sold in multiple countries.

Barron and Hollingshead’s (2004) definition likewise takes the producer’s perspective, since its focus is on the tasks that sellers must do to communicate a global brand position. For them, a global brand is one that “expresses the same values in all of its markets and owns a similar position vis-à-vis its competitors around the world” (Barron & Hollingshead, 2004, p. 9). By defining a global brand in terms of values and positioning, Barron and Hollingshead extend the global brand definition into elements of a consistent marketplace position, wherever in the world the product is sold. This universal platform gives the global brand several advantages including increased leverage with channel partners, economies of scale and increased revenue.

Steenkamp, Batra and Alden (2003), in contrast, take a decidedly consumer-focused perspective when defining a global brand. A global brand for them is any brand that consumers perceive to be global. “A brand benefits from consumer perceptions that it is
‘global’…only if consumers believe the brand is marketed in multiple countries and is generally recognized as global in these countries” (p. 54). They term this perspective “perceived brand globalness.” Johansson and Ronkainen (2005) integrate both producer and consumer perspectives into their definition. A global brand is defined as “the multi-market reach of products that are perceived as the same by both consumers and internal constituents” (p. 340). Our approach, outlined below, follows Steenkamp, Batra and Alden’s (2003) perceived brand globalness. If a survey respondent thought a brand was global, then it was.

Global brand benefits can be divided into benefits to the producer and benefits to the consumer. For the firm, a global brand provides economies of scale (as Levitt proposed); opportunities to establish a worldwide identity (Hsieh, 2002); a cost-efficient platform for global line and brand extensions; a consistent positioning strategy; promotion synergies; global organizational learning opportunities and human capital benefits that are gained through recruitment and retention of talented individuals committed to global branding activities (Quelch, 1999). For consumers, a global brand provides higher perceived quality, greater prestige, higher status, and reflects greater esteem (Johansson & Ronkainen, 2005) than local/domestic brands. Holt, Quelch and Taylor (2004) found that global brands, in addition to being quality signals, were symbols of cultural ideals were representatives of socially responsible actions and often embodied American values.

**Country-of-Origin**

Country of origin (COO) is a well-researched global marketing topic. In mid-1997, Heslop, Papadopoulos and Bourke (1998) estimated that there were over 300 COO-related studies. By the time Pharr (2005) conducted her extensive literature review, the COO literature had increased to well over 700 studies. Hsieh (2004) suggested that COO “definitions can be classified into three groups: overall country image, aggregate product–country image, and specific product–country image” (p. 269).

In Hsieh’s (2004) framework, “overall country image” relates to the stereotypes and generalized attitudes individuals have about a specific country. Russia’s overall country image, for example, might be thought of as a Communist, repressive, poor, backward, monotone country. In contrast, “aggregate product-country image” and “specific product-country image” refer to the COO attitudes individuals hold at the level of product category and individual brand level, respectively. Aggregate product-country image is tapped when individuals evaluate “the made in” label, such as computers made in Malaysia. Specific product-country image is evoked when consumers evaluate a brand, such as a Porsche Cayenne made in Slovakia. More recently, Pappu, Quester and Cooksey (2006) simplified Hsieh’s framework into just macro and micro country image.

Pharr (2005) noted that over the years, COO research has been refined into a nuanced concept that now includes Hofstede’s work on culture, brand image, brand name, consumer levels of involvement, country stereotypes, quality/price relationships, and differentiation (if possible) between country-of-assembly, country-of-parts and country-of design. COO has also been studied in developed as well as in developing countries.
(Bilkey & Nes, 1982; Lee, Yun & Lee, 2005; Speece & Nguyen, 2005). Additionally, scholars have variously tried to understand how COO effects perceived product value (Cervino, Sanchez & Cubillo, 2005; Hui & Zhou, 2002); brand image and brand equity (Lin & Kao, 2004; Pappu, Quester & Cooksey, 2007).

Consumer ethnocentrism can act as a mediating variable in any COO evaluation. Following the definition first used by Shimp and Sharma (1987), consumer ethnocentrism is the belief held by consumers about “the appropriateness, indeed morality, of purchasing foreign products” (p. 280). Consumer ethnocentrism is a systematic preference favoring purchase of domestic over foreign products. Consumer ethnocentrism is more contemporaneously termed “domestic country bias” (Balabanis and Diamantopoulos, 2004, p. 80). Empirical research has identified differences in domestic country bias between consumers living in developed versus developing countries (Batra et al., 2000; Upadhyay & Singh, 2006). The former clearly favored domestic over foreign products, while the latter favored the opposite. Research by Bawa (2004) indicated that contrary to earlier findings that consumers from developing countries were biased toward imported over domestic products, “the label ’made in India’ is not a liability. The Indian consumers will not lap up foreign goods merely because of their ‘made in’ tags” (p.43).

Phar (2005) developed a holistic, country of origin model that integrated most of the antecedent, moderating and outcome variables outlined above. Whatever the research focus, though, COO is inevitably linked with trying to understand how COO mediates product evaluation and consumer purchase intention (Pharr, 2005; Usunier & Cestre, 2007).

Recently, another stream of research has explored the accuracy of consumer COO attribution. Samiee et al. (2005) found that (a) consumers varied in their accurate recognition of a brand’s true country of origin, and (b) respondents inferred country of origin by associating the brand name with a language thought to be representative of a specific country. They postulated a new construct called “brand origin recognition accuracy.” AndersonAnalytics (2007) extended Samiee et al’s findings. Their research used a representative sample of 1,000 college and university students enrolled in 375 different United States institutions and found that students often inaccurately identified the COO for well-known brands. For example, 53% of the sample thought Nokia to be a Japanese company rather than a Finnish one, and 48.5% of respondents identified Adidas’ COO as the United States as opposed to Germany (Weiss, 2007).

COO remains a complex construct. It is not possible to choose one set of variables over another to develop a uniform perspective. Research that has begun to explore consumer accuracy in their COO perceptions may well be a key pivot point. For the marketing pragmatist, a consumer perception of where a product or service is thought to be from is what matters. Strategy evolves from that data point.
Brand Trust

Trust is an elusive concept (Elliot & Percy, 2007) and can be thought of as an individual characteristic, as a characteristic of interpersonal relations and/or as an institutional attribute (Lewicki & Bunker, 1995). Trust is also a nuanced concept that has familiarity as its precondition (Luhmann, 1979). There are multiple definitions of trust. Rotter (1971) defined trust as “a generalized expectancy held by an individual or group that a word, promise, verbal or written statement of another individual or group can be relied on” (p.1). Barney and Hansen (1994) add the idea of hurt and harm when they defined trust as “The mutual confidence that no party to an exchange will exploit another’s vulnerabilities” (p. 176). Finally, Battaharrya, Devinney & Pilluta (1998) highlight the protective nature of trust when they defined trust as “an expectancy of positive (or nonnegative) outcomes that one can receive based on the expected action of another party in an interaction characterized by uncertainty” (p. 462). Trust thus involves commitment, risk and mutuality. Trust is also a dynamic concept that is always contingent. “The amount of knowledge necessary for trust is somewhere between total knowledge and total ignorance. Given total knowledge there is no need for trust and given total ignorance there is no basis upon which to rationally trust” (McAllister, 1995, p.26).

Relationship marketing has encouraged further the transfer and application of trust to brands (Romaniuk & Bogomolova, 2005; Fournier, 1988). This led Delgado-Ballester, Munera-Alemain and Yague-Gullien (2003) to define brand trust as “The confident expectations of the brand’s reliability and intentions in situations entailing risk to the consumer” (p. 37). Brand trust has also been defined as “the confidence a consumer develops in the brand’s reliability and integrity” (Chatterjee & Chaudhuri, 2005, p.2). Brand trust has been linked with brand loyalty (Lau & Lee, 1999) as well as increased market share and advertising efficiency (Chatterjee & Chaudhuri, 2005). Brand trust has also been hypothesized to be leading indicator of brand equity (Ambler, 1997).

Of recent interest has been the question of whether brands vary in terms of trust. Romaniuk and Bogomolova (2005) studied this question by controlling for brand size effects when they assessed trust scores of 110 local brands in 13 markets in subjects living in the United Kingdom and Australia. They found little variation in brand trust scores when controlling for market share. They concluded that “trust is more like a ‘hygiene’ factor in that all brands have to have a certain level of trust to be competitive in the market” (Romaniuk & Bogomolova, 2005, p. 371). If brands do not vary greatly in terms of trust, would the same hold true when consumers were asked to evaluate specifically their trust in a global brand?

The goal of this paper is to examine the notions of global brands, “perceived brand globalness,” country-of-origin, consumer ethnocentrism, and brand trust to determine how the interactions of these factors will might affect global marketing strategy.
Methodology

Young adult consumers in three emerging market countries and one fully-developed economy were specifically targeted for this research: Nepal, Bulgaria and Poland were the emerging market countries and the United States was the fully-developed economy. Nepal, Bulgaria and Poland were selected primarily because young adult consumers from these three countries were underrepresented in the marketing literature. Young adult consumers from the United States were selected so that more extensive generalizations about the strength and scope of global brands could be made. Given the global awareness of young adult consumers, we did not want to make any a priori assumptions about brand preferences even for U.S. young adults.

Access to respondents was through educational institutions in all countries. In Nepal and the United States, several educational institutions were used to avoid sampling bias. Only one educational institution was used in both Bulgaria and Poland, which we recognize as a research design limitation. Young adults attending these educational institutions were asked by their teachers to participate in the research.

The survey we developed had three parts. Part one asked respondents to evaluate the importance of buying a global brand in each of 23 different consumer categories. Our approach mirrored that of Steenkamp, Batra and Alden (2003) in the use of perceived brand globalness.

Table 1. Product Categories Explored

<table>
<thead>
<tr>
<th>A bank checking account</th>
<th>VHS player</th>
<th>Clothes dryer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shampoo</td>
<td>Refrigerator</td>
<td>Personal credit card</td>
</tr>
<tr>
<td>Disposable batteries</td>
<td>Soft drink</td>
<td>Mobile phone</td>
</tr>
<tr>
<td>Hamburger - Fast Food</td>
<td>Rice cooker</td>
<td>Coffee</td>
</tr>
<tr>
<td>Home computer</td>
<td>Toothpaste</td>
<td>Bottled drinking water</td>
</tr>
<tr>
<td>DVD player</td>
<td>Washing machine</td>
<td>Jeans n</td>
</tr>
<tr>
<td>Running shoes</td>
<td>TV</td>
<td>Motorcycle</td>
</tr>
<tr>
<td>Chocolate candy bar</td>
<td>Yogurt</td>
<td></td>
</tr>
</tbody>
</table>

As noted above, there is no agreed upon, unitary meaning for what constitutes a global brand, other than the fact that the brand must be sold outside its domestic market. We wanted to avoid the artificiality of some academic definitions and to let consumer perceptions emerge as to what constituted a global brand for them. We thus told respondents that “a global brand is one that you think is found or sold in several countries around the world.” A seven-point Likert scale (anchored with “very unimportant” and “very important”) was used to capture level of importance. We developed the product categories to span a range of dimensions: (1) high and low involvement product categories (computers versus candy bars); (2) durable versus nondurable products (washing machines and coffee); and (3) categories not often reported in the marketing literature (e.g., rice cookers, disposable batteries, motorcycles and clothes dryers). Table 1 lists all 23 product categories.
Part two of the survey asked respondents to evaluate country of origin and brand trust. This was a forced choice question. For each of the 23 product categories listed in Table 1, respondents were asked to choose the one country that their most trusted brand(s) came from. We limited country choice to China, France, Germany, Great Britain, India, Japan, South Korea and the United States because we knew that at least one global brand in each category in Table 1 came from at least one of the listed countries. Respondents could note if the brand(s) they trusted most came from a country not listed.

Part three of the survey collected basic demographic information: age, gender, home country, employment status, highest education level and whether the respondent was living outside their home country when taking the survey. The entire survey was written in English.

We pre-tested the online survey by having colleagues review and critique it. Based on their feedback, we revised the survey by deleting some of the original product categories and adding others. Additionally, colleagues confirmed that all product categories had a single meaning. We posted the survey on SurveyMonkey.com, an online survey website, for ease of data collection. Online data collection did not present any problems to these Internet-savvy young adults. The survey’s first page assured all respondents that their answers would be kept confidential and that the identity of every respondent would remain anonymous. Data were collected from 2006-2007.

**Results**

A total of 215 individuals, residing in over a dozen different countries, took the survey. Ninety percent of the respondents came from five countries: United States (42.3%), Nepal (27.9%), Bulgaria (9.3%), India (7.9%) and Poland (3.3%). Although not specifically targeted, Indian nationals participated in the survey because of their admission to schools in both Nepal and the United States. The mix of men to women taking the survey was almost evenly split, with men representing 49.1% of total sample and women representing the remaining 50.9%. Forty-five percent of the sample reported having some college, while almost 38% of respondents had completed college. A much smaller percentage of respondents had completed a master’s degree (16.4%), and a negligible percentage had completed a doctorate (0.9%). Respondents’ age was skewed toward younger respondents with 47.5% of total respondents being between 19-23 years old. Mean age for all respondents was 26.2 year, with the modal age of respondents being 21 (16.4% of all respondents).

**Global brand importance.** Table 2 presents mean scores for all 23 product categories in rank order. The first ten products in Table 2 (mobile phones through running shoes), indicate that these products are all high risk, are all high involvement and, except for a checking account and running shoes, are all technological -- in the broad sense of the word. A credit card is technological because it embodies the technology part of banking and purchasing. The high risk, high involvement nature of these ten products places increased consumer emphasis on product quality, reliability and dependability. In each case, the consequence of product failure can be significant. We consider a checking account to be high risk because errors in reporting or the inability to access accounts on-
demand can result in serious negative consequence for the consumer (e.g., overdrawn accounts, reduced credit scores, account surcharges, etc.).

**Table 2. Importance of Buying a Global Brand: Ranked Order of Importance**

<table>
<thead>
<tr>
<th>Product</th>
<th>Mean</th>
<th>n</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mobile Phone</td>
<td>5.98</td>
<td>202</td>
</tr>
<tr>
<td>Home Computer</td>
<td>5.78</td>
<td>199</td>
</tr>
<tr>
<td>TV</td>
<td>5.76</td>
<td>205</td>
</tr>
<tr>
<td>Credit Card</td>
<td>5.56</td>
<td>184</td>
</tr>
<tr>
<td>Refrigerator</td>
<td>5.37</td>
<td>188</td>
</tr>
<tr>
<td>Checking Account</td>
<td>5.26</td>
<td>193</td>
</tr>
<tr>
<td>DVD</td>
<td>5.11</td>
<td>193</td>
</tr>
<tr>
<td>Washing Machine</td>
<td>5.00</td>
<td>183</td>
</tr>
<tr>
<td>Running Shoes</td>
<td>4.91</td>
<td>199</td>
</tr>
<tr>
<td>Motorcycle</td>
<td>4.92</td>
<td>144</td>
</tr>
<tr>
<td>Shampoo</td>
<td>4.78</td>
<td>202</td>
</tr>
<tr>
<td>Jeans</td>
<td>4.75</td>
<td>197</td>
</tr>
<tr>
<td>Clothes Dryer</td>
<td>4.56</td>
<td>158</td>
</tr>
<tr>
<td>Coffee</td>
<td>4.52</td>
<td>180</td>
</tr>
<tr>
<td>Toothpaste</td>
<td>4.50</td>
<td>204</td>
</tr>
<tr>
<td>Soft Drinks</td>
<td>4.40</td>
<td>196</td>
</tr>
<tr>
<td>Bottled Water</td>
<td>4.39</td>
<td>198</td>
</tr>
<tr>
<td>Rice Cooker</td>
<td>4.37</td>
<td>157</td>
</tr>
<tr>
<td>VHS</td>
<td>3.96</td>
<td>146</td>
</tr>
<tr>
<td>Hamburger-Fast Food</td>
<td>3.90</td>
<td>182</td>
</tr>
<tr>
<td>Chocolate</td>
<td>3.90</td>
<td>186</td>
</tr>
<tr>
<td>Yogurt</td>
<td>3.85</td>
<td>188</td>
</tr>
<tr>
<td>Disposable Batteries</td>
<td>3.78</td>
<td>189</td>
</tr>
</tbody>
</table>

*Note.* Rated on a seven point scale with 1=very unimportant and 7=very important.

We also note the preponderance of durable goods (TVs, washing machines, refrigerators, home computers) in the list of products for which buying a global brand was most important. As noted above, 58% of our sample resided outside the United States and all these respondents were from countries with emerging or transitional economies. We hypothesize that in these countries, a durable good’s purchase is a risky purchase since it accounts for a larger percentage of total household or total personal budgets than in fully developed economies. Adding to the risk level of these products is the lack of enforceable warranties and guarantees in many of the respondents’ home countries (e.g., India, Nepal, Bulgaria). Buying global brands serves to reassure buyers due to the brand’s perceived dependability and reliability, in other words, they trust a global brand.

Table 2 also suggests that purchase of a global brand is not very important for low involvement products, such as fast food hamburgers, chocolate candy bars, yogurt and disposable batteries. We suggest, then, a relationship between risk and the importance of
buying a global brand. The greater the perceived risk, the more important it is to buy a
global brand – and vice versa. A statement often made about a global brand is that it is a
surrogate for quality (Keller, 2008). The rankings in Table 2 confirm this.

Clearly, all product categories are not equal relative to the importance of purchasing a
global brand. Table 3 presents statistically significant gender differences for the
importance of purchasing a global brand. Buying a global brand is much more important
for women than men when purchasing a computer, toothpaste, bottled water, a washing
machine, yogurt, shampoo, a fast food hamburger, a rice cooker and coffee. Gender roles
and patriarchy in countries like India and Nepal can help explain why women more then
men would prefer purchasing a globally branded washing machine and rice cooker. In
these two product categories, women will have

<table>
<thead>
<tr>
<th>Product</th>
<th>Male (means)</th>
<th>Female (means)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Computer</td>
<td>5.54</td>
<td>6.03</td>
</tr>
<tr>
<td>Washing Machine</td>
<td>4.72</td>
<td>5.34</td>
</tr>
<tr>
<td>Shampoo</td>
<td>4.32</td>
<td>5.25</td>
</tr>
<tr>
<td>Rice Cooker</td>
<td>3.71</td>
<td>5.05</td>
</tr>
<tr>
<td>Coffee</td>
<td>4.14</td>
<td>4.89</td>
</tr>
<tr>
<td>Bottled Water</td>
<td>3.91</td>
<td>4.88</td>
</tr>
<tr>
<td>Toothpaste</td>
<td>4.17</td>
<td>4.87</td>
</tr>
<tr>
<td>Hamburger-Fast Food</td>
<td>3.52</td>
<td>4.28</td>
</tr>
<tr>
<td>Yogurt</td>
<td>3.47</td>
<td>4.22</td>
</tr>
</tbody>
</table>

Note. Rated on a seven point scale with 1=very unimportant and 7=very important. All
reported mean differences are significant at the .05 level or less.

more knowledge about both local and global brands then men. More traditional shopping
and family roles in countries outside the United States might likewise explain why
women more then men would prefer a global brand of coffee, bottled water, hamburgers
and yogurt. With personal grooming products, like shampoo and toothpaste, women may
be able to more clearly discern the differences between global and domestic brands than
men. Lastly, the importance of buying a computer that is a global brand is again greater
for women than it is for men. We hypothesize that buying a global brand reduces the
functional, financial and psychological risks associated with computers.

**Trusted Countries and Product Category.** Table 4 summarizes part two of the survey,
which asked respondents to choose the one country that their most trusted brand(s) came
from. Table 4 lists the top three countries for brand trust for the 23 product categories.
Brands associated with the United States were most trusted (column 1) in 16 categories,
while brands from Japan were most trusted (column 1) in six categories. These results,
we believe, can be explained not only by the large proportion of respondents from the
United States but also by the intense and highly visible brand campaigns developed for
American consumers.
Table 4. Product Categories And Country Most Trusted

<table>
<thead>
<tr>
<th>Product Category</th>
<th>Most Trusted</th>
<th>2\textsuperscript{nd} Most Trusted</th>
<th>3\textsuperscript{rd} Most Trusted</th>
</tr>
</thead>
<tbody>
<tr>
<td>Computer (n = 200)</td>
<td>US (37.3%)</td>
<td>Japan (38.7%)</td>
<td>Other Country (4.3%)</td>
</tr>
<tr>
<td>Toothpaste (n = 172)</td>
<td>US (58.7%)</td>
<td>India (23.8%)</td>
<td>Other Country (8.7%)</td>
</tr>
<tr>
<td>Bottled Water (n = 176)</td>
<td>US (53.4%)</td>
<td>Other Country (26.7%)</td>
<td>India (7.4%)</td>
</tr>
<tr>
<td>DVD Player (n = 182)</td>
<td>Japan (67%)</td>
<td>China (10.4%)</td>
<td>US (9.9%)</td>
</tr>
<tr>
<td>Washing Machine (n = 167)</td>
<td>US (35.9%)</td>
<td>Japan (35.3%)</td>
<td>Germany (9.6%)</td>
</tr>
<tr>
<td>Jeans (n = 174)</td>
<td>US (60.9%)</td>
<td>Other Country (13.2%)</td>
<td>China (7.5%)</td>
</tr>
<tr>
<td>Running Shoes (n = 177)</td>
<td>US (54.8%)</td>
<td>China (12.4%)</td>
<td>Other Country (9.6%)</td>
</tr>
<tr>
<td>TV (n = 186)</td>
<td>Japan (65.6%)</td>
<td>US (15.1%)</td>
<td>China (7.0%)</td>
</tr>
<tr>
<td>Motorcycle (n = 131)</td>
<td>Japan (43.5%)</td>
<td>India (19.1%)</td>
<td>US (18.3%)</td>
</tr>
<tr>
<td>Chocolate Bar (n = 167)</td>
<td>US (46.1%)</td>
<td>Germany (10.6%)</td>
<td>Other Country (10.6%)</td>
</tr>
<tr>
<td>Yogurt (n = 152)</td>
<td>US (48.7%)</td>
<td>Other Country (28.9%)</td>
<td>India (11.2%)</td>
</tr>
<tr>
<td>Checking Account (n = 172)</td>
<td>US (73.8%)</td>
<td>Other Country (11.6%)</td>
<td>India (6.4%)</td>
</tr>
<tr>
<td>VHS Player (n = 139)</td>
<td>Japan (56.1%)</td>
<td>US (16.5%)</td>
<td>China (13.7%)</td>
</tr>
<tr>
<td>Clothes Dryer (n = 141)</td>
<td>US (44.0%)</td>
<td>Japan (17.7%)</td>
<td>China (9.9%)</td>
</tr>
<tr>
<td>Shampoo (n = 172)</td>
<td>US (56.4%)</td>
<td>India (14.5%)</td>
<td>France (8.7%)</td>
</tr>
<tr>
<td>Refrigerator (n = 170)</td>
<td>US (43.5%)</td>
<td>Japan (27.6%)</td>
<td>India (6.5%)</td>
</tr>
<tr>
<td>Credit Card (n = 167)</td>
<td>US (78.4%)</td>
<td>Other Country (10.2%)</td>
<td>India (4.8%)</td>
</tr>
<tr>
<td>Disposable Batteries (n = 150)</td>
<td>US (39.3%)</td>
<td>Japan (28.0%)</td>
<td>India (8.7%)</td>
</tr>
<tr>
<td>Soft Drinks (n = 165)</td>
<td>US (70.3%)</td>
<td>India (12.7%)</td>
<td>Other Country (12.1%)</td>
</tr>
<tr>
<td>Cell Phone (n = 186)</td>
<td>Japan (38.2%)</td>
<td>US (27.4%)</td>
<td>Other Country (14.0%)</td>
</tr>
<tr>
<td>Hamburger (n = 166)</td>
<td>US (75.9%)</td>
<td>Other Country (11.4%)</td>
<td>India (4.8%)</td>
</tr>
<tr>
<td>Rice Cooker (n = 131)</td>
<td>Japan (41.2%)</td>
<td>US (20.6%)</td>
<td>China (11.5%)</td>
</tr>
<tr>
<td>Coffee (n = 150)</td>
<td>Other Country (34.7%)</td>
<td>US (32.0%)</td>
<td>India (16.7%)</td>
</tr>
</tbody>
</table>

To test further the validity of these associations and to remove the distortions caused by unequal numbers of respondents from different home countries, we ran chi-square tests for respondents' home country and the country associated with the most trusted brand.
Table 5. Most Trusted Region For Product Categories

<table>
<thead>
<tr>
<th>Product Category</th>
<th>Regions</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>US</td>
<td>Eastern Europe</td>
<td>South Asia</td>
</tr>
<tr>
<td>Toothpaste</td>
<td>More Likely To Trust US</td>
<td>More Likely To Trust Germany</td>
<td>More Likely Trust To India</td>
</tr>
<tr>
<td>Bottled Water</td>
<td>More Likely To Trust US</td>
<td>------------------</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>DVD Player</td>
<td>------------------</td>
<td>More Likely To Trust Germany and France</td>
<td>------------------</td>
</tr>
<tr>
<td>Washing Machine</td>
<td>More Likely To Trust US</td>
<td>More Likely To Trust Germany</td>
<td>More Likely To Trust Japan</td>
</tr>
<tr>
<td>Running Shoes</td>
<td>More Likely To Trust US</td>
<td>------------------</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>TV</td>
<td>More Likely To Trust US</td>
<td>More Likely To Trust Germany</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>Motorcycle</td>
<td>More Likely To Trust US</td>
<td>More Likely To Trust Germany</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>Chocolate Bars</td>
<td>More Likely To Trust US</td>
<td>More Likely To Trust France</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>Yogurt</td>
<td>More Likely To Trust US</td>
<td>More Likely To Trust Germany</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>Checking Account</td>
<td>More Likely To Trust US</td>
<td>------------------</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>VHS Player</td>
<td>------------------</td>
<td>More Likely To Trust Germany</td>
<td>More Likely Trust India</td>
</tr>
<tr>
<td>Clothes Dryer</td>
<td>More Likely To Trust US</td>
<td>More Likely To Trust Germany</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>Shampoo</td>
<td>More Likely To Trust US</td>
<td>More Likely To Trust France</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>Refrigerator</td>
<td>More Likely To Trust US</td>
<td>More Likely To Trust Germany</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>Credit card</td>
<td>More Likely To Trust US</td>
<td>------------------</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>Disposable Batteries</td>
<td>More Likely To Trust US</td>
<td>More Likely To Trust Germany</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>Soft Drinks</td>
<td>More Likely To Trust US</td>
<td>------------------</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>Mobile Phones</td>
<td>More Likely To Trust US</td>
<td>More Likely To Trust Germany</td>
<td>------------------</td>
</tr>
<tr>
<td>Hamburger</td>
<td>More Likely To Trust US</td>
<td>------------------</td>
<td>More Likely To Trust India</td>
</tr>
<tr>
<td>Coffee</td>
<td>More Likely To Trust US</td>
<td>------------------</td>
<td>More Likely To Trust India</td>
</tr>
</tbody>
</table>

Note. Eastern Europe consisted of Bulgaria, Serbia, and Poland while South Asia consisted of India and Nepal. Chi squares were significant at the .05 level or less.
We reduced the number of respondent home countries to wider geographic regions to increase the robustness of the test.

Table 5 provided some unexpected evidence concerning the notion of global brands and trust. It appears that respondents trusted brands which they perceived to have a country-of-origin where they lived (micro level) or in the region where they lived (meso level). Thus a favoured brand might be one that is trusted in some sense because of geography, thus making it feel more local or regional while still having a global brand flare. Almost all the product categories in Table 5 exhibit this characteristic. There were some minor exceptions such as Eastern Europeans trusting French chocolate bars, DVD players, and shampoo. The only exception for South Asia was that Japanese washing machines were trusted more than those from other countries in South Asia.

Table 6 provides a detailed look at brand trust by nationality/home country and the countries from which the most trusted brand names came. For the categories listed in the table, respondents were asked to provide specific “brand names you trust most.” Those brand names were then coded by country-of-origin and crossed by nationality/home country of the respondent.

Overall, the local/regional preferences presented in Table 5 are supported by Table 6. For U.S. respondents, the most trusted brand names for toothpaste, washing machines, running shoes, motorcycles, chocolate bars, checking accounts, clothes dryers, refrigerators, credit cards, disposable batteries, cell phones, and coffee continued to be U.S. brand names. Bulgarians (Eastern Europe) trusted German brand names of toothpaste, washing machines, refrigerators, and coffee. Indians (South Asia) trusted brand names from Indian in the categories of toothpaste, bottled water, washing machines, checking accounts, credit cards, and soft drinks.

There were some anomalies from the patterns mentioned above. For U.S. respondents, French bottled water and yogurt had trusted brand names. Nepalis trusted German brand names of running shoes, British chocolate bars and jeans, Japanese motorcycles, Korean brand named refrigerators, and Japanese and Korean brands of washing machines. This group was by far the most eclectic. Bulgarians moved from their German pattern by trusting British brand names of chocolate bars and Japanese brand names of disposable batteries.
Table 6. Results of Trusted Country Brand by Nationality

<table>
<thead>
<tr>
<th>Product Category</th>
<th>Nationality</th>
</tr>
</thead>
<tbody>
<tr>
<td>Toothpaste</td>
<td>Indians Were More Likely to Trust Indian Brands, Americans Were More Likely to Trust US Brands, Bulgarians Were More Likely to Trust German Brands</td>
</tr>
<tr>
<td>Bottled Water</td>
<td>Indians and Nepalis Were More Likely to Trust Indian Brands, Americans Were More Likely to Trust French and US Brands</td>
</tr>
<tr>
<td>Washing Machine</td>
<td>Indians Were More Likely to Trust Indian Brands, Nepalis Were More Likely to Trust Japanese and Korean Brands, Americans Were More Likely to Trust US Brands, Bulgarians Were More Likely to Trust German Brands</td>
</tr>
<tr>
<td>Jeans</td>
<td>Nepalis Were More Likely to Trust British Brands</td>
</tr>
<tr>
<td>Running Shoes</td>
<td>Nepalis Were More Likely to Trust German Brands, Poland Was More Likely to Trust German Brands, Americans Were More Likely to Trust US Brands</td>
</tr>
<tr>
<td>Motorcycle</td>
<td>Americans Were More Likely to Trust US Brands, Nepalis Were More Likely to Trust Japanese Brands, Bulgarians Were More Likely to Trust German Brands</td>
</tr>
<tr>
<td>Chocolate Bar</td>
<td>Indians Preferred British Brands, Americans Were More likely to Trust US Brands, Bulgarians Were More Likely to Trust British Brands, Nepalis Were More Likely to Trust British Brands</td>
</tr>
<tr>
<td>Yogurt</td>
<td>Nepalis Were More Likely to Trust Indian Brands, Americans Were More Likely to Trust French Brands</td>
</tr>
<tr>
<td>Checking Account</td>
<td>Indians Were More Likely to Trust Indian Brands, Americans Were More Likely to Trust US Brands</td>
</tr>
<tr>
<td>Clothes Dryer</td>
<td>Nepalis Were More Likely to Trust Indian Brands, Americans Were More Likely to Trust US Brands</td>
</tr>
<tr>
<td>Refrigerator</td>
<td>Nepalis Were More Likely to Trust Korean Brands, Americans Were More Likely to Trust US Brands, Bulgarians Were More Likely to Trust German Brands</td>
</tr>
<tr>
<td>Credit Card</td>
<td>Americans Were More Likely to Trust US Brands, Indians Were More Likely to Trust Indian Brands</td>
</tr>
<tr>
<td>Disposable Batteries</td>
<td>Americans Were More Likely to Trust US Brands, Bulgarians Were More Likely to Trust Japanese Brands</td>
</tr>
<tr>
<td>Soft Drink</td>
<td>Indians Were More Likely to Trust Indian Brands</td>
</tr>
<tr>
<td>Cell Phone</td>
<td>Americans Were More Likely to Trust US Brands</td>
</tr>
<tr>
<td>Coffee</td>
<td>Americans Were More Likely to Trust US Brands, Nepalis Were More Likely to Trust Indian Brands, Bulgarians Were More Likely to Trust German Brands</td>
</tr>
</tbody>
</table>

Note. Chi squares are significant at the .05 level or less.

Taken together, Tables 5 and 6 extend a main research finding about COO and consumer ethnocentrism into the brand trust arena: that “a universal domestic preference is a fallacy” (Heslop and Papadopoulos, 1993, p. 45). Table 6 indicates consumers have
brand trust preferences from many countries of origin but those preferences are generally tightly bound by region (Table 5). Our findings also support Etzel and Walker’s (1974) conclusion that COO effects are specific to product categories. Table 6 raises an interesting question about the brands Nepali consumers trust in that Nepali consumers often seem to prefer brands outside South Asia (See Table 7) This finding is intriguing, and we readily admit it needs further analysis.

A partial explanation of these findings is that Nepal is a small country, mired in poverty. Nepal’s current population is around 29 million (CIA Fact book), yet World Bank estimates are that 50.3% of Nepal’s population live on less than $1 a day (Asian Development Bank, 2000). Relatively small market size coupled with low consumer purchasing power limit the number of brands available in any given category. East Asian brands, specifically from Japan and Korea, have had a long-standing presence in the Nepali market. In some categories, they are market leaders. HeroHonda dominates the motorcycle market, for example, as do LG and Samsung the washing machine and refrigerator market. Why the trusted brand(s) for clothes dryers do not follow a similar out-of-region preference, since it too is a durable good and is marketed by both Samsung and LG in Nepal, is confounding.

### Table 7. Nepali Trusted Country Brands

<table>
<thead>
<tr>
<th>Product Category</th>
<th>Regional Preference (Brands within South Asia)</th>
<th>Out of Region Preference (Brands outside of South Asia)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bottled Water</td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Washing Machines</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Jeans</td>
<td>☑</td>
<td></td>
</tr>
<tr>
<td>Running shoes</td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Motorcycles</td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Chocolate bars</td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Yogurt</td>
<td>☑</td>
<td></td>
</tr>
<tr>
<td>Clothes dryer</td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Refrigerator</td>
<td></td>
<td>✓</td>
</tr>
<tr>
<td>Coffee</td>
<td>☑</td>
<td></td>
</tr>
</tbody>
</table>

### Discussion

Overall, our research into the importance of global brands and brand trust confirms that brands perceived as global function as quality surrogates for young adult consumers. Across a wide variety of categories, trust in a perceived-to-be global brand helped reduce the uncertainty and risk associated with high involvement products, many of which were durable goods.

The purchase of a perceived global brand may not be very important for low involvement products, such as fast food hamburgers, chocolate candy bars, yogurt and disposable batteries. Since many of these are food categories, our finding supports Ahmed et al.’s (2004) conclusion that “consumers’ purchase decisions are influenced more by the brand
than by the COO of a food product” (p. 114). We suggest, then, a relationship between risk and the importance of buying a global brand. The greater the perceived risk, the more important it is to buy a brand perceived as global and vice versa.

Brands associated with the United States were most trusted. 70% of the categories used in the research had the U.S. mentioned as the most trusted country while brands from Japan were mentioned in 26% of the categories. Our findings are consistent with latest Interbrand Best Global Brand Report of 2007 which had 70% of their top 20 global brands as U.S. These results may be explained by the intense and highly visible global IMC campaigns from U.S. marketers and their international partners.

County-of-origin did not operate as an independent factor. It co-varied with the notion of trust. When COO was combined with the notion of brand trust, it was clear that they were both dependent upon the geographical region of the respondent. A perceived global brand that was from the consumers’ home county or their region had a decided preference. The strong, regional preferences captured in Table 5 add something new to the literature about global branding and brand trust. Our findings suggest that both brand trust and country of origin may exist for consumers at a meso or regional level. Traditionally, researchers and practitioners have conceptualized the global brand at either a macro level (everywhere, everything about the brand is the same) and at a micro-level (glocalization or the need for local adaptation). Perhaps there is now a meso level emerging in which regionalization becomes an important brand characteristic.

If true, then our research mirrors a number of interesting developments in corporate strategic thinking. Ghemawat (2007), most recently, has directly challenged the issue of global standardization. His argument is that the world is not becoming increasingly globalized (i.e., more standardized), but is, in fact, becoming “semi-globalized.” Semi-globalization will last for a long time because powerful regional differences still serve as a significant barrier to firm’s developing one, over-arching, grand corporate strategy. For Ghemawat, regionalization is at the core of contemporary, strategic thinking. Regionalization is what our research suggests as well.

Further, our research provides empirical support for Kapferer’s (2005) descriptive conceptualization of “the post-global brand.” Kapferer observed what brand managers were actually doing in the global marketplace and reached the conclusion that “it is becoming more and more common for companies to develop products for specific geographic regions….Furthermore, it is at [the] regional level that the world’s markets…are at their most permeable” (p. 321). Thus a global brand is much more complicated than simply the consistent use of the name, logo, trade dress, value proposition and positioning everywhere the product is marketed.

At the macro level, the essence of global brands -- quality, reliability, higher status, greater esteem and trust -- remain important. But, as this research suggests, brand trust operates at both the meso (regional) and micro levels (local). One question that arises is whether the global brand trust quotient would be affected by the more typical
local/regional adaptation strategies, such as repositioning or minor changes in IMC strategy?

To extend our research, we encourage further investigations into the relationship of country of origin and brand trust. Such investigations should move beyond the countries of origin presented here. The case of Nepal noted above suggests that consumers in countries with small market size and low levels of economic development might provide intriguing counterparts to research done in more fully developed economies.

Finally, we note one of the most interesting aspects of this research: the accuracy of COO attributions. Combining Samiee et al. (2005)’s findings with Steenkamp, Batra and Alden (2003)’s concepts of “perceived brand globalness,” perhaps there is a complementary concept of “perceived brand localness.” Glocalization strategies are attempts to do just that. If consumers believe a brand to be local, then perhaps it is. In turn, this brings us back our original question: How global are global brands? To date, there is still no definitive answer.

References


Challenges and Opportunities for International Businesses in Kuwait

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Introduction
Kuwait is a small but affluent country in the GCC (Gulf Cooperation Council) region. Kuwait economy is dominated by oil industry with ten percent of the world reserves. With ever increasing oil prices, the Kuwait economy is booming in recent years. The increased oil income boosted economic activity in the country. The business growth and expansion are further facilitated by the liberal economic policies of the Kuwait government. Kuwait started implementing the World Trade Organization (WTO) regime in 2005. This opened up the service industries to outside competition. In addition, other economic policy goals such as the need for diversifying the predominantly oil depended economy and the need to generate employment opportunities for increasing Kuwaiti population are also providing the necessary impetus to expand the private sector in the country. In recent years, Kuwait government started implementing active privatization policies to achieve the national goals. Other national goals such as the desire to develop Kuwait into a regional financial services hub, develop tourism industry with major projects and create new townships to alleviate the housing problems for nationals; have the same effect of expanding the business activity. The traditional non-profit services sectors such as higher education and health care are being opened up for private sectors. These macro-economic developments are creating many business opportunities not only to Kuwaiti nationals but also to international business enterprises. In order to profitably participate in the Kuwait economic development, it behooves international businesses to become fully familiar with the emerging business opportunities and challenges in the context of Kuwait economy. Hence, the major purpose of this chapter is to identify and discuss in detail the business opportunities and challenges in Kuwait to international businesses. The rest of the chapter is presented under the following sections in terms of Kuwait business environmental trends. These trends have significant implications for assessing business opportunities and challenges by international businesses. Business environmental trends included in this paper are:

1. Macro-economic
2. Demographic
3. Employment
4. External trade
5. Major Development Projects
6. Political and Legal
7. Social and Cultural
8. Technological

Macro-economic trends
The Kuwaiti economy is witnessing its best performance in years, as nominal gross domestic product (GDP) growth soared to 35 percent in 2005, following 20 percent plus
growth in each of the previous two years. The oil sector continued to lead growth with soaring oil prices, which contributed 59 percent to GDP. In real terms, the non-oil sector also did equally well. Real GDP went up more than 10 percent in each of the past two years (2006-2007), with the growth in non-oil activities matching the oil sector on the average. Higher government expenditures, accompanied by increased public and private sector investment, boosted domestic spending. With continued strong domestic demand and oil prices reaching new record highs in 2006, it is expected that nominal GDP will increase by more than 12 percent and real growth to be around 5 percent.

Kuwait is currently experiencing its first oil-price-driven economic boom in three decades. The current rise in oil prices can only be compared with the soaring prices in the early 1970s, which also fueled rapid economic growth. However, the current economic expansion differs notably from the one that followed the 1974 jump in oil prices. Then growth was largely led by government spending, with capital spending on infrastructure playing an important role. In contrast, the current boom has seen the private sector play a far more pivotal role with private investment leading growth, although public spending continued to play a key role as well.

“Analysing GDP by type of expenditure revealed the fact that Kuwait economy was primarily a consumption led economy up to the end of 2005. Through the period 2001 – 05, final consumption- both private and public – continued to account for the major share of GDP followed by net exports. By the end of 2005, they formed 32.2 percent and 15.7 percent respectively of GDP. However, it is important to note that, over years final consumption’s contribution to GDP continued to decline in favor of the increasing share of Net Exports. As a result, Net Exports accounted for the highest contribution in GDP for the first time during 2006.” – AlWatan Daily (May 26, 2008)

<table>
<thead>
<tr>
<th>Table 1 : Gross Domestic Product</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Nominal GDP (KD billion)</strong></td>
</tr>
<tr>
<td>2001: 10.7</td>
</tr>
<tr>
<td>2002: 11.6</td>
</tr>
<tr>
<td>2003: 14.3</td>
</tr>
<tr>
<td>2004: 17.5</td>
</tr>
<tr>
<td>2005: 23.6</td>
</tr>
<tr>
<td>2006: 28.6</td>
</tr>
<tr>
<td>2007: 34.4</td>
</tr>
<tr>
<td><strong>Nominal GDP (US$ billion)</strong></td>
</tr>
<tr>
<td>2001: 37.5</td>
</tr>
<tr>
<td>2002: 40.8</td>
</tr>
<tr>
<td>2003: 50.1</td>
</tr>
<tr>
<td>2004: 61.6</td>
</tr>
<tr>
<td>2005: 83.0</td>
</tr>
<tr>
<td>2006: 100.8</td>
</tr>
<tr>
<td>2007: 120.9</td>
</tr>
<tr>
<td><strong>Nominal GDP growth rate (%)</strong></td>
</tr>
<tr>
<td>2001: -7.5</td>
</tr>
<tr>
<td>2002: 8.3</td>
</tr>
<tr>
<td>2003: 23.0</td>
</tr>
<tr>
<td>2004: 22.9</td>
</tr>
<tr>
<td>2005: 34.7</td>
</tr>
<tr>
<td>2006: 21.4</td>
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<tr>
<td>2007: 20.0</td>
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<tr>
<td><strong>Real GDP (KD billion)</strong></td>
</tr>
<tr>
<td>2001: 11.6</td>
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<tr>
<td>2002: 11.9</td>
</tr>
<tr>
<td>2003: 14.0</td>
</tr>
<tr>
<td>2004: 15.5</td>
</tr>
<tr>
<td>2005: 17.3</td>
</tr>
<tr>
<td>2006: 18.4</td>
</tr>
<tr>
<td>2007: 19.6</td>
</tr>
<tr>
<td><strong>Real GDP (US$ billion)</strong></td>
</tr>
<tr>
<td>2001: 40.8</td>
</tr>
<tr>
<td>2002: 42.0</td>
</tr>
<tr>
<td>2003: 49.3</td>
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<tr>
<td>2004: 54.6</td>
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<tr>
<td>2005: 60.8</td>
</tr>
<tr>
<td>2006: 64.6</td>
</tr>
<tr>
<td>2007: 68.9</td>
</tr>
<tr>
<td><strong>Real GDP growth rate (%)</strong></td>
</tr>
<tr>
<td>2001: 0.2</td>
</tr>
<tr>
<td>2002: 3.0</td>
</tr>
<tr>
<td>2003: 17.3</td>
</tr>
<tr>
<td>2004: 10.7</td>
</tr>
<tr>
<td>2005: 11.4</td>
</tr>
<tr>
<td>2006: 6.3</td>
</tr>
<tr>
<td>2007: 6.6</td>
</tr>
<tr>
<td><strong>Per capita GDP (KD)</strong></td>
</tr>
<tr>
<td>2001: 4,633.8</td>
</tr>
<tr>
<td>2002: 4,789.5</td>
</tr>
<tr>
<td>2003: 5,596.9</td>
</tr>
<tr>
<td>2004: 6,361.3</td>
</tr>
<tr>
<td>2005: 7,887.6</td>
</tr>
<tr>
<td>2006: 8,999.2</td>
</tr>
<tr>
<td>2007: 10,110.8</td>
</tr>
<tr>
<td><strong>Per capita GDP (US$)</strong></td>
</tr>
<tr>
<td>2001: 16,299.1</td>
</tr>
<tr>
<td>2002: 16,846.5</td>
</tr>
<tr>
<td>2003: 19,686.4</td>
</tr>
<tr>
<td>2004: 22,375.1</td>
</tr>
<tr>
<td>2005: 27,743.8</td>
</tr>
<tr>
<td>2006: 31,654.0</td>
</tr>
<tr>
<td>2007: 35,563.8</td>
</tr>
<tr>
<td><strong>Crude Oil Production (million b/d)</strong></td>
</tr>
<tr>
<td>2001: 1.95</td>
</tr>
<tr>
<td>2002: 1.75</td>
</tr>
<tr>
<td>2003: 2.17</td>
</tr>
<tr>
<td>2004: 2.34</td>
</tr>
<tr>
<td>2005: 2.50</td>
</tr>
<tr>
<td>2006: 2.52</td>
</tr>
<tr>
<td>2007: 2.46</td>
</tr>
<tr>
<td><strong>Avg. Kuwait Crude Export Prices (US$/b)</strong></td>
</tr>
<tr>
<td>2001: 21.4</td>
</tr>
<tr>
<td>2002: 23.6</td>
</tr>
<tr>
<td>2003: 26.9</td>
</tr>
<tr>
<td>2004: 34.1</td>
</tr>
<tr>
<td>2005: 48.7</td>
</tr>
<tr>
<td>2006: 58.9</td>
</tr>
<tr>
<td>2007: 66.4</td>
</tr>
</tbody>
</table>

(Source: Central Bank of Kuwait, 2008, (Note: At the Current exchange rate 1 KD = US$3.7))

Oil Sector
Oil portion of Gross Domestic Product (GDP) rose to KD 13.83 billion in 2005, which was more than 60 percent following the previous two years of strong growth. Crude oil, which accounted for 93 percent of oil GDP, generated most of the sector’s growth as oil prices rose significantly. The price of Kuwait export crude averaged $46.8 per barrel, up 48 percent on the previous year’s average. Oil production was also higher, increasing 12.4 percent to 2.57 million barrels per day. Value added by petroleum refining, which accounted for the remaining 7.2 percent of oil GDP, also saw rapid growth of 26 percent, although this was slower than the previous year’s growth of 39 percent. The increase was primarily driven by higher refining margins that averaged $10.5 per barrel. The value added by the oil sector should rise by about 13 percent in 2006.

Non-Oil Sector
Growth in the non-oil sector was solid at 10.7%, with non-oil GDP rising to KD 10.4 billion. Growth was slower than in the previous two years (2005 - 2007), when it had benefited from a boost in trade and business activity following the end of war in Iraq. This trend, which saw Kuwait become a base for foreign companies doing business in the Iraqi market and a conduit for a large part of Iraq’s imports, has continued, though at a slower pace. The sectors that benefited the most from the trend were transport, storage, communications, and business services. In 2005, these sectors continued to grow, at a slower pace as the trend matured and the security situation in Iraq worsened resulting in limited growth in business activities between the two countries. Nevertheless, transport and storage remained the fastest-growing non-oil activity, with its contribution to GDP rising by 25 percent. Their growth was driven in large part by the rise in oil shipments, but also by growth in re-exports and logistics services related to Iraq. Communications ranked second with a rapid growth of 22 percent compared with last year’s (2006) 25 percent rate. The much-smaller business services sector also saw rapid growth of 16 percent.

Financial institutions, which continued to be the leading non-oil sector in the economy in terms of contribution to non-oil Gross Domestic Product (GDP), saw rapid growth of 20 percent. At 17.2 percent of non-oil GDP, their size has surpassed public administration and defense in the last two years. The solid performance of banks and investment companies raised their importance in the economy, though most of the value added by this sector is from profits, a big part of which is investment related.

Real estate services are second in importance among activities led by the private sector. However, this sector’s growth was disappointing at 3.8 percent, although it was slightly higher in the previous year’s 3.1 percent. Real estate services’ contribution to non-oil Gross Domestic Product (GDP) decreased from 13.4 percent in 2002 to 10.9 percent in 2005.
Table 2: GDP by Economic Activity
(in current prices)

<table>
<thead>
<tr>
<th>Million KD</th>
<th>percent change</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2003</td>
</tr>
<tr>
<td>Agriculture &amp; Fishing</td>
<td>65</td>
</tr>
<tr>
<td>Mining &amp; Quarrying</td>
<td>5,815</td>
</tr>
<tr>
<td>Petroleum Refining</td>
<td>572</td>
</tr>
<tr>
<td>Manufacturing (excl. refining)</td>
<td>555</td>
</tr>
<tr>
<td>Electricity, Gas, &amp; Water</td>
<td>299</td>
</tr>
<tr>
<td>Construction</td>
<td>349</td>
</tr>
<tr>
<td>Trade, Hotels &amp; Restaurants</td>
<td>1,064</td>
</tr>
<tr>
<td>Transport, Storage, Communication</td>
<td>800</td>
</tr>
<tr>
<td>Finance, Real Estate, &amp; Business Services</td>
<td>2,485</td>
</tr>
<tr>
<td>Community, Social, &amp; Personal Services</td>
<td>2,726</td>
</tr>
<tr>
<td><strong>Subtotal</strong></td>
<td>14,731</td>
</tr>
<tr>
<td>less: Imputed Bank Services</td>
<td>613</td>
</tr>
<tr>
<td><strong>GDP at Producer Prices</strong></td>
<td>14,118</td>
</tr>
<tr>
<td>plus: Import Duties</td>
<td>135</td>
</tr>
<tr>
<td><strong>GDP at Purchaser Prices</strong></td>
<td>14,254</td>
</tr>
</tbody>
</table>


Wholesale and retail trade, whose share of non-oil GDP was slightly lower than real estate, also saw moderate and slowing growth of 4.2 percent compared with 8.2 percent and 6.7 percent registered in the previous two years (2005-2007), respectively. This may come as a surprise given that growth in imports nearly doubled and that much of the wholesale trade activities are import related. These suggested substantial revisions could be made to this sector's figures in the future.

Construction, which represented nearly 5 percent of non-oil activities, registered strong growth of 13 percent following double-digit growth in the previous two years. In the manufacturing sector, chemicals and chemical products, which included petrochemicals, saw a third year of strong growth. However, at 23.5 percent, that growth was slower than in the previous two years. Strong global demand helped lift prices of commodities and
related industries in general. Fabricated metals also performed well because this subsector tended to be correlated with construction activity.

**GDP by Type of Expenditure**

Strong growth in fixed investment spending and private consumption fueled a rapid 19 percent increase in domestic demand, contributing to 41 percent of the growth in total expenditure on GDP. However, the primary engine behind the strong economic performance remained exports, specifically oil exports. Meanwhile, imports rose more than 26 percent, the strongest increase since liberation (1991).

Investment, which has seen strong growth in recent years, soared still higher. Gross capital formation rose 49 percent following increases of 19 percent and 32 percent in the previous two years (2005-2007), respectively. The growth reflected strong private sector investment, particularly in the real estate sector, in addition to the rapid growth in capital spending by the government on development and maintenance projects. Accordingly, investment’s share of domestic demand surged to 30 percent, or 20 percent of GDP.

Private consumption, which represented almost half of domestic demand, also increased at a rapid 13 percent rate. Growth was fueled by higher transfers to households and salary increases for government employees and Kuwaiti nationals. Consumer spending also benefited from the boom in real estate and equity markets, with wealth effect on consumer wallets. In contrast, government consumption spending continued to moderate for a third consecutive year, rising a more modest 4.6 percent.

| Table 3: Aggregate Expenditures on GDP *(in current prices)* |
|-----------------|-------|-------|-------|-------|-------|-------|
|                 | Million KD |       |       | percent Change |       |       |
|                 | 2003   | 2004   | 2005   | 2003   | 2004   | 2005   |
| **Total Expenditures on GDP** | 14,254 | 17,466 | 23,588 | 23.0 | 22.5 | 35.1 |
| Government Consumption | 3,281 | 3,478 | 3,637 | 12.0 | 6.0 | 4.6 |
| Private Consumption | 6,098 | 6,574 | 7,395 | 6.1 | 7.8 | 12.5 |
| Gross Capital Formation | 2,359 | 3,116 | 4,656 | 19.2 | 32.1 | 49.4 |
| Net Exports | 2,515 | 4,298 | 7,900 | 171.0 | 70.9 | 83.8 |
| Exports | 7,432 | 9,970 | 15,059 | 43.7 | 34.1 | 51.0 |
| Imports | 4,917 | 5,672 | 7,159 | 15.9 | 15.4 | 26.2 |
| **Domestic Demand** | 11,739 | 13,168 | 15,688 | 10.2 | 12.2 | 19.1 |


*“Domestic Demand” is defined as government and private consumption and gross capital formation.*
Inflation, as measured by Consumer Price Index (CPI) has gone up to unprecedented level of 7.1 percent in the 4th quarter of 2007 standing at 122.2 points. Such inflation level came on top of 3.03 percent reported by the end of 2006. It is important to note that inflation rates went through an increasing trend over the last four quarters. More importantly, was the higher inflation rates reported during the year 2007.

On a monthly basis inflation picked up even much more rapidly to hit new records above 7.54 percent up to the end of December 2007 to stand at 124.1 points. Entering the year 2008, figures from Central Statistics Office revealed inflation picking up even more too unprecedented record levels of 9.53 percent by the end of January 2008. According to the data, CPI hit 126.4 points by the end of January 2008 as compared with 115.4 points a year ago.

Table 4: Constituents of CPI (2000=100)

<table>
<thead>
<tr>
<th>Categories</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>1Q07</th>
<th>2Q07</th>
<th>3Q07</th>
<th>4Q07</th>
</tr>
</thead>
<tbody>
<tr>
<td>Food</td>
<td>103.1</td>
<td>104.5</td>
<td>106.6</td>
<td>110</td>
<td>119.4</td>
<td>124</td>
<td>129.6</td>
<td>127.4</td>
<td>128.6</td>
<td>133.9</td>
</tr>
<tr>
<td>Beverages &amp; Tobacco</td>
<td>101.5</td>
<td>105.8</td>
<td>107.5</td>
<td>111.2</td>
<td>112.2</td>
<td>114.3</td>
<td>119.3</td>
<td>118.5</td>
<td>122.6</td>
<td>128.9</td>
</tr>
<tr>
<td>Clothing &amp; Footwear</td>
<td>103.2</td>
<td>105.9</td>
<td>108</td>
<td>111</td>
<td>118.1</td>
<td>122.8</td>
<td>126.6</td>
<td>128</td>
<td>128</td>
<td>131.9</td>
</tr>
<tr>
<td>Housing Services</td>
<td>101.1</td>
<td>102.1</td>
<td>103.8</td>
<td>104.6</td>
<td>105.3</td>
<td>108</td>
<td>110.4</td>
<td>113.4</td>
<td>117.6</td>
<td>123.3</td>
</tr>
<tr>
<td>Household goods &amp; services</td>
<td>96.9</td>
<td>99.1</td>
<td>100.3</td>
<td>96</td>
<td>99.5</td>
<td>102.2</td>
<td>103.7</td>
<td>105.1</td>
<td>106.1</td>
<td>108.2</td>
</tr>
<tr>
<td>Transport &amp; Communications</td>
<td>99.1</td>
<td>95</td>
<td>93.8</td>
<td>99.8</td>
<td>100.7</td>
<td>102.6</td>
<td>109.6</td>
<td>110</td>
<td>110.2</td>
<td>111.1</td>
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<td>Education &amp; Medical Care</td>
<td>103.9</td>
<td>106.6</td>
<td>112.4</td>
<td>116.6</td>
<td>123.2</td>
<td>126.2</td>
<td>126</td>
<td>126.4</td>
<td>134.7</td>
<td>140.8</td>
</tr>
<tr>
<td>Other goods &amp; services</td>
<td>106.2</td>
<td>108.5</td>
<td>105.7</td>
<td>102</td>
<td>110</td>
<td>115.3</td>
<td>117.4</td>
<td>117</td>
<td>119</td>
<td>119</td>
</tr>
<tr>
<td>General Index</td>
<td>101.3</td>
<td>102.2</td>
<td>103.2</td>
<td>104.5</td>
<td>108.8</td>
<td>112.1</td>
<td>115.7</td>
<td>116.5</td>
<td>118.7</td>
<td>122.2</td>
</tr>
<tr>
<td>Y-o-Y change</td>
<td>1.30%</td>
<td>.89%</td>
<td>.98%</td>
<td>1.26%</td>
<td>4.11%</td>
<td>3.03%</td>
<td>4.33%</td>
<td>5.05%</td>
<td>5.32%</td>
<td>7.10%</td>
</tr>
</tbody>
</table>

(Source: Central Bank of Kuwait, 2008)

Demographic Trends

The total population of Kuwait by the end of 2005 was 2.99 million. This was an increase of 8.63 percent over 2004. The growth rate of Kuwaiti population was 3.76 percent in 2005; this rate of growth was more than in 2004. The growth rate of non-Kuwaiti population in 2005; was 11.2 percent, which was almost the same as the rate of growth in 2004. The Kuwaiti population is growing at an increasing rate , while the non-Kuwaiti population is growing at a constant rate.
The Kuwaiti population by the end of 2005 was 33.2 percent of the total population, as compared to 34.7 percent in 2004, 36.4 percent in 2003. Whereas the non-Kuwaiti population was 66.8 percent of the total population by the end of 2005 as compared to 65.3 percent in 2004.

In general, the number of Kuwaiti females exceeded the number of males (51 percent females and 49 percent males by the end of 2005). This ratio was almost the same as in 2004. However, the percentage of non-Kuwaiti males was significantly more than the percentage of non-Kuwaiti females (69.6 percent in 2005). Percentage of females in Non-Kuwaiti population was only 30.4 percent in 2005.

The distribution of population according to age groups indicates the dominance of young Kuwaiti population. By the end of 2005, the percentage of young Kuwaiti people in the age groups less than 15 years was 40 percent of total Kuwaiti population, as compared to 40.5 percent in 2004. The percentage of Kuwaiti population less than 30 years of age was 67.9 percent in 2005, as compared to 68.3 percent in 2004. The majority of non-Kuwaiti population is concentrated in age group of 25-49 years (66.4 percent in 2005). The young non-Kuwaiti population (less than 15 years) accounted for only 12.4 percent in 2005.

The percentage of illiteracy among the Kuwaiti population continued to fall. It was 5.7 percent by the end of 2005 as compared to 6 percent in 2004, 6.8 percent in 2002, and 8 percent in 1999. The educational status of Kuwaiti population in 2005 was as following: Illiterates (5.7 percent), Just read and write (11.5 percent), primary school (20.9 percent), intermediate school (27.9 percent), high school (15.9 percent), diploma (7.5 percent) and university and higher education (10.7 percent).

Table 5: Total population (Kuwaiti and Non-Kuwaiti) according to Age groups and gender

<table>
<thead>
<tr>
<th>Age Groups</th>
<th>Kuwaiti Male</th>
<th>Kuwaiti Female</th>
<th>Kuwaiti Total</th>
<th>Non-Kuwaiti Male</th>
<th>Non-Kuwaiti Female</th>
<th>Non-Kuwaiti Total</th>
<th>Total Male</th>
<th>Total Female</th>
<th>Total Population</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 5</td>
<td>72317</td>
<td>70591</td>
<td>142908</td>
<td>46447</td>
<td>43465</td>
<td>89912</td>
<td>118764</td>
<td>114056</td>
<td>232820</td>
</tr>
<tr>
<td>5 – 9</td>
<td>67556</td>
<td>64267</td>
<td>131823</td>
<td>43764</td>
<td>41244</td>
<td>85008</td>
<td>111320</td>
<td>105511</td>
<td>216831</td>
</tr>
<tr>
<td>10 – 14</td>
<td>61973</td>
<td>59659</td>
<td>121632</td>
<td>38935</td>
<td>33390</td>
<td>72325</td>
<td>100908</td>
<td>93049</td>
<td>193957</td>
</tr>
<tr>
<td>15 – 19</td>
<td>54506</td>
<td>53253</td>
<td>107759</td>
<td>41126</td>
<td>34286</td>
<td>75412</td>
<td>95632</td>
<td>87539</td>
<td>183171</td>
</tr>
<tr>
<td>20 – 24</td>
<td>45589</td>
<td>45818</td>
<td>91407</td>
<td>113585</td>
<td>62607</td>
<td>176192</td>
<td>159174</td>
<td>108425</td>
<td>267599</td>
</tr>
<tr>
<td>25 – 29</td>
<td>38051</td>
<td>40005</td>
<td>78056</td>
<td>249828</td>
<td>96579</td>
<td>346407</td>
<td>287879</td>
<td>136584</td>
<td>424463</td>
</tr>
<tr>
<td>30 – 34</td>
<td>33183</td>
<td>36467</td>
<td>79650</td>
<td>235967</td>
<td>86213</td>
<td>322180</td>
<td>269150</td>
<td>122680</td>
<td>391830</td>
</tr>
<tr>
<td>35 – 39</td>
<td>28900</td>
<td>32343</td>
<td>61243</td>
<td>215764</td>
<td>77304</td>
<td>293068</td>
<td>244664</td>
<td>109647</td>
<td>354311</td>
</tr>
<tr>
<td>40 – 44</td>
<td>23836</td>
<td>27315</td>
<td>51151</td>
<td>157793</td>
<td>55910</td>
<td>213703</td>
<td>181629</td>
<td>83225</td>
<td>264854</td>
</tr>
<tr>
<td>45 – 49</td>
<td>17230</td>
<td>22027</td>
<td>39257</td>
<td>115139</td>
<td>35740</td>
<td>150879</td>
<td>132369</td>
<td>57767</td>
<td>190136</td>
</tr>
<tr>
<td>50 – 54</td>
<td>13023</td>
<td>17023</td>
<td>30046</td>
<td>69066</td>
<td>18700</td>
<td>87766</td>
<td>72089</td>
<td>35723</td>
<td>117812</td>
</tr>
<tr>
<td>55 – 59</td>
<td>8606</td>
<td>12611</td>
<td>21217</td>
<td>36511</td>
<td>9897</td>
<td>46408</td>
<td>45117</td>
<td>22508</td>
<td>67628</td>
</tr>
<tr>
<td>60 – 64</td>
<td>7184</td>
<td>9425</td>
<td>46609</td>
<td>15482</td>
<td>4990</td>
<td>20472</td>
<td>22666</td>
<td>14415</td>
<td>37081</td>
</tr>
<tr>
<td>65 – 69</td>
<td>6376</td>
<td>6754</td>
<td>13130</td>
<td>7321</td>
<td>3172</td>
<td>10493</td>
<td>13697</td>
<td>9926</td>
<td>23623</td>
</tr>
<tr>
<td>70 – 74</td>
<td>3728</td>
<td>4253</td>
<td>7981</td>
<td>2875</td>
<td>1896</td>
<td>4771</td>
<td>6603</td>
<td>6149</td>
<td>12752</td>
</tr>
<tr>
<td>75 – 79</td>
<td>2268</td>
<td>2302</td>
<td>4570</td>
<td>1057</td>
<td>1177</td>
<td>2234</td>
<td>3325</td>
<td>3479</td>
<td>6804</td>
</tr>
<tr>
<td>80 – 84</td>
<td>1036</td>
<td>1212</td>
<td>2248</td>
<td>385</td>
<td>583</td>
<td>968</td>
<td>1421</td>
<td>1795</td>
<td>3216</td>
</tr>
<tr>
<td>85 or more</td>
<td>727</td>
<td>803</td>
<td>1530</td>
<td>277</td>
<td>497</td>
<td>774</td>
<td>1004</td>
<td>1300</td>
<td>2304</td>
</tr>
<tr>
<td>TOTAL</td>
<td>486089</td>
<td>506128</td>
<td>992217</td>
<td>1391322</td>
<td>607650</td>
<td>1998972</td>
<td>1877411</td>
<td>1113778</td>
<td>2991189</td>
</tr>
</tbody>
</table>

Kuwait’s population is witnessing its third year of rapid growth in 2006. Statistics by the Public Authority for Civil Information (PACI) show that total population rose to 3.05 by June 2006, growing at a 6.5% rate over the previous twelve months. Rapid growth, which has characterized Kuwait’s population since 2001, has been driven in large part by the inflow of expatriate workers into the country to meet growing demand for labor in a buoyant economic environment.

Table 6: Population
(at mid-year)

<table>
<thead>
<tr>
<th>Year</th>
<th>Population (‘000)</th>
<th>Percent Growth</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Kuwait</td>
<td>Non-Kuwaiti</td>
</tr>
<tr>
<td>2003</td>
<td>913.5</td>
<td>1570.8</td>
</tr>
<tr>
<td>2004</td>
<td>942.9</td>
<td>1701.9</td>
</tr>
<tr>
<td>2005</td>
<td>973.3</td>
<td>1893.6</td>
</tr>
<tr>
<td>2006</td>
<td>1008.1</td>
<td>2043.8</td>
</tr>
</tbody>
</table>

(Source: Public Authority of Civil Information, 2007)

The expatriate population has grown at an average annual rate of 6.5% since 2001. The growth had accelerated until a year ago, peaking at 11.3% in the twelve months ending June 2005, before dropping to a still rapid 7.9% rate in the last twelve month period. The number of non-Kuwaitis reached 2.04 million to represent 67% of the total population, 86% of whom participate in the labor force. The expatriate population is heavily skewed toward males, who account for almost 70% of non-Kuwaitis. To adjust such imbalances, the government eased residency requirements for family members in 2005, by reducing the minimum monthly income needed for applicants to issue a residency permit for a relative.

The population of Kuwaiti nationals continued to grow at a relatively steady pace rising by 3.6% during the past year 2006. The rate was slightly higher than in recent years, as the population grew at an annual average of 3.3% in the previous four years. Though the Kuwaiti population is relatively young, it is slowly maturing. The percentage of nationals under the age of 19 has fallen from 55% a decade ago to under 51% in June 2006. This is taking place as Kuwaitis are marrying at a later age, and as the fertility rate declines. Despite this maturing trend, the population of Kuwaiti nationals remains a very young one.

Educational Profile of the Adult Population

Kuwait’s adult population – over 20 years of age or older – reached 2.2 million, constituting 73% of the total population. Kuwaiti adults number 498,000; making up 22.5% of the total, while expatriates number 1.7 million.
Around 212,000 adult Kuwaitis – representing 42% of nationals – have some education but have not completed high school. Men account for a disproportionate 55% of this segment. About 15.5% of the Kuwaiti adult population is college educated or has professional training, up from 14.4% five years ago. These figures reflect the rise in the level of education and career expectations in parallel to the economic growth. The government has made tangible efforts to improve the accessibility and quality of education. Kuwaiti women are more likely to have a university education than Kuwaiti men, and constitute almost 64% of total nationals with college education.

Table 7: Population by Educational Attainment

<table>
<thead>
<tr>
<th></th>
<th>Kuwaiti Male</th>
<th>Kuwaiti Female</th>
<th>Kuwaiti Total</th>
<th>Non-Kuwaiti Male</th>
<th>Non-Kuwaiti Female</th>
<th>Non-Kuwaiti Total</th>
<th>Grand Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adult Population (‘000)</td>
<td>234</td>
<td>264</td>
<td>498</td>
<td>1257</td>
<td>463</td>
<td>1720</td>
<td>2217</td>
</tr>
<tr>
<td>No Education</td>
<td>6</td>
<td>34</td>
<td>41</td>
<td>79</td>
<td>38</td>
<td>117</td>
<td>157</td>
</tr>
<tr>
<td>Can read and write</td>
<td>11</td>
<td>15</td>
<td>26</td>
<td>632</td>
<td>228</td>
<td>860</td>
<td>886</td>
</tr>
<tr>
<td>With some schooling</td>
<td>107</td>
<td>80</td>
<td>186</td>
<td>314</td>
<td>99</td>
<td>413</td>
<td>599</td>
</tr>
<tr>
<td>High School</td>
<td>56</td>
<td>52</td>
<td>108</td>
<td>130</td>
<td>57</td>
<td>187</td>
<td>296</td>
</tr>
<tr>
<td>Diploma</td>
<td>25</td>
<td>33</td>
<td>58</td>
<td>37</td>
<td>14</td>
<td>51</td>
<td>109</td>
</tr>
<tr>
<td>University or professional</td>
<td>29</td>
<td>49</td>
<td>78</td>
<td>65</td>
<td>27</td>
<td>92</td>
<td>170</td>
</tr>
<tr>
<td>Adult Population (%)</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Public Authority for Civil Information (www.paci.gov.kw) (June 2006)

Expatriates with at least a high school diploma represent 19% of non-Kuwaiti adults. Although only 5.2% of expatriates hold a university degree, Kuwait still relies on the expatriate labor force to fill a significant number of professional jobs. By June 2006, more than half of adults with professional training or a college degree were expatriates. The percentage of expatriates who have not completed high school but had some schooling is significant, representing as much as 74% of non-Kuwaitis adults. Illiteracy is high among expatriates reaching up to 7% of total non-Kuwaiti adults, with a heavy skew towards men.

Employment trends

Table 8: Labor Force by Gender, nationality and Employment status

<table>
<thead>
<tr>
<th>Nationality</th>
<th>Gender</th>
<th>Unemployed</th>
<th>Employed</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>2003</td>
<td>2004</td>
</tr>
<tr>
<td>KUWAITI</td>
<td>Male</td>
<td>3990</td>
<td>5020</td>
</tr>
<tr>
<td></td>
<td>Female</td>
<td>5614</td>
<td>6612</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>9604</td>
<td>11632</td>
</tr>
</tbody>
</table>
The total number of employees in 2001 was 79617 of which 8.4 percent were in mining and oil sector and 91.6 percent in manufacturing. Value added in the industrial sector in 2001 was KD 5265.8 million of which 87.1 percent was in mining and oil sector and 12.9 percent in manufacturing. The total output in the industrial was KD 7709.3 million in 2001, divided between 60.7 percent from oil and mining sector and 39.3 percent from manufacturing sector.

Table 9: Selected indicators of Industrial Activities and Employment in Kuwait

<table>
<thead>
<tr>
<th>Industrial Activity</th>
<th>Year</th>
<th>Gross Addition to Fixed Assets</th>
<th>Total value added</th>
<th>Gross output</th>
<th>Compensation of Employees</th>
<th>No. of persons engaged</th>
<th>No. of Establishments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mining &amp; Quarrying:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Crude Oil &amp; Natural Gas</td>
<td>1999</td>
<td>233.6</td>
<td>3327.7</td>
<td>3391.8</td>
<td>110.5</td>
<td>6273</td>
<td>3</td>
</tr>
<tr>
<td></td>
<td>2000</td>
<td>176.5</td>
<td>5543.9</td>
<td>5622.3</td>
<td>120.4</td>
<td>6529</td>
<td>3</td>
</tr>
<tr>
<td></td>
<td>2001</td>
<td>188.8</td>
<td>4586.5</td>
<td>4676.3</td>
<td>129.2</td>
<td>6558</td>
<td>3</td>
</tr>
<tr>
<td>Total Mining and Quarrying</td>
<td>1999</td>
<td>233.7</td>
<td>3328.6</td>
<td>3393.8</td>
<td>110.8</td>
<td>6431</td>
<td>7</td>
</tr>
<tr>
<td></td>
<td>2000</td>
<td>176.6</td>
<td>5544.4</td>
<td>5623.1</td>
<td>120.6</td>
<td>6683</td>
<td>6</td>
</tr>
<tr>
<td></td>
<td>2001</td>
<td>188.8</td>
<td>4587</td>
<td>4677.2</td>
<td>129.4</td>
<td>6718</td>
<td>6</td>
</tr>
<tr>
<td>Total Manufacturing Industries</td>
<td>1999</td>
<td>89.3</td>
<td>1015.6</td>
<td>3037.2</td>
<td>243.2</td>
<td>71678</td>
<td>4104</td>
</tr>
<tr>
<td></td>
<td>2000</td>
<td>68.4</td>
<td>801.7</td>
<td>3437</td>
<td>226.2</td>
<td>70463</td>
<td>4109</td>
</tr>
<tr>
<td></td>
<td>2001</td>
<td>186.1</td>
<td>678.8</td>
<td>3032.1</td>
<td>257.2</td>
<td>72899</td>
<td>4130</td>
</tr>
<tr>
<td>Total Mining and Manufacturing</td>
<td>1999</td>
<td>323</td>
<td>4344.2</td>
<td>6431.1</td>
<td>354</td>
<td>78109</td>
<td>4111</td>
</tr>
<tr>
<td></td>
<td>2000</td>
<td>244.9</td>
<td>6346.1</td>
<td>9060.1</td>
<td>346.8</td>
<td>77146</td>
<td>4115</td>
</tr>
<tr>
<td></td>
<td>2001</td>
<td>374.9</td>
<td>5265.8</td>
<td>7709.3</td>
<td>386.6</td>
<td>79617</td>
<td>4136</td>
</tr>
</tbody>
</table>


External Trade Trends

Trade
Kuwait’s merchandise trade surplus continued to widen, rising from KD 4.7 billion in 2004 to KD 8.0 billion in 2005, and KD 8.9 billion in the first 9 months of 2006. In 2005, the surplus amounted to 34 percent of GDP, up from 27 percent in the previous year and a
22 percent average during the previous five years. The rise in oil exports was the main factor behind the improvement.

Oil exports, which account for 95 percent of Kuwait’s total exports, increased 29 percent in the first 9 month of 2006 following a 58 percent increase in 2005 and an average 35 percent rise in the previous two years. Soaring prices for crude oil and refined products were the main driver behind this growth. While a 12.4 percent production increase contributed to export growth last year, it was much smaller in 2006 as production neared full capacity.

Growth in non-oil exports was also strong, mainly in ethylene products and fertilizers. Petrochemicals dominated non-oil exports of Kuwaiti origin and constituted more than half of the total. Other exports included rubber, plastics, and base metals. Re-exports, having grown rapidly since the resumption of trade with Iraq, constituted 25 percent of the total.

Table 10: Summary of Foreign Trade

<table>
<thead>
<tr>
<th></th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>9M06</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Exports</strong></td>
<td>4,969.7</td>
<td>4,666.2</td>
<td>6,162.1</td>
<td>8,428.1</td>
<td>13,101.6</td>
<td>12,371.5</td>
</tr>
<tr>
<td><strong>Oil</strong></td>
<td>4,590.8</td>
<td>4,272.8</td>
<td>5,663.5</td>
<td>7,861.1</td>
<td>12,392.6</td>
<td>11,822.5</td>
</tr>
<tr>
<td><strong>Non-oil</strong></td>
<td>378.9</td>
<td>393.4</td>
<td>498.5</td>
<td>567.0</td>
<td>709.0</td>
<td>549.0</td>
</tr>
<tr>
<td><strong>Ethylene</strong></td>
<td>190.3</td>
<td>191.0</td>
<td>188.4</td>
<td>229.1</td>
<td>311.0</td>
<td>261.0</td>
</tr>
<tr>
<td><strong>Fertilizers</strong></td>
<td>21.5</td>
<td>15.5</td>
<td>31.6</td>
<td>41.1</td>
<td>56.0</td>
<td>47.5</td>
</tr>
<tr>
<td><strong>Other</strong></td>
<td>104.8</td>
<td>121.2</td>
<td>153.3</td>
<td>156.9</td>
<td>162.0</td>
<td>102.5</td>
</tr>
<tr>
<td><strong>Re-exports</strong></td>
<td>62.3</td>
<td>65.7</td>
<td>125.3</td>
<td>140.0</td>
<td>180.0</td>
<td>138.0</td>
</tr>
<tr>
<td><strong>Imports</strong></td>
<td>2,413.3</td>
<td>2,735.8</td>
<td>3,274.1</td>
<td>3,722.2</td>
<td>5,106.4</td>
<td>3,442.1</td>
</tr>
<tr>
<td><strong>Balance of Trade</strong></td>
<td>2,556.5</td>
<td>1,930.5</td>
<td>2,888.0</td>
<td>4,705.8</td>
<td>7,995.2</td>
<td>8,929.4</td>
</tr>
</tbody>
</table>

Note: Imports are stated on c.i.f. basis

After growing by 37 percent in 2005, imports dropped 13 percent in the first 9 months of 2006. An exceptionally large increase in 1Q05 accounted for the drop in imports this year. A comparison of the second and third quarters with the same period in 2005 reveals growth of 10 percent. Rapid growth in domestic demand was the main factor behind the rise in imports. Consumer products constitute the largest share of the import bill, although since the resumption of trade with Iraq and the surge in construction activity, imports of capital goods have increased substantially, making up a larger share of total imports.

According to the latest 2004 data, the European Union, the United States, and Japan remain Kuwait's main trading partners. Trade with these countries increased strongly.
during the three years through 2004, although at a slower rate than trade with developing Asian economies (mainly China and India). Trade with Iraq and inter-GCC trade also saw rapid growth since 2003, when the GCC customs union and resumption of trade with Iraq provided a strong boost.

Kuwait has made efforts to strengthen trade relations with partners in the region as well as internationally. Starting January 2005, Kuwait began enforcing a zero-tariff regime on exports originating from members of the Greater Arab Free Trade Area. The same year also witnessed the signing of a number of bilateral trade agreements for the promotion of bilateral investment and the avoidance of double taxation, including with South Africa, South Korea, Singapore, Malaysia, and Hong Kong. Additionally, Kuwait signed a trade and investment framework agreement with the United States as a first step toward a free trade agreement. Within the GCC framework, the country is taking part in negotiations that will lead to free trade agreements with the European Union, China, Japan, and Turkey.

Table 11: Top Trade Partners

(million KD)

<table>
<thead>
<tr>
<th></th>
<th>Exports percent Change</th>
<th>Imports percent Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Trade</td>
<td>7,380</td>
<td>-3</td>
</tr>
<tr>
<td>U.S. and Canada</td>
<td>931</td>
<td>-7</td>
</tr>
<tr>
<td>Japan</td>
<td>1,542</td>
<td>-5</td>
</tr>
<tr>
<td>European Union</td>
<td>726</td>
<td>-20</td>
</tr>
<tr>
<td>West Asia</td>
<td>197</td>
<td>-12</td>
</tr>
<tr>
<td>Gulf Co-operation Council</td>
<td>145</td>
<td>7</td>
</tr>
<tr>
<td>Developing Asia</td>
<td>3,851</td>
<td>8</td>
</tr>
<tr>
<td>Other</td>
<td>132</td>
<td>-37</td>
</tr>
</tbody>
</table>


Kuwait Trade surplus continued to grow for the fifth year in row up to the end of 2007. Trade surplus grew rapidly by 29.7 percent over the period 2001-07. Such growth was supported by increasing exports over the year surpassing the growth in imports of 23.6 percent and 14.8 percent respectively. By the end of 2007 , trade surplus budged to a new landmark of 12.2 billion Kuwaiti dinars over last year’s peak of KD11.5 billion. Such increase translates into a growth rate of 5.6 percent on top of 35.9 percent of growth reported last year. As a result of its declining growth rate in 2007 trade surplus represented 35.4 percent of the GDP down from 40.3 percent in 2006.
### Table 12: Non Oil Exports by origin

<table>
<thead>
<tr>
<th>Year</th>
<th>Manufactured Fertilizers</th>
<th>Ethylene Products</th>
<th>Other</th>
<th>Re-Exports</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>21.5</td>
<td>190.3</td>
<td>104.8</td>
<td>62.3</td>
<td>378.9</td>
</tr>
<tr>
<td>2002</td>
<td>15.5</td>
<td>191.0</td>
<td>121.2</td>
<td>65.7</td>
<td>393.4</td>
</tr>
<tr>
<td>2003</td>
<td>31.6</td>
<td>188.4</td>
<td>153.3</td>
<td>125.2</td>
<td>498.5</td>
</tr>
<tr>
<td>2004</td>
<td>41.1</td>
<td>229.0</td>
<td>156.9</td>
<td>140.0</td>
<td>567.0</td>
</tr>
<tr>
<td>2005</td>
<td>56.0</td>
<td>311.0</td>
<td>162.0</td>
<td>180.0</td>
<td>709.0</td>
</tr>
<tr>
<td>2006</td>
<td>63.5</td>
<td>348.0</td>
<td>138.5</td>
<td>186.0</td>
<td>736.0</td>
</tr>
<tr>
<td>2007</td>
<td>76.0</td>
<td>400.0</td>
<td>160.0</td>
<td>207.0</td>
<td>843.0</td>
</tr>
<tr>
<td>Growth rate</td>
<td>23.4 percent</td>
<td>13.2 percent</td>
<td>7.3 percent</td>
<td>22.2 percent</td>
<td>14.3 percent</td>
</tr>
</tbody>
</table>

(Source: Central Bank of Kuwait, 2008)

### Table 13: Balance of Trade

<table>
<thead>
<tr>
<th>KD Million</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>Growth rate (01-07)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Exports</td>
<td>4,970</td>
<td>4,666</td>
<td>6,162</td>
<td>8,428</td>
<td>13,102</td>
<td>16,167</td>
<td>17,689</td>
<td>23.6 percent</td>
</tr>
<tr>
<td>Oil Exports</td>
<td>4,591</td>
<td>4,273</td>
<td>5,664</td>
<td>7,861</td>
<td>12,393</td>
<td>15,431</td>
<td>16,846</td>
<td>24.2 percent</td>
</tr>
<tr>
<td>Non-Oil Exports</td>
<td>379</td>
<td>393</td>
<td>499</td>
<td>567</td>
<td>709</td>
<td>736</td>
<td>843</td>
<td>14.3 percent</td>
</tr>
<tr>
<td>Total Imports</td>
<td>2,413</td>
<td>2,736</td>
<td>3,274</td>
<td>3,722</td>
<td>4,614</td>
<td>4,629</td>
<td>5,510</td>
<td>14.8 percent</td>
</tr>
<tr>
<td>Balance of Trade</td>
<td>2,556</td>
<td>1,930</td>
<td>2,888</td>
<td>4,706</td>
<td>8,488</td>
<td>11,538</td>
<td>12,179</td>
<td>29.7 percent</td>
</tr>
</tbody>
</table>

(Source: Central Bank of Kuwait, 2008)

### Table 14: Select Construction Projects

*(million KD)*

<table>
<thead>
<tr>
<th>Project</th>
<th>Value</th>
<th>Status</th>
<th>Project Start</th>
<th>Project End</th>
</tr>
</thead>
<tbody>
<tr>
<td>Silk City (Tamdeen/Ajial)</td>
<td>24,820</td>
<td>Planned</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subiya Urban Development (PAHC)</td>
<td>5,840</td>
<td>Planned</td>
<td>2008</td>
<td>2012</td>
</tr>
<tr>
<td>Arifjan/Sabah Al-Ahmad Urban Housing (PAHC)</td>
<td>2,920</td>
<td>Design</td>
<td>2007</td>
<td>2012</td>
</tr>
<tr>
<td>Mutlaa Township (PAHC)</td>
<td>2,920</td>
<td>Planned</td>
<td>2008</td>
<td>2012</td>
</tr>
<tr>
<td>Fahd Al-Abdullah Township (PAHC)</td>
<td>2,920</td>
<td>Planned</td>
<td>2008</td>
<td>2012</td>
</tr>
</tbody>
</table>
### Major Development Projects

**Construction Activity**

Government spending on development and maintenance projects has seen solid growth for five consecutive years, giving rise to a boom in construction activity. The fiscal accounts for 2005/2006 show capital spending reaching KD 750 million, or 11% of total government spending, compared with KD 570 million two years earlier.

The bulk of the increase in spending was at the Ministry of Public Works (MPW), which also accounted for a third of capital expenditures. MPW also accounts for a list of government-sponsored projects with schemes worth KD 1 billion (US$ 3.4 billion) including the development of Boubyan and Failaka islands. The Public Authority for Housing Care, with its independent budget, has a still more sizable portfolio, including multimillion-dinar housing projects and township developments. In total, government and affiliated institutions are sole sponsors on roughly KD 10 billion in projects, awarded or under way.

Although government spending has played a key role in the current construction boom, increased private investment has also contributed to the sector’s growth. Roughly KD 2.5
billion in private investments have been earmarked to real estate projects since 2005, encouraged by amendments to the building code that lifted the maximum permitted built area to 210% of a plot’s surface area for residential plots, and to 270% for investment plots. Rapidly rising rents across commercial, residential, and investment sectors have also helped boost private investment. In the future, the government is expected to contribute further to the growth in private investment through planned public-private-partnership (PPP) initiatives, including the proposed multibillion-dinar developments at Failaka and Boubyan islands.

In line with the increase in construction activity, commercial loans for the construction sector increased 30% in 2005 and an additional 27% in the first three quarters of 2006 to reach KD 974 million. Commercial loans to the real estate sector also increased 25% and 17% in the two periods, respectively, reaching almost KD 3 billion. Bank loans extended to the construction and real estate sectors constituted 28.5% of local banks' total loans to residents at the end of September 2006.

**Building Permits**

<table>
<thead>
<tr>
<th>Permits Issued</th>
<th>% Change</th>
<th>% of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>New Construction</td>
<td>35.3%</td>
<td>40%</td>
</tr>
<tr>
<td>Commercial</td>
<td>-64.3%</td>
<td>1%</td>
</tr>
<tr>
<td>Investment</td>
<td>5.2%</td>
<td>10%</td>
</tr>
<tr>
<td>Industrial</td>
<td>-66.0%</td>
<td>1%</td>
</tr>
<tr>
<td>Residential</td>
<td>-41.1%</td>
<td>28%</td>
</tr>
<tr>
<td>Additions</td>
<td>-29.0%</td>
<td>50%</td>
</tr>
<tr>
<td>Renovations</td>
<td>-57.9%</td>
<td>11%</td>
</tr>
<tr>
<td>Total</td>
<td>-36.1%</td>
<td>100%</td>
</tr>
</tbody>
</table>

*Source: Kuwait Municipality (www.municipality.gov.kw), 2006.*

Buoyant construction activity ought to be reflected in a rise in the number of building permits issued, however data are not yet available for 2006. The Kuwait Municipality reported issuing around 9,700 permits in 2005, 6% more than in the previous year. Although permits issued for additions and renovations accounted for 60% of this growth, the rise in permits issued for new construction was solid compared with the previous year.

Permits for new construction were mainly issued for residential properties. The number of industrial permits also increased significantly during the year, but they constituted only
a small part of permits. Meanwhile, permits for the construction of investment properties, primarily multi-story residential apartment buildings, experienced a significant drop, possibly as a result of an increase in interest rates and the rapid growth experienced by this sector in prior years.

Infrastructure

Transportation:

Kuwait's road system links Kuwait City to every population center within the country as well as to the Saudi Arabia and Iraq borders. Kuwait has no railroads.

Kuwait has three commercial ports. The largest port is located at Shuwaikh (near Kuwait City) and has a total of 21 berths. Shuaibia, 50 km south of Kuwait City, is mainly used for the import of heavy equipment and materials. The smallest port is located at Doha and has 20 small berths. Mina al-Ahmadi, 40 km south of Kuwait City, is Kuwait's oil port and is capable of loading over two million barrels of oil per day.

Kuwait has 4 airports with permanent-surface runways all between 2,440-3,659 m in length. The country's primary airport is Kuwait International in Kuwait City.

Communications:

Kuwait's civil network suffered extensive damage as a result of the Gulf War and reconstruction is still under way with some restored international and domestic capabilities. The country's communications capability is comprised of the following:

- 3 AM, 0 FM, 3 TV broadcast stations
- Satellite earth stations
  - Destroyed during Gulf War and not yet rebuilt; temporary mobile satellite ground stations provide international telecommunications
- Coaxial cable and microwave radio relay to Saudi Arabia

Roads

An extensive network of mostly well surfaced roads covers the country. There are 5,749 km of bituminous roads and another 1,000 km of road surfaced with earth, sand or gravel. Buoyed by high income from oil in three decades, Kuwait announced a number of road infrastructure projects in the second half of 2005 including a 25 km causeway linking the northern area of Subbiya with Kuwait City at a cost of USD1.5 billion as well as two main road projects linking Iraq to the Kuwaiti port of Bubiyan and to Saudi Arabia for an additional 250 km. There are also plans to upgrade the country's system of seven ring roads with the addition of an eighth ring road to divert traffic away from the suburbs of Kuwait city.

Railways
There is no railway network in Kuwait but discussions are underway regarding the development of a domestic rail network as part of an overall USD5 billion Gulf rail link and the building of an underground metro system. During the visit of the then German chancellor, Gerhard Schröder, in March 2005, the possibility of the sale of a magnetic above-the-ground railway option was also discussed. This would link into the regional plan to provide a railway link between Kuwait and Muscat. The exact route of the Metro has yet to be defined but it is likely to consist of a 32 km section from Ardiya to Salmiya as part of the first phase, with two further phases to extend the line, southwards to Fintas and Fahaheel and westwards to Shuwaikh. The network would include both surface and underground rails and is projected to carry an average of 8,000 passengers an hour.

Ports

Kuwait exports its oil and refined hydrocarbon products through the ports of Mina Ahmadi, Mina Abdullah, Mina Az-Zoor and Shuaiba. Kuwait also has two commercial sea-ports, in Shuwaikh and Shuaiba, for imports and non-oil exports. These ports handle bulk, containerised, refrigerated and general cargoes and they also have Ro-Ro (roll-on roll-off) facilities. A third commercial port in Doha is used by dhows and barges carrying light cargoes between Kuwait and Iran and ports lower down in the Gulf.

The country is also developing its logistics infrastructure, especially with the Kuwait Free Trade Zone (KFTZ), which is located in Shuwaikh Port, close to the international airport. Operational since 2000, it offers a range of business-friendly incentives, including 100% foreign ownership, tax exemption and full repatriation of capital and profits. Backed by established infrastructure and advanced telecommunication systems, the free zone has already proved a valuable asset to the country's logistics industry, although simplifying the current procedures could boost activities further.

"The free zone is strategically located in Shuwaikh Port providing access to these big potential markets in northern Iran, Iraq, Turkey, the Commonwealth of Independent States or the CIS," says DHL's Parker. "However, it is currently at an early stage in terms of capacity and operations. The procedures are not very user friendly as it could take up to three days to process a Kuwait inbound or outbound clearance process."

Indeed, the local government's ability to simplify procedures and further develop its infrastructure will naturally play an important role in transforming Kuwait into a logistical superhub. – (The Arabian Business.com, February 1, 2007).

Political and Legal Trends

The political system

Kuwait votes in a parliamentary election on Saturday (May 17, 2008), two months after its ruler dissolved parliament to end a crisis within the government.
Following are some facts about the Gulf Arab state's political system:

* Kuwait gained independence from Britain in 1961 and its first fully-elected parliament was voted in 1963.

* Kuwait has a 50-seat parliament with a history of challenging the government, unusual for a region dominated by families. Deputies have to approve the state budget and all major laws. They often exercise their right to question ministers, sometimes prompting them to resign under pressure.

* Kuwait's ruler, Emir Sheikh Sabah al-Ahmad al-Sabah, has the last say in policy. He can dissolve the assembly and appoint new governments. Key cabinet portfolios such as defence, interior and foreign affairs are held by members of the ruling al-Sabah family, none of whom have ever held a parliament seat.

* The emir or his predecessors have dissolved parliament five times since its establishment -- in 2008, 2006, 1999, 1986 and 1976. According to Kuwaiti law, elections must be held within 60 days of the assembly being dissolved, but rulers have ignored this rule before, suspending the assembly for five years from 1976 and six years from 1986.

* Kuwait does not allow political parties but tolerates informal political groups. These include the hardline Islamist Salafist movement, the liberal Democratic Forum Bloc, the Shi'ite Muslim-led National Islamic Coalition, the Islamist Ummah Party, the Islamic Constitutional Movement and the liberal Popular Action Bloc.

* Parliament passed a law in May 2005 giving women the right to vote and run in elections for the National Assembly. No woman was elected in the last vote in 2006.

* The current emir is the 15th ruler in a dynasty which has ruled Kuwait for 250 years since part of the Anaiza tribe, to which the al-Sabah belong, migrated from the Arabian hinterland.

* Since the U.S.-led invasion of neighbouring Iraq in 2003 and U.S. calls for change in the Middle East, the ruling family has come under pressure from both Islamists and pro-Western liberals to loosen its grip on government and share power.

* In July 2003, the emir issued a landmark decree separating the post of prime minister from the crown prince for the first time since Kuwait's independence.

* Kuwait passed a new election law in 2006 cutting the number of constituencies from 25 to five in the hope that it would increase competition and reduce vote-buying that has long marred polls.

* Some 361,685 Kuwaitis, over half of them women, are eligible to vote in the 2008 election. Members of the security forces are not allowed to vote, nor are expatriates, who form almost 2.2 million of Kuwait's 3.2 million population.
* Over 270 candidates, including 27 women, contested in 2008 election.

* Changes of the oil minister usually do not have an impact on the energy policy of the major OPEC producer.

(Source: FACTBOX – Some facts about Kuwait’s political system, Reuters India, May 17, 2008)

**Legal Framework for doing business**

**Legal forms of companies**

<table>
<thead>
<tr>
<th>Form</th>
<th>Number of partners/shareholders</th>
<th>Minimum and/or maximum capital</th>
<th>Liability</th>
<th>Registration fee</th>
<th>Release of financial documents</th>
</tr>
</thead>
<tbody>
<tr>
<td>The close shareholding company</td>
<td>Minimum 5 partners.</td>
<td>KWD 7,500 minimum capital.</td>
<td>Partners' liability is limited to the amount contributed.</td>
<td>About KWD 3,000.</td>
<td>Yes</td>
</tr>
<tr>
<td>Limited Liability Company (WLL's)</td>
<td>Minimum 2 partners. Maximum 30 partners.</td>
<td>KWD 7,500 minimum capital.</td>
<td>Partners' liability is limited to the amount contributed.</td>
<td>About KWD 1,500.</td>
<td>Yes</td>
</tr>
<tr>
<td>General Partnership</td>
<td>Minimum 2 partners.</td>
<td>No minimum capital.</td>
<td>Partners' liability is limited to the amount contributed.</td>
<td>About KWD 500.</td>
<td>No</td>
</tr>
<tr>
<td>Limited Partnership</td>
<td>Minimum 2 partners Two types of partners: sleeping partners and active partners.</td>
<td>No minimum capital.</td>
<td>Liability of active partners is unlimited. The liability of sleeping partners is limited to the amount contributed.</td>
<td>About KWD 500.</td>
<td>No</td>
</tr>
</tbody>
</table>

(Source: FITA(The Federation for International Trade Association), 2007)
The right to carry on business

Any Kuwaiti or GCC national over 21 years of age may carry on commercial activities in Kuwait provided he or she is not affected by any personal restrictions (such as bankruptcy) or by the nature of the transactions undertaken (such as dealing in contraband goods).

However, non-GCC nationals may not, as a general rule (Article 23(1) of the Commercial Code), carry on a trade in Kuwait unless they have one or more Kuwaiti partners and the capital owned by the Kuwaiti partner(s) in the joint business is not less than 51 percent of the total capital (60 percent in case of financial institutions such as banks, investment houses and insurance companies).

And a foreign company (including a partnership) may not set up a branch in Kuwait and may not perform any business activities in the country except through a Kuwaiti agent (part 24 of the Commercial Code). In addition, foreign individuals and corporations may not acquire commercial licenses in their own name, nor may they own real estate in Kuwait.

In the past few years, the above general rules have been modified to enable Kuwait to join the WTO (World Trade Organization). Foreigners (non-GCC nationals) may now establish businesses in the Free Trade Zone, in Shuwaikh, and retain 100 percent ownership of their businesses. The new FDI (foreign direct investment) law allows wholly foreign owned businesses to be established in Kuwait. And foreigners may invest directly on the Kuwait Stock Exchange, rather than being restricted to mutual funds as in the past.

Recent Business Laws

The three main laws regulating business in Kuwait, which have been amended several times since they were first issued are:

- The Civil Code (Law 67 of 1980)
- The Commercial Code (Law 68 of 1980)
- The Commercial Companies Law (Law 15 of 1960)

The rules of commerce in Kuwait are, in general, similar to West European practice.

Intellectual property rights protection

The protection of intellectual property rights in Kuwait is quite good in theory. Trademarks are well protected provided they have been registered. A law protecting intellectual property, such as the rights of publishing or reproducing literary, artistic, musical, computer software and other intellectual works, issued on the last day of 1999 is comprehensive. However, pirated copies of software, and audio and visual CDs and cassettes, are freely available on the streets in Kuwait and in many shops, notably in Hawally area. However, in recent years, especially after the implementation of WTO regime in 2005, Kuwait government clamping down on violations of intellectual property rights.
The state of Kuwait is a signatory to the World Trade Organization (WTO) agreement on the protection of intellectual property rights (TRIPIS) and is a party to the Arab Convention for Copyright Protection. It is affiliated to the World Intellectual Property Organization.

A trademark is anything that takes a distinctive shape and that is used or intended to be used to distinguish products for the purpose of indicating that they belong to the owner of the mark because he or she, makes them, selects them, trades in them or displays them for sale. Articles 61 to 85 of the Commercial Code provide for the registration and protection of trademarks.

A patent is the sole right to the proceeds of an invention, including the right to exclude others from making, using or selling an invented product during specified time. Law 64 of 1999 is designed to provide comprehensive protection to the authors of all forms of intellectual works in letters, arts, and the sciences including:

- Literary works (written and oral)
- Theoretical shows
- Musical works (with or without lyrics)
- Choreographic works
- Motion pictures
- Audio, video, radio and TV works
- Artistic works (paintings, sculptures, carvings and architectural and decorative works)
- Photographs
- Works of applied art (craft and industrial designs);
- Illustrations and maps
- Designs and models
- Computer works (software and databases)
- Translated works

Protection, however, is not limited to the above types of work and the legislation has been framed so that new types of works will be protected. The title to a work is also protected provided this has been created and it is not a common expression.

Extent of modernization of the society

Kuwait's democracy has experienced ups and downs, and more are probably in the offing as the country takes up such problems as women and naturalized citizens (along with their descendants), claim their political rights as well as allowing political parties to organize. It's critical that democracy not fragment Kuwaiti society along tribal, sectarian, and religious lines. Intellectuals and opinion leaders in Kuwait commonly object not to democracy but to the way that it is practiced in their country. Khalifa al-Luqayan, a leading Kuwaiti poet and writer, recently expressed this sentiment:

Democracy, as we understand it, is a way of citizen participation in the affairs of society. But unfortunately it brings us inexcusable behavior by awakening tribal and sectarian
fanaticism. What we saw in the 1992 elections for the Assembly, municipal council, and cooperatives--voting for tribal and sectarian reasons--will fragment our society rather than unite it.¹

Conditions in Kuwait have reached near maturity, yet it should always be remembered that such a process is by nature slow, and that maturation depends, internally, on the development of social and economic factors, and externally, on a more peaceful coexistence in the region, with progressive economic and political development. If Kuwait can take these steps forward, it may have an immense impact not just on Kuwait itself but also on developments in the entire region. Only time will tell.

(Source : http://www.arabianbusiness.com/520573-kuwaitys-youth-struggle-to-find-work.html)

Social and Cultural Trends

Islamic Culture

Arab culture and traditions, anchored by Islam, are the secure foundations upon which the modern State of Kuwait is built. The metamorphosis in lifestyle brought about by the discovery of oil did not efface the identity of the people of Kuwait. The ravages brought by the Iraqi aggression also did not stifle the spirit of the Kuwaitis as they rebuilt their country in record time.

The State of Kuwait has always paid special attention to the preservation of its culture and heritage by maintaining monuments and preserving art facts and historical documents. The National Museum is one of the 50 locations where these are housed. The destruction caused by the Iraqi troops created a heightened awareness among the people about the need to preserve and resurrect the arts and crafts of Kuwait. The new architecture of the city, which combines modern design with traditional, reflects this awareness.

Kuwait has a large variety of customs and traditions, and this gives rise to a colourful and extensive culture, reflected in the Diwaniya, the Bedouin traditions and Al Sadu weaving. The people of Kuwait also have special love for the arts, be it literature, theatre, music, dance, films or contemporary art. The National Council of Culture, Arts and Literature (NCCAL); The Free Art Studio and The Kuwaiti Society of Formative Artists are promoting the visual arts in Kuwait.

Most aspects of the business culture are conservative. Dress should be formal and conservative (particularly for women) and greetings should be between same sexes only. There is often accompanying small talk when meeting someone for the first time. Be sure to adhere to local customs. Affection between opposite sexes is not shown in public. Most business is conducted in English, although using a few words of Arabic (particularly for titles) will be appreciated. It can be difficult to conduct business in
Kuwait as the working week runs from Sunday to Thursday. Business hours vary, but are usually from 7am to 1pm and 4pm to 10pm. Government offices and banks are usually open from 8am to 2pm.

Importance of working with Kuwaiti partners

In order to do business in Kuwait, an expatriate entrepreneur or company needs an agent, sponsor or equity partner, unless he is investing under the direct foreign investment rules. Choosing a Kuwaiti associate wisely is one of the critical factors for success.

Because locally there is no such thing as a pure business relationship, the reliability and depth of the personal relationship are very important when choosing a Kuwaiti associate. Other factors that must be considered are the associate’s financial resources, his overall business experience, the extent of his current operations, and his experience in the proposed products or services. Practical issues such as the availability of the licenses needed to carry on the particular business and how to control over day-to-day management and business assets is to be shared should never be overlooked.

One of the most important criteria in choosing a Kuwaiti associate is his standing in the local business community and in government circles. If a foreign firm’s products or services are directed to a particular ministry or business area then a potential associate’s personal connections with the main decision-makers in that field require thorough evaluation.

However, an overseas businessman will soon discover that many individuals and firms habitually present themselves as having more influence than they do in fact have in a particular area and caution needs to be exercised in evaluating offers of sponsorship. A foreigner is strongly advised to refrain from signing with an agent until he has made several trips to the country, knows some of the main decision-makers in the areas in which he is interested, and is fully satisfied as to the suitability of a particular associate.

Large and growing youth market

Kuwait's Census Bureau has called on authorities to establish training programmes and incentives to start small businesses in order to stem rising youth unemployment. Hessa Al-Janahi, acting director of the bureau, also suggested curbs on the number of foreign workers entering Kuwait. The latest unemployment data shows that 19,250 Kuwaitis are unemployed; 5.5% of the national work force. Over 80% of those unemployed are women. Only 16% are men.

Kuwait's rising youth population is struggling to find work. Half of the total unemployed are aged under 30, and three-quarters are under 40. Education appeared to be key to cutting long term jobless rates, Al-Janahi said. Over half of the unemployed in Kuwait do not hold "below high school credentials," according to the Census Bureau. 12.8% hold no formal education.

(Source: Arabian business.com, May 28, 2008)
**Technological Trends**

**Telecom and IT**

Kuwait's mobile telecommunication segment is regarded as one of the strongest and most advanced in the world. Current penetration rate rests at 90%, but is expected to reach 100% by 2008. The country's two operators, Zain and Wataniya, continually roll out advancements of their products and services, such as 3.5G and 3.8G respectively, with the goal of providing greater download speeds and the use of TV and online services, as well as increasing the ease of user accessibility. Both operators have also become involved in a rampant spate of merger and acquisition activity in recent years. Such activity is allowing both companies to expand their operations abroad – Zain now has operations in 20 countries and close to 30m subscribers, with further growth expected in the years to come. A third operator, however, is expected to enter the market in the coming months, although bids have yet to be formally tendered. The introduction of a third operator will increase competition, resulting in a price reduction for mobile users, which will be much-welcomed by consumers, who currently pay some of the highest rates in the region. The fixed-line segment, however, is not doing so well, having long been superseded by the mobile segment. The Ministry of Communications' (MoC) monopoly on fixed lines is at the root of the problem, with international call rates the highest among Gulf countries, thus discouraging the use of landlines. Many now argue the MoC should relinquish its control on regulatory matters to an independent telecommunications regulatory authority or privatise its landlines, as taking on the role of both regulator and operator impedes further expansion. Despite an impressive IT history that includes the distinction of being the first country in the Middle East to have widespread internet access, Kuwait's prominence among its Gulf Cooperation Council neighbours in terms of IT has slightly fallen over the past five years. Liberal import laws for IT hardware and a relatively high GDP per capita, some $29,000 per citizen, will serve to bolster desire for the latest technologies, with 15% to 30% growth expected for the PC market in 2008. While the hardware segment will continue to grow, software piracy in Kuwait remains one of the biggest hindrances to overall growth in the IT sector, with the rate of piracy in 2006 resting at 64%, down from the previous year, yet still the highest in the region. Broadband penetration, at only 28% in 2006, is also facing problems. A lack of infrastructure, particularly in newly developed areas, along with high prices for internet services, have been the key inhibiting factor to further penetration. New initiatives and reforms are currently being implemented in a joint effort by the private sector and the government to increase penetration, but these efforts may prove irrelevant, as mobile operators are now offering faster-than-ADSL internet speeds to mobile subscribers. Meanwhile, new projects and organisations are currently being set up with the hope of diversifying Kuwait's economy through the widespread transfer of IT knowledge and the creation of more IT jobs, thus spurring the development of IT software and services.

**Development of IT**
The State of Kuwait has a long history of active use of physical development planning. It is now more than forty years since the first Kuwait Master Plan, 1952 laid down the essential principles that have been followed ever since. These principles and a succession of master plans and reviews have helped guide the development of Kuwait from a small mud brick town of 75,000 persons to today's contemporary metropolis of 3 million persons.

Before the review of the Kuwait Master Plan in 1989 - 90, the need to establish a systematic database using computer technology was recognized by Kuwait Municipality. At that time a utility and data management project (KUDAMS - Kuwait Utility and data Management System) was nearing completion. This had been conceived as a large-scale utility management project derived from field survey and aerial photography, implemented on Intergraph equipment basically as a CAD-system for access to public utility data.

Disruption caused by the Iraqi occupation and its aftermath has been a prime factor in aborting many projects. Among them the Kuwait Master Plan Review and the KUDAMS project.

In post-liberation Kuwait Municipality recognized that it was no longer sensible to carry out a further review of the Master Plan. Instead a new comprehensive development planning project was required in view of the transformation in Kuwait, principally in terms of demographic composition and economic structures. Following a short initial assessment study in 1992, to identify and prepare data needed for the new Master Plan, Kuwait Municipality formed a team associated with a local consultants (SSH- Salem Al-Marzouk & Sabah Abi-Hanna) to prepare a wholly new Third Kuwait Master Plan (3KMP). This furnished an opportunity to embody GIS technology as an integral part of the new master plan. In recent years, Kuwait government is placing major emphasis on developing and implementing e-government development programs.

**Internet Access and use**

The .kw is managed by the Ministry of Communications, which entered into a contract with GulfNet Kuwait Computer Company (now Gulfnet International Company) on 12 June 1994 to offer Internet connections on an exclusive basis to the public and government agencies for two years, with the contract being renewable for additional two-year terms. The contract remains in force today, although, in early 1996, the Ministry announced that a second ISP was to be licensed, in order to “improve the Internet service” and lower prices; no second license has been forthcoming.

The service is marketed as the Kuwait Electronics Messaging Services (KEMS) (www.moc.kw). KEMS is connected to the Internet in the United States via a satellite circuit leased from SprintLink, operating originally with one Class C network (196.1.69) registered with the InterNIC and now with a complete Class B network (168.187).
Services offered include dial-up shell (UNIX) and SLIP/PPP accounts, and leased lines. At the time that it was granted the ISP contract, the Ministry of Communications had already registered and connected more than 200 Internet hosts, principally at government agencies. An affiliated company, Gulfnet Kuwait (www.kuwait.net), offers identical services, although most government agencies and public companies are connected to the Internet via KEMS. Gulfnet has been assigned 64 Class C blocks of IP numbers (194.54.192-194.54.255) by UUNet Gulf (Dubai), and is connected to a UUNet Technologies Internet port in the United States by a satellite link.

Kuwait hosts the most Internet sites in the Persian Gulf region, almost half of the total. A large number of domains are registered with the InterNIC, however, rather than the Ministry of Communications. Some of these registrations pre-date the existence of the Internet in Kuwait, but many companies today continue to prefer a domain name without a country identifier. Of passing note, the Kuwait Ministry of Information has its own Web site (www.info-kuwait.org), which includes among the ministry’s responsibilities “censorship,” but the domain is not only registered with the InterNIC, but the server is located in North Carolina. At least several Kuwaiti companies also use servers located in the United States.

An Internet service provider, ZakSat, was established in Kuwait in 1997 and started offering public Internet access on 10 September 1997. The company uses satellite technology similar to Hughes Network System’s “PC Direct” Internet service, whereby subscriber-to-ISP transmissions are carried via leased or dial-up telephone lines but ISP-to-subscriber communications (i.e., the bulk of the data) are transmitted via satellite. ZakSat is connected to the Subic Bay Satellite Systems Inc. teleport in the Philippines, which is in turn connected to the Internet in the United States via a 7.7 Mbps satellite link which will be increased to 45 Mbps in the near future. The teleport’s network operations center also hosts proxy servers that locally cache frequently-requested Web pages. Subscriber communications are carried on AsiaSat 2 (100.5°E), with a footprint reaching from Egypt to New Zealand, wherein resides two-thirds of the earth’s population.

**Table 16: Mobile Research Rates in GCC – 2007**

<table>
<thead>
<tr>
<th>Country</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Oman</td>
<td>93</td>
</tr>
<tr>
<td>Saudi Arabia</td>
<td>101</td>
</tr>
<tr>
<td>Kuwait</td>
<td>111</td>
</tr>
<tr>
<td>Qatar</td>
<td>140</td>
</tr>
<tr>
<td>UAE</td>
<td>142</td>
</tr>
<tr>
<td>Bahrain</td>
<td>113</td>
</tr>
</tbody>
</table>

(Source : Global research)
Table 17: Share in Total Mobile Telecom Subscriber Base (2007)

<table>
<thead>
<tr>
<th>Subscriber</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Zain</td>
<td>56.8</td>
</tr>
<tr>
<td>Wataniya</td>
<td>43.2</td>
</tr>
</tbody>
</table>

(Source: Zain & Wataniya Telecom)

Conclusions

International business enterprises intending to enter Kuwait market should become familiar with the overall business environments and its emerging trends. This chapter attempts at providing an overview of the Kuwait business environmental dimensions. An understanding of the emerging Kuwait business environmental trends would enable international business to become aware of both opportunities and challenges of doing business in Kuwait. As the Kuwait economy is expected to be infused with increased oil revenues in the foreseeable future, it is logical to expect that many business opportunities will be available to international businesses. The globalization, privatization and liberalization forces shaping the Kuwait economy and society provide business opportunities. The opening up of business opportunities are enhanced by the following key characteristics of the Kuwait business environment:

1. Kuwait is highly import dependent country. The imports of various products and services from different parts of the world are continuously increasing facilitated by increased favorable balance of trade.

2. The capital intensive country with the national goal of diversifying the predominantly oil dependent economy is resulting in the initiation of a variety of industrial, infrastructural and tourism development projects. The technological and human needs of such projects offer many business opportunities to international businesses. Business opportunities will be especially attractive in the area of developing upstream petrochemical industries.

3. Participation of foreign enterprises in retailing field is progressively increasing. Given the Kuwaiti consumer preferences for quality foreign products and services many well established US and Western European franchises.

4. Recent legislation by Kuwait government aimed at attracting foreign direct investment will also facilitate entry of foreign enterprises.

5. Many leading trading companies in Kuwait have long experience in dealing with foreign businesses which should help the new entrants to function effectively in the Kuwait market.

6. One of the national goals of Kuwait governments is to develop the country to develop into a regional business hub which provides foreign businesses a regional alternative to Dubai when the costs of operating business operations are escalating..

The international businesses should become aware of some of the challenges of operating businesses in Kuwait. The following are some of such challenges:
1. First and foremost, effective business functioning would require a Kuwaiti partner. Both legal and practical aspects of doing business in Kuwait would require finding a suitable Kuwaiti partner.

2. Given the rising unemployment problem with Kuwaiti population, Kuwait government follows an active Kuwaitization policy. This policy requires the private sector businesses to employ certain proportion of their human resource requirements with Kuwaitis. Given the general paucity of qualified and experienced Kuwaitis, the foreign businesses may have to develop programs to recruit, train and employ Kuwaitis.

3. For bulk of the technically qualified and experienced human resource needs, foreign companies have to depend on expatriates from other Arab and Asian countries. This situation poses two types of challenges. First, given the global demand exceeding the supply for such skilled personnel, it becomes progressively more difficult to recruit and retain the qualified expatriate skilled employees. Second, the need to assemble the human resources from diverse cultures results in facing the problems of effectively managing multi-cultural work forces.

4. Adapting to cultural values, traditions and norms of Islamic Arab society becomes imperative when doing business in Kuwait. Although Kuwait is more modernized society by Arab regional standards, the core cultural aspects of Kuwait confirm to Islamic Arab cultural environment.

5. Finally, it is important to emphasize that competitiveness in Kuwait is progressively becoming more intense. For many imported consumer goods and services, the intensity of competition is ever increasing as Kuwait imports from many countries. In recent years, imports from emerging Asian countries have vastly increased the intensity of competition. In manufacturing sector in the past several companies enjoyed monopoly conditions since the government policy was not to license additional manufacturing companies, if some company already exists in that product field. However, this policy seems to have been relaxed. Hence, one can expect increasing competition in non-oil manufacturing industries.

Finally, It is no doubt that major challenges facing the Kuwait economy as well as other GCC members in the future would mainly be economic diversification, employment generation and increasing inflation. This is especially in the current scenarios of tumbling dollar as well as high population growth rates and skewness towards young population.

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Moldovan Self-Directed International Transferees: The Syndrome of Home-Host Country Foreignness

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Abstract: This paper undertakes an exploratory multi-case study of five Moldovan women on self-initiated ongoing foreign work arrangements in Italy. Using the results of human capital migration research, we argue that our sample can be better described in terms of ‘brain drain’, ‘brain waste’ and ‘optimal brain drain’, as opposed to ‘brain circulation’ and ‘brain exchange’, which are the specific characteristics of nationals from advanced economies. Based on the analysis of our case material, we identify four stages through which self-initiated foreign experiences evolve and several types of workers according to their urgency to migrate, their lack of resistance to the shock of reality and their attitudes towards self-accomplishment. We further explain the ‘home-host country foreignness’ syndrome which prevails in our sample and determine the differentiating features between self-directed and expatriated journeys.

Key words: brain waste, exploratory multi-case study, Moldovan migrant workers, self-initiated foreign experiences

Introduction

International human resource management literature is dominated by continuously growing body of research focusing on expatriation within multinational companies. The traditional and still most common type of international employee is an expatriate who is transferred to a subsidiary outside his home country for a limited period of time to achieve some company-related objectives. More recently, researchers have shifted slightly their focus towards the exploration of a reverse phenomenon, that of inpatriation (Harvey, Novicevic, Buckley & Fung, 2005; Kedia and Mukherji, 1999). Inpatriates are host or third country nationals relocated to the home organisation on permanent or semi-permanent basis (Harvey et Buckley, 1997). The researchers’ interest in these particular categories of international workers is mainly explained by their easiness of identification and accessibility. Since the initiation of the foreign assignment for both expatriate and inpatriate managers comes from the employer, these types of employees can be easily identified and their participation in surveys can be facilitated with the cooperation of home-country management.
In reality, however, foreign work-related experiences are much more diversified and cannot be reduced to those two types. The corporate expatriation and, to a lesser extent, inpatriation start now to be reasonably well understood and there is a clear need to move forward and study other largely under-explored groups of international employees. Recent evolutions in labour markets and shifts in technology coupled with the recognition that career management becomes increasingly the responsibility of individuals rather than organisations, allowed for the emergence of an alternative model of international work, that of self-initiated foreign experience. Individuals who are travelling abroad for a long-term period and find their jobs by themselves is nowadays a very common phenomenon, particularly in the European context, yet we know little about those sojourners, their particular motivations to leave their home and the challenges they experience in a foreign country.

According to Inkson, Arthur, Pringle & Barry (1997), literature on self-initiated international assignments was nonexistent in the mid-90s. In a discussion of important unresolved research issues, Bonache, Brewster & Suutari (2001) specifically call for more empirical work on such categories of international workers as expatriates working for international joint-ventures or international organizations like the United Nations and the European Union, and on self-directed foreign assignees. Vance (2002) also urges us to “advance the development of a much neglected line of career research related to self-selected or self-initiated expatriation”. Our analysis of existing studies in this field reveals that the emerging stream of research tends to concentrate on those individuals who are moving from developed countries and looking for a job in other developed (and rarely developing) economies. This is the case of research conducted by Inkson et al. (1997), who concentrated on a sample of young New Zealanders working overseas, and by Suutari and Brewster (2000), who collected data on university-level educated Finnish employees on self-initiated foreign assignments based in other European Union countries. Little research has been conducted so far inquiring about those employees who are nationals of developing or transitional economies and who decide to look for work opportunities in developed countries. We suppose that the individual motivations and challenges the developing economies’ workers face differ from what advanced countries’ nationals experience while working abroad and, therefore, the existing although very limited evidence on the latter employee type could not apply to the former.

Our investigation is motivated by an ongoing discussion whether people from former Union of Soviet and Socialist Republics (USSR) (excluding Estonia, Latvia and Lithuania which on May 1, 2004 became members of the European Union) undertaking self-initiated foreign experiences are returning home or whether those nations are experiencing a brain drain. This type of brain migration became a widespread occurrence in the large majority of countries of what is now known under the name of Commonwealth of Independent states (constituted by all of the former republics of the USSR except the three Baltic states), organization that was conceived as the successor to the USSR in its role of coordinating the foreign and economic policies of its member nations. This trend is particularly striking in Moldova, a small Eastern European transitional economy facing mass emigration. Confronted with political instability, collapsing incomes and rapidly rising unemployment, highly trained people began
emigrating from Moldova on a large scale in the first half of the 1990s and continue to do so nowadays. World Bank (2005) has estimated that over 30% of Moldovan active population is working abroad, most illegally. Since this emigration is the dominant trait of the country in the new century, having important economic, political and social drawbacks, the future development of Moldova is seriously hampered.

On the nations’ level, there is an urgent need to design viable policies and procedures in order to build upon these and create an effective system of managing particularly those more vulnerable migrant workers who enter in less formalized labour market settings abroad. Yet remarkably little data and knowledge exist on these workers, their extant social and economic situation in the destination country, their working and housing conditions and other complexities of their daily life in an alien environment. Our research is thus based on the premise that unless appropriate information is collected and sufficient knowledge base is developed, improper policies will be implemented that would not go towards satisfying migrant employees’ needs.

In this paper we undertake an exploratory multi-case study of five Moldovan women on self-directed foreign work experiences, question that remains unaddressed in the scientific literature. We build on the previous work of Inkson et al. (1997) and Suutari and Brewster (2000) by being one of the first studies to provide the empirical evidence about Moldovan citizens who made their own arrangements to find a job in Italy. Based on Lowell’s (2003) brain mobility classification, we argue that our sample of self-initiated international transferees can be better described in terms of ‘brain drain’, ‘brain waste’ and ‘optimal brain drain’ as opposed to the ‘brain circulation’ and ‘brain exchange’, which are the distinguishing features of those developed economies’ nationals who are making their own way to get work abroad. The expected contribution of our study is twofold. First, our results aim to contribute to the building of a body of literature in our field of interest, by detecting four stages though which self-directed foreign experiences evolves over time and by identifying two new subgroups among the larger self-initiated international transferees group. Second, from the States’ perspective, our research findings help to generate knowledge that is required for fostering better policies and institutions to protect the rights and enhance security of those types of workers.

The remainder of this paper is organized as follows. In the next section we make a brief literature review, providing an overview of empirical findings in our field of interest and integrating the self-initiated foreign experiences with broader body of research on human capital migration. Then we justify our interest in the study of Moldova’s case, highlighting the distinctive features of this small transitional economy. In the section on methodology, we describe our data collection sources and explain the method used to perform the case analyses. We continue by presenting an overview of the individual life stories of Moldovan women who participated in our investigation. The key findings are illustrated in a model and discussed in details in light of extant evidence on brain mobility. Finally, the concluding remarks underline our study contributions and its implications for future research.
Literature Review

Empirical evidence on self-initiated foreign experiences

Literature on individually-initiated foreign experiences is very limited and is mainly conducted using samples of young nationals of New Zealand or Australia heading overseas for a long-lasting period of tourism, work or study. Since the only means for those islanders to get a job abroad is to cross the sea, the first term ever used to design this type of work was that of ‘oversea experience’. Inkson et al. (1997) broke new ground in the field of international human resource management, by being the first researchers to address explicitly the issue of overseas experiences. Their article paved the way to subsequent and impressive empirical work on this category of international employees in the New Zealand context. Scholars from both the University of Auckland and the Auckland University of Technology have literally monopolised the scientific journals having a global focus, publishing their findings about the overseas transferees and their personal experience. Among most notable research on this issue are studies by Glass and Choy (2001), Bell (2002), Inkson and Myers (2003), Myers and Inkson (2003), Inkson et al. (2004), Carr, Inkson & Thorn (2005), and Myers and Pringle (2005).

The focal point of the pioneering study conducted by Inkson et al. (1997) is in contrasting the overseas experiences with more traditional expatriate international assignments. Four major distinguishing characteristics are thus identified: the source of initiative, goals for the foreign job, the source of funding, and career type. Without no doubt, the clear defining difference between the two groups is that the initiative for leaving the home country comes from the individual for the overseas experiences and not from the employer, as in the case of expatriates. The goals for the foreign job are rather diffuse and often unspecified personal development for the former, as opposed to the completion of specific organizational projects for the latter. People fund their overseas transfers themselves from personal savings and casual earnings, while for expatriate assignments the funding comes from company salary and expenses. Finally, the career type is defined as being boundaryless for those who independently seek a job abroad as those individuals may see it as their own responsibility to plan their careers, while the expatriates are rather following the patterns of an organisational career since in most cases they expect and are offered company supported career guidance.

All these differentiating features, particularly that related to the source of funding, reflect Inkson et al.’s (1997) view on another character of overseas experiences in that a job is usually not prearranged before departure. Their case material comes from a larger study of career development in New Zealand, enabling them to provide examples of both overseas experiences and their consequences for the individuals involved. The authors conducted in-depth interviews with 75 young and randomly chosen workforce members focusing on their career patterns in the decade 1985-95. Inkson et al. (1997) conclude their paper discussing the impacts of overseas experiences on national competitiveness. They posit that the traditions of the nation’s young people streaming overseas at the yearly stages of their careers can create a national reservoir of talent which may be used to good effect in an increasingly global and competitive economy.
To our knowledge, Suutari and Brewster (2000) are among the first non-New Zealanders to provide European evidence on this category of international employees. The main objective of their investigation is to expand the analysis made by Inkson et al. (1997) in two ways: by getting a sample of highly educated Finnish self-employed people and by including the representatives of different age categories and not just younger generations. Due to their European sample, Suutari and Brewster (2000) propose a change in terminology that will be extensively utilised in subsequent research on this employee category. Since in Europe people can work in other countries without crossing the sea, the authors propose the ‘self-initiated foreign experience’ as the European version of the ‘overseas experience’ term. Data on 448 Finnish graduate engineers working outside their home country were collected in 1997 through 1998 using the questionnaire methodology. Their results showed that a total of 147 people initiated their foreign assignment by themselves, while the remaining 301 were expatriates.

Similarly to Inkson et al. (1997), the authors identify some important differences between self-initiated foreign assignments and traditional expatriate forms along five distinctive variables: individual features, employer and task-related information, motives for the international tasks, repatriation and future careers and compensation package design. However, Suutari and Brewster (2000) make a significant contribution to the literature by suggesting that the group of employees who looked for a job abroad under their own initiative is not homogeneous and is itself composed of identifiable subgroups that have different characteristics. More specifically, six different subgroups are specified: young opportunists, job seekers, officials, localized professionals, international professionals and dual career couples.

Young opportunists are people below 30 years old who being in an early phase of their career and due to their relatively independent family situation head abroad for a prolonged period of travel and work. Job seekers are not satisfied with or have limited possibilities for career progression at home or were even unemployed before leaving their country. Officials work within international organizations such as European Union and the United Nations in order to get higher economic benefits and satisfy their personal interests in such kind of work. Individuals within localized professionals group have decided to stay abroad over a longer period of time with no clear plans to return to their home country because of their preferences for the foreign environment or strong personal relationships in host country. The best available indicator of membership of international professionals’ subgroup is the fact of having long experience of working in international operations at least on two occasions before the present job. At last, among the dual career couples subgroup, the major reason for seeking a job abroad is the expatriate assignment of the spouse.

Three years later, New Zealand researchers Inkson and Myers (2003) replied with another typology of six distinctive overseas experience forms, based on the priority attributed to work and employment. For cosmopolitans, returners and boundaryless careerists the career development plays a significant part in determining their travel abroad, while alternative tourists, stimulation seekers and Londoners develop little career related concerns. Cosmopolitans are defined as “go-anywhere” professionals who tend to
utilize a qualification in a specialist area to find work, as opposed to boundaryless careerists who are more flexible in their work and less constrained by professional boundaries. Returners have made more than one overseas experience, the first being short and more exploratory, while the second more career focused. Alternative tourists and stimulation seekers are both driven by the desire to travel and meet people in new places, but the time period is more limited and travel locations are less diversified for the former group than for the latter. Finally, Londoners like the security of being based in London and using it as a focus-point from which to find employment and travel.

More recently, investigations on self-directed international workers became more diversified, addressing several research questions that have been traditionally tested on expatriate samples. Such global careers’ issues as how receptivity to self-initiating international work opportunities originally develops (Tharenou, 2003), the role of individual agency and the perceived value of international experience for self-directed expatriation as an increasingly common career choice (Richardson and Mallon, 2005), gender influences on self-initiated foreign experiences (Myers and Pringle, 2005) and antecedents and consequences of underemployment among self-initiated expatriates (Lee, 2005) started to raise scholars’ interest. For instance, for a New Zealand sample of 26 women and 24 men on self-initiated foreign assignments, Myers and Pringle (2005) find that the propensity for women to seek out less risky and more secure environments afforded them greater career opportunities and resultant career capital. Then, Lee’s (2005) findings suggest that the lack of job autonomy, job suitability, job variety and fulfillment of psychological contract translate into reduced perception of underemployment, which, in turn, has negative effect on both job and career satisfaction leading to higher levels of alienation among 302 self-initiated expatriates working in Singapore. This paper differs from previous research in that it takes the host country perspective, highlighting the potential economic benefits it can receive from highly skilled foreign workforce.

**Integration with human capital migration (brain mobility) research**

So, what can be concluded from this brief literature review on self-initiated foreign experiences? In spite of the recent diversifying developments in this field of investigation, it seems that much of the existing research has concentrated on highlighting the heterogeneity of these experiences by building different typologies. Although the analysis of differentiating characteristics proposed in extant studies is very useful and convincing, we think that this analysis is not complete and there are still other types of self-initiated global workers to be identified and further explored. We argue in this paper that a more comprehensive understanding of the phenomenon of people going abroad on their own initiative might be produced if complemented by insights from human capital migration (also referred to as brain mobility) research. Since self-initiating foreign experiences and other types of high skilled mobility play significant role in nation’s economic development, it is important to be aware of the consequences they generate for both sending (home) and receiving (host) countries.
Recognizing that some level of skilled mobility is needed to participate in the global economy, Lowell (2003) identifies various outcomes that might result from this ‘brain globalisation’: ‘brain circulation’, ‘brain exchange’, ‘brain drain’, ‘brain gain’, ‘optimal brain drain’, ‘brain waste’ and ‘brain export’ (see Table 1). The concept of ‘brain circulation’ (Gaillard and Gaillard, 1998; Johnson and Regets, 1998) refers to the cycle of moving abroad to study, then taking a job there, and later returning home to take advantage of a good opportunity. It is believed that this form of mobility is positive as it increases knowledge transfer to the home country. According to the OECD (1997) report, a ‘brain exchange’ implies a two-way flow of expertise between a sending country and a receiving country. Yet, where the net flow is heavily in one direction, the term ‘brain gain’ or ‘brain drain’ is used. However, the ‘optimal brain drain’ theory finds some support for the notion that the possibility of emigration for higher wages induces more students in the sending country to pursue higher education. For some developing countries it may even pay off to keep these students abroad so that they continue to send important remittances back home, while for others keeping young intelligentsia outside might slow down the pace of reforms, reducing the likelihood of an institutional and political change. A ‘brain waste’ describes the waste of skills that occurs when highly skilled workers migrate into those forms of foreign employment which are not commensurate with their qualifications and experience. Finally, the ‘brain export’ refers to the strategy of educating and exporting highly skilled in order to stimulate a reverse flow of innovations and technological capacity due to the social and professional networks those people establish in the receiving country.

Addressing the general issue of brain migration among European Union nationals, Mahroum (2000) comes up with five distinct groups of highly-skilled globetrotters: managers and executives (accidental tourists), engineers and technicians (economy-class passengers), academics and scientists (pilgrims), entrepreneurs (explorers) and students (passengers). Although the author does not apply this typology specifically to the self-

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### TABLE 1

Types of brain mobility and their consequences

<table>
<thead>
<tr>
<th>Type</th>
<th>Description</th>
<th>Countries’ consequences</th>
<th>Sending</th>
<th>Receiving</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brain circulation</td>
<td>Significant rate of return migration brings valuable skills</td>
<td></td>
<td>Positive</td>
<td></td>
</tr>
<tr>
<td>Brain exchange</td>
<td>Loss of skilled locals is offset by an inflow of foreigners</td>
<td></td>
<td>Positive</td>
<td>Positive</td>
</tr>
<tr>
<td>Brain drain/brain gain</td>
<td>Significant losses of highly skilled and few offsetting economic feedbacks / significant gains in highly skilled</td>
<td></td>
<td>Negative</td>
<td>Positive</td>
</tr>
<tr>
<td>Optimal brain drain</td>
<td>Possible emigration can stimulate students in sending countries to pursue higher education</td>
<td></td>
<td>Positive/Negative</td>
<td>Positive</td>
</tr>
<tr>
<td>Brain waste</td>
<td>Highly trained workers are underemployed either in receiving or sending country</td>
<td></td>
<td>Negative</td>
<td>Negative</td>
</tr>
<tr>
<td>Brain export</td>
<td>A strategy to educate and export highly skilled in order to reap economic feedbacks</td>
<td></td>
<td>Positive</td>
<td></td>
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</table>

initiated foreign assignees, we believe it can usefully complete the picture we have drawn so far on this category of international workers. Managers are referred to as accidental tourists, because the decision for their mobility comes often unplanned and more as a result of business expansion of the employing firm than a personal decision. As such, this group describes the expatriation assignments but not the self-initiated ones. Engineers-technicians are like economy-class passengers, since they make their choices according to what they perceive as most rewarding for them. Academic-scientists are pilgrims who seem to be attracted to the nature of the work they are required to do and the conditions under which they have to conduct their work. The particular feature of these last two groups is that their self-initiated foreign jobs are usually prearranged before leaving home. Entrepreneurs are business-oriented explorers stimulated by a variety of immigration and fiscal policies who arrive in a new country with capital and ideas aiming at setting up certain business activities. Finally, students are perceived as passengers who are heading abroad to certain destinations, but the motives or the ultimate destiny of the various passengers at their destinations is unknown to most of us. Both entrepreneurs and students are self-initiated foreign employees who are likely to head overseas without having any pre-arranged work agreements.

Using the research on human capital migration we can now outline the major features that distinguish the existing typologies of self-initiated foreign experiences. As outlined in Table 2, scholars have tended to demonstrate the applicability of these typologies for Finns (Suutari and Brewster, 2000), New Zealanders (Inkson and Myers, 2003) and European Union nationals generally (Mahroum, 2000). Suutari and Brewster’s (2000) research was motivated by the commonly expressed worry in the Nordic countries about highly educated people leaving for work abroad, partly due to the high taxation levels in these countries. While these concerns animated the political debate in Finland during the period of 1997-1998 when the authors collected their data, recent evolutions in Finish legislation are likely to produce favourable feedbacks. The new law on dual citizenship passed on June 1, 2003, could make it easier for both foreigners and people of Finnish descent to work in Finland and could also catalyze the return of many expatriate Finns, stimulating the ‘brain circulation’ phenomenon. As of 2003, more than 25,000 Ingrians (Finns living within the former USSR) who fulfilled the heredity criteria had returned to Finland and tens of thousands of labour immigrants who have first secured job contracts with Finnish employers have been admitted (Tanner, 2004). ‘Brain exchange’ has also became a more common pattern with Finland’s entry into the European Union in 1995, which made it a better known and more accessible country for potential migrants. As suggested by Mahroum (2000), the freedom of movement within the European Union allows the sending countries to compensate their losses of skilled locals by an inflow of foreigners primarily from other member states. Further, it is worth noting that all individuals who participated in Inkson and Myers’ (2003) research returned home after their overseas experiences and enjoyed good career opportunities at home. Although the ‘brain circulation’ is the distinguishing feature of their sample, the concept of ‘brain exchange’ could also apply as New Zealand has an active labour immigration policy, prioritizing the entry of people whose skills are in demand.
To sum up, we believe that two major types of brain mobility describe the national samples used in prior research, namely the ‘brain circulation’ and ‘brain exchange’. According to the Table 1, both types are considered to have positive consequences not only for the sending but also for the receiving countries. Other types of brain mobility, that have rather negative impacts on the home country, remain unexplored. Moreover, the existing literature concentrates on the exploration of self-initiating foreign experiences undertaken by individuals from advanced countries exclusively. People from developing economies or transitional economies such as Moldova are also characterized in terms of high individually-initiated international mobility, but their differentiating patterns and specific motivations for looking for a foreign job on their own initiative are still not sufficiently well understood.

**TABLE 2**

<table>
<thead>
<tr>
<th>Authors</th>
<th>Types</th>
<th>Sample</th>
<th>Brain mobility</th>
<th>Consequences</th>
</tr>
</thead>
<tbody>
<tr>
<td>Suutari &amp; Brewster</td>
<td>- Young opportunists</td>
<td>Finns</td>
<td>Brain circulation, brain exchange</td>
<td>Positive for both home (sending) and host (receiving) countries</td>
</tr>
<tr>
<td>(2000)</td>
<td>- Job seekers</td>
<td>European</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mahroum (2000)</td>
<td>- Officials</td>
<td>nationals</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Inkson &amp; Myers</td>
<td>- Localized professionals</td>
<td>Union</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(2003)</td>
<td>- International professionals</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Dual career couples</td>
<td>New Zealanders</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Economy-class passengers</td>
<td></td>
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<tr>
<td></td>
<td>- Pilgrims</td>
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<td></td>
<td>- Explorers</td>
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<td></td>
<td>- Passengers</td>
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</tr>
<tr>
<td></td>
<td>- Cosmopolitans</td>
<td></td>
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<tr>
<td></td>
<td>- Returners</td>
<td></td>
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<td></td>
</tr>
<tr>
<td></td>
<td>- Boundaryless careerists</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Alternative tourists</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Stimulation seekers</td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td>- Londoners</td>
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Studying Moldovan self-employed international workers

Our exploratory study presents data about Moldovan citizens on self-initiated foreign work experiences. We argue that several distinguishing features of this country, such as ‘brain drain’, ‘brain waste’ and ‘optimal brain drain’, make it relevant for empirical investigation. From the beginning of its existence in 1991, the Republic of Moldova, this small state situated between Romania and Ukraine, has been in a deep economic crisis. The break-up of the USSR resulted in the loss of export markets for Moldova-made intermediary goods and agricultural products. Russia’s financial crisis in 1998 made matters worse in this closely linked to the Russian economy country. As a consequence, many Moldovans lost their savings as several banks went bankrupt, salaries collapsed and jobs disappeared. In 2005, average annual income per person officially amounted to only €425, just 1.8 percent of the EU average, which makes Moldova the poorest country in Europe (EIU ViewsWire, 2005).

The resulting wave of unemployment, estimated at over 25%, prompted many Moldovans to seek work opportunities in other states. According to the United Nations’ world migration report, in percentage terms Moldova is the planet’s second biggest exporter of labour migrants (UNO, 2006). In interviews with state officials and returned migrants,
the following countries are mentioned as the main destinations: Russia, Italy, Ukraine, Romania, Portugal, Spain, Greece, Turkey, and Israel. Although no official statistics exist due to the clandestine nature of these migration flows, nearly a quarter of the entire republic’s citizens are currently considered to be working abroad, either as seasonal employees or permanent migrants. Some 200,000 Russian speaking male Moldovans, members of large Ukrainian (8.3%), Russian (6%) and Bulgarian (2%) minorities are thought to be working in Russia, mainly in construction (Dujiisin, 2006). Another estimate puts the number of Moldovan women working in Italy as housekeepers, social assistants and waitresses at 200,000 (World Bank, 2005). Meanwhile, members of the 160,000-strong Gagauz minority (a Christian community in the southern part of the country whose language is related to Turkish and who enjoys substantial autonomy) are drawn predominantly towards Turkey.

Still others choose the Romanian option. Some historical reasons could explain this trend, as up to 1812 and between the two world wars Moldova was part of the great Romanian state. In 1991 there was an intense discussion about whether the two countries should seek reunification, but Moldovan political leaders at the time decided against forfeiting their newly gained independence. Special relations with Romania persisted and up until July 2000, Moldovans could travel to Romania with simple identity cards. Romania’s aspiration to become a member of the European Union has changed things: up to 2006 Moldovans were still free to travel with a possession of passport, while from January 1, 2007 (when Romania acquired the European Union membership) Moldovans are required to have a visa. Due to their close historical and cultural links, Moldovan citizens have also had the opportunity to acquire Romanian citizenship if they can demonstrate that their grandparents lived on Romanian soil before 1918. Since 2002, there was a big rush to obtain Romanian passport, as it allowed the visa-free travel to the European Union. As much as one third of the Romanian-speaking population of Moldova is now estimated to have dual citizenship.

Following more than a decade of migration, Moldova faces a significant loss being caused by a ‘brain drain’ effect. A specific feature of the country is that predominantly the highly educated people find it hard to escape poverty. Lots of higher education graduates are forced to go abroad to take up employment, generating significant shortages of professionals in some areas of Moldovan labour market. Yet the diplomas of professors, engineers, doctors, artists, scientists, who form a substantial part of Moldova’s expatriate community, are rarely recognised in other countries, resulting in migrants engaging in activities that are far below their qualification levels. Since neither Moldova nor the destination countries benefit from their professional knowledge skills, the ‘brain waste’ becomes another distinguishing trait of Moldovan mobility.

Moreover, all Moldovans working abroad do regularly send much of their hard-earned money back home, making the country to feature now as the second most remittance-dependent country in the world. While it is hard to quantify the scale of these transfers, total (official and unofficial) remittances are estimated by some to be as high as twice the official GDP (Dujiisin, 2006). Although these cash inflows have been instrumental in alleviating poverty for numerous families, analysts agree that the long-term development
of Moldova, with a largely agricultural economy, cannot be dependent upon them. Remittances cannot be taxed and are rarely invested, rather being spent on basic goods necessary for everyday survival and for the acquisition of apartments. The massive emigration of the younger and most entrepreneurial population of the country has also become a serious impediment to economic and political modernization. Therefore, this ‘optimal brain drain’ pattern in Moldova does not play any positive role in its future development and cannot secure its long-term stability.

Due to these unique features, the study of the Moldovan case could extend the existing typologies on self-initiated foreign experiences. Despite the significant social, economic and political consequences of the international self-employment among Moldovans, it is an unresearched phenomenon, except as one form of migration in the broad statistics of those leaving and entering the country. This may be due in part to Moldovan emigration being taken for granted as part of the national scene (in the words of one official, “in view of the dismal economic situation, emigration is better than revolution” [Jandl, 2003]), and in part to the slender resources available for social research in former USSR countries. The main objective of this paper is therefore to provide a descriptive account of self-initiated foreign experience, including the demographic characteristics and motivations of those who undertake it, the predisposing events that encourage it and those that influence its duration, and to consider the effects of this experience while it is still taking place on personal development.

Method

We explored these issues by means of five case studies of self-employed Moldovan women who headed to Italy to find employment on their own initiative. According to some sources, the most popular destination for Moldovan females is Italy, where 35% go (Dujisin, 2006) and, as such, Italy provides an ideal location for research among self-employed Moldovans. Thus, the empirical part of the study was conducted in the receiving country and not in the sending one. The use of the exploratory approach and multiple-case study methodology was considered appropriate given the absence of general information and empirical evidence on this particular group of international workers. A case study allows the comprehension of complex social phenomena, because it takes into consideration the contextual conditions that remain extremely pertinent to the phenomenon under investigation (Creswell, 2003). Since multiple-case studies’ outcomes are considered to be more compelling, our overall research is therefore conceived as being more robust than a single case study (Yin, 2003).

Our analysis draws upon three different sources of data: direct observations, in-depth interviews, and secondary data. Direct observations were made possible due to the creation, at the beginning of 2004, of the association “Together – Immigrants in Italy”, which is based in the province of Latina (situated in the southern part of Italy). From our personal contacts within this association, we gained access to people who actively participated in it and organized activities involving self-employed female Moldovans. During the summers of 2005 and 2006, when we travelled to the region for a two-month period, we had the opportunity to observe these people, participate in their meetings,
attend cultural events they organized and simply listen to their life stories. We could also discuss informally with one Italian language professor who was willing to share her experience as a co-founder of this association. We have then identified ten women and approached them asking to take part in an interview in a neutral setting. Two of them declined right away fearing potential consequences, even if we explained the ethical issues of our study and assured confidentiality. Although the other eight were willing to participate, five of them refused because of particular time constraints but were extremely cooperative in providing further contacts. We could finally recruit five Moldovan women who sought employment in Italy by themselves and who have been working in this country for at least one year. There were no other particular criteria to qualify for inclusion.

There are four limitations of this sample which need to be acknowledged. First, it is confined to women and therefore prevents us to conclude whether our findings apply to self-directed employment undertaken by men. Second, although we did not target our study at purposefully selected types of migrant workers, our sample represents only service sector employees including domestics and irregular workers in the informal economy and services. Third, it focuses on Moldovans who are still working abroad, but does not include those who have previously been on self-initiated international work and have already returned to their home country. Fourth, the sample comprises the workers undertaking their foreign experiences in the same cultural context (Italy), but does not permit assuming whether these experiences are similar in other national settings or vary according to the country of destination.

All the interviews were carried out by both authors and typically lasted 90 minutes, although two of them ran as long as two and a half hours. A qualitative semi-structured interview guide (Fontana and Frey, 2000) was developed in such a way that would allow us capturing all the complexities of life of migrant workers in a foreign environment. It included three main sections: before departure, during the foreign experience, and plans for future. The first section covered the participants’ age, education, marital status, the motivation for going abroad and choosing Italy, and the goals settled for this experience, including an estimate of the time expected to be away. The second section enabled the respondents to tell their stories in their own words, in all their richness and complexity. They were asked to talk about their employment history, relationships made, the particular difficulties they encountered, the changes occurred in their perception and behaviour throughout the time and the personal learning taken from their experience so far. Given that participants were contacted within their country of destination, making them to reflect upon their self-initiated foreign experience while it is still taking place, this section of the guide was the most important and largest in size. The last section referred to participants’ perceptions regarding their relationships with those left at home, their feelings while travelling back to Moldova, their intention to return permanently to their home country and, more generally, their plans for the future.

The order of topics included in the interview guide was flexible, enabling respondents to frame their individual stories in their own way, while ensuring coverage of a complete range of topics. Each author independently analyzed the responses to each question, with
a clear focus on subjective perceptions and feelings of the people involved in those self-directed foreign experiences. After this in-depth analysis and interpretation of actual episodes in migrant workers’ lives abroad, major themes were drawn out by content analysis and coded into prevalent patterns (Huberman and Miles, 2002). Finally, the results of each author were compared and synthesized.

To enrich our analysis, some secondary sources have also been consulted such as World Bank country reports, publications of the Migration Policy Institute, statistics on apprehensions and regularisation, issuance of work and residence permits, information on labour migration streams published in both Italian and Moldovan press, and articles written by members of “Together” association themselves and published in Italian newspapers. In the following part of this paper we briefly present the stories of five Moldovan women (Natalya, Angela, Galina, Maria, Aliona) who participated in our exploratory research. Their real names are not disclosed for confidentiality reasons.

Results

Natalya: is a 31-year-old business graduate who left the country in 2000. Prior to heading abroad she worked in a local insurance company based in Chisinau (the capital city of Moldova). Her monthly salary of €35 hardly allowed her to live decently. Among several possible destinations she had chosen Italy because her older sister was already working there for more than two years. The decision to look for a job abroad was a rational one and resulted from a serious reflection about her future personal and professional opportunities at home. “When I left, I was not married and had no boyfriend. My work was becoming monotonous and I saw no particular opportunity for my career development. My sister and lots of my university colleagues have already been working for several years in Italy. My personal and professional life became void and I had no reason to continue staying in Moldova. I had to go away. I felt the need to try something else, something that would change my life for ever”. To make her adjustment to the Italian culture smoother, she took Italian language lessons during one year. Although she was not going to a prearranged work, her sister’s presence coupled with her knowledge of Italian helped her to pass through the initial difficulties. “The first year was very difficult from psychological point of view. Several times I wanted to abandon everything and go back home. But the time is the best medicine. At the beginning I was working as a domestic, but latter on found a job as an insurance agent. Although I don’t have the same level of responsibilities I had in Moldova, I am reasonably well paid and I don’t have to do the unpleasant domestic work I did before. I have also made a lot of friends and married an Italian man. Although I am happy now, I still want to learn lots of new things and reach new heights”. Over the time, Italy became her second home and she does not seem to be willing to return to her home country. She is used to travel back to Moldova once per year, but she does not feel there completely comfortable anymore. “The country has changed, so did I. What was so obvious for me when I lived in Moldova became completely unbearable. For instance, I can easily get crazy when there is no hot water or electricity. People who knew me before I left keep saying that I am not the same anymore. I feel confused as I don’t really know where my real home is”.

Angela: arrived in Italy in the summer of 1999. Some psychological and economic reasons motivated this 33-year-old Moldovan to leave her home. “Recently divorced, I had nowhere to go but to my parents’ house. I wanted to start a new life, purchase my own apartment, leave behind my sentimental problems and demonstrate myself that I can be financially independent. The miserable salary I was getting working as a psychologist in a high school could definitively not make my ‘independence-dream’ come true”. She has heard a lot about Italy – gorgeous country, impressive history, welcoming and nice people, one of the most beautiful languages in the world. Her beginnings in this country were very difficult: she felt lonely and scared as she had no acquaintances in the region and did not how the things worked. “Some days after my arrival, I was employed to take care of a 95-year-old woman. The family I worked for treated me quite well, but as a university graduate, I could not accept doing that kind of job. I became aware of my social status: I was nothing and had no rights”. Her initial intentions were to work in Italy for a maximum of two years and with the money earned start a new business in Moldova. However, since the political and economic situation in her home country was not getting better and with a newly born child, she decided to stay. “I said I would do everything to give my daughter a better future and to make her be proud of me”. Angela started to study, got a new diploma in accounting, accepted to work for free in a construction company to get some professional experience and now is struggling to get a job in this field. “I am pleased I came here, as all my sacrifices are starting to yield positive results. I met nice people here who are willing to help, learned a lot and became mature. But I am still trying to find myself in this new society and if I continue working as hard as I do, I am sure I will find it one day. My heart is still Moldovan and I don’t really think this would ever change. Both my past and my present made of me a stronger person and permitted to grow”.

Galina: was a physical trainer at the State University of Moldova when she decided to do something in order to improve the financial situation of her family. This 50-year-old wife, mother of two children, was encouraged to follow the example of several relatives who became wealthier working abroad. “Although two of my cousins were already working in Italy and offered to stay at their place, I was really scared to go alone and seek for employment in a foreign country. Fortunately, a friend of mine also needed money and as she was literally in love with Italy we decided to go there together”. One week after her arrival in spring of 1999, she has already started her first job as a house cleaner. She leaned to manage her frustration of being underemployed by orienting all her energy towards the realization of her unique goal: earning more money and giving her children a nicer future. “I feel so guilty for all that time I did not stay with my sons, but know they understand and pardon me. Since I am working in Italy, I could send them enough money for living and paying their studies at the University. I have also purchased one apartment for each of them”. Galina qualifies her life in Italy as being emotionally difficult, but financially rewarding. “It is difficult to become a full member of the Italian society: the culture and the ways of thinking and doing are very different from what I was used in my country. The professional experience I acquired in Moldova is not recognized here, so I can not give the best of myself. Whatever I will do, the locals will always look at me as at their servant. There is nothing to do about that”. However, she admits not having any plans to return home, at least not in the near future. “When you got used to being paid 20
or even 30 times more than what you were getting in Moldova, you think twice before taking such kind of decision. I am happy to travel to Moldova, but, strangely enough, few days after my arrival, I start feeling the need to go back to Italy. As long as I can work here and help my children to build a better life, I will stay. I miss my family and they are in my mind all the day long, but for now I am more useful staying here”.

Maria: is a 58-year-old woman with incredible entrepreneurial spirit. Prior to the break-up of USSR she worked as actress at the National Theatre of Chisinau. However, during the 90s when Moldova has started to make its way towards the market economy, she has rapidly understood that she needed to start her own business in order to maintain her living standards. She has tried almost everything: shoes shop, bread factory, food deposit, small supermarket, etc. Inflation, high interests rates, lack of serious workforce have all contributed to the decline so that in 1998 she had to close her businesses, reimburse the loans and wait for better times. “During the 1999 I divorced, stayed closed in my flat and kept crying. Then, one day I woke up and decided to do something. What? As I had no forces to start from zero in Moldova once again, why not in Italy? Italy was the unrealized dream of my life, the country of all possibilities: La Scala, Rome, yachts, shops, the mirage of ‘made in Italy’ – the most beautiful things come from Italy! During the best years of my life, I was used to spend all my holidays in Italy, so that I could learn the language. Hence, I decided to go there”. One week later she was already in Italy. After her arrival in 2000, her mirage has suddenly disappeared and she started to face the reality. “Once there as a foreign worker and not as a tourist, you see the country and its people through other lenses. Bureaucracy, precarious health, high rents, high costs of living, illegal work, sometimes xenophobia, loneliness, frustration, etc. - all became part of my daily life. In Moldova - member of high society, here - nobody! It is difficult to accept and be accepted”. Maria has, however, decided to fight for what she calls “her place under the sun”, meaning to work and involve in all kinds of activities that would allow her to take advantage of all the opportunities Italy offers to learn and become better. She did all kinds of jobs, starting as a cleaner and a social assistant and continuing as a seller of coffee Lavazza, a real estate agent, and a corporate archivist, she passed the ‘Italian as a second language’ examination at the University of Siena, she is actively involved in the association, organizes different cultural events, writes newspaper articles, reads a lot, listens to music, goes to the theatre, makes paintings and handcrafted jewelleries. “Here I rely only on myself. What I learned is that everything is possible if you really want it”. But what about her relationships with her home country and her plans to return? How does she see her future in general? “When I go back to Moldova to visit my son and my friends, I feel at home only during the first days. For Moldovans I am Italian, for Italians I am Moldovan. I am living in two worlds, but none is mine at 100%. The roots in Moldova are deep, but they dry because of my absence. In Italy I did not spend enough time to have sufficiently deep roots. Where will my real place be in the future? I don’t really know. Sometimes I imagine myself in Moldova in the role of a Granma, sometimes as a lonely woman in Italy. If I go back to Moldova, will I be able to readjust to the local realities, since the country has also changed a lot? If I stay in Italy, is this what I really want to do?”…

Aliona: is a Russian literature graduate who has always worked as a Russian language school teacher in a small village in the northern part of the country. Times became harder
for this 47-year-old woman in the yearly 90s when she divorced and was left alone with two small boys. As her children were growing and the situation in Moldova was becoming “terribly bad”, her need for more money became urgent. “People were all going abroad to improve their financial situation. Why not me? I have heard and read a lot about Italy, its beautiful music, warm people and delicious food. One day, in December of 1998 I woke up and said: ‘I am going to Italy!’ In a couple of weeks, the trip was already arranged. I borrowed some money, got my tourist visa, left my sons with my mom and made it to Italy with the intention to give my family a nicer future”. At the beginning, the language was a barrier, but she has learned it quite rapidly as it was the best way to get a job. “During my first days as a housekeeper in an Italian family, I felt very badly. I could not accept working in that position for people who didn’t even complete their secondary school but were living better than I was in Moldova. I cried, shouted, got afraid to be sent back to Moldova, changed jobs and did it over and over again. Finally, I understood that I am nothing in Italy, I am nobody for Italians, I will always be underemployed and this will never change. I have just sent those frustrating feelings in the back of my soul and decided to concentrate on my work. That was my destiny”. Two years ago, Aliona managed to bring over her recent university graduate sons who were not managing to find decent employment in Moldova. At least, they could start making money by themselves. Now, when she travels back to Moldova, she admits experiencing strange and even frustrating feelings. “I was shocked that my acquaintances in Moldova do not look at me as at an intelligent person, but consider me a ‘money making machine’. When I am in Italy, I want to be in Moldova; when I am in Moldova, I want to go back to Italy”. For now, she does not plan to return to Moldova, but she doesn’t have anything decided about her future life either. “I am just taking it day by day and then see what happens”.

Discussion

Our in-depth analysis of the five case studies presented above allows us drawing interesting conclusions. Despite the variety of personal stories, we could identify several common patterns that characterize our sample. Before getting deeper into the discussion of our findings, it is worth underlining some socio-demographic features of the individuals who participated in our study. Their age on departure varied significantly from 25 (Natalya) to 52 (Maria) years, while the mean age was 37.2. Contrarily to Inkson and Myers (2003), in our sample the self-initiated foreign experience does not seem to be an activity of the mid-20s, but rather of the late 30s. The age does not prevent the women to involve in such experiences and seek financially more rewarding opportunities abroad. This may be probably explained by the fact that our participants were not driven primarily by career goals when deciding to head abroad. With respect to their marital status, interestingly enough, all but one (Galina, who is the only married woman in our sample) did not seem to have strong family ties in Moldova prior to departure: Natalya was single, Angela divorced (no children), Maria divorced (with one son) and Aliona divorced (with two children). Finally, all of them are university graduates having several years of professional experience acquired in Moldovan labour market. This bias of our sample towards better-educated people may be due to the dynamics of the selection process.
process where women that we approached nominated further contacts from the same group of highly skilled and qualified professionals.

During our interviews, all participants recognized having observed some changes that occurred throughout the time in their perceptions of both internal (themselves) and external (others) worlds. Therefore, we decided to approach the self-directed international experiences from an evolutionary perspective, allowing us to identify four distinctive stages through which these experiences evolve: virtual trip, shock of reality, new status acceptance and personal accomplishment (see Figure 1).

FIGURE 1
Evolution of self-initiated international experience: stages towards personal accomplishment

The first stage – virtual trip – takes place prior to the worker’s arrival in the host country and refers mainly to the specific motivations for going abroad and choosing a given destination. Inkson and Myers (2003) find that overseas experiences are based on wide set of ‘whole-life’ factors, including social connection, imitation, non-work-related exploration, cultural experience, the pursuit of stimulation and change, and changing personal relationships. In our sample we observed two particular reasons that motivated female Moldovans to head abroad. In the first place, they were driven by the desire to reject a negative, something that refers to the detrimental personal situation at home and which can be both economic and socio-affective in nature. All five women mentioned their need to escape from dismal economic conditions in Moldova, while two of them talked about the lack of personal relationships at home (Natalya) and the desire to leave behind the sentimental problems caused by a recent divorce (Angela). In the second place, once the decision to initiate a foreign experience was taken, they were willing to approach a positive, fact that determined their choice of Italy as a host country. Some of them were “literally in love with Italy” and its culture (Maria and Angela), while others were inspired by their friends and relatives to go and discover the beauties of this wonderful country (Natalya and Galina). Italy was therefore seen as a fascinating and mysterious region of the world, the solution to all their problems and the location where the “independence dreams could come true”.
We called this stage ‘virtual trip’, as the contact with the future host country takes place entirely in the transferee’s head and is lived like a surreal dream: the destination is not really known but it is already loved for the vide range of opportunities it seems to be offering. We found that the length of this first stage varied among the participants according to their degree of urgency to migrate and take advantage of these new opportunities, solve specific problems and achieve pre-established goals. This allowed us to distinguish two types of travellers: desperate and rational. For Angela, Aliona and Maria, who were qualified as desperate travellers, the ‘virtual trip’ lasted only a couple of weeks, as they felt the immediate need to escape from their bad personal situation in Moldova at that time. For Galina and particularly Natalya, our rational travellers, it was a much longer virtual experience that resulted in a serious preparation for arrival in the host country. The former waited for her friend in order to go abroad together and had several family members who were already working in Italy, while the latter had also taken Italian language courses one year prior to her departure.

The second stage – shock of reality – starts upon the worker’s arrival in the foreign country and covers the period when the first real contact with this country takes place. During this stage, that typically occurs over the first couple of weeks but can also last as long as several months, our self-employed international worker has the opportunity to compare her virtual vision with what she really sees and experiences on a daily basis. The perception of the external world is transformed in the first place, when the worker feels overwhelmed with so many new things to learn and discover: a new culture, a new language, a new society with its traditions and a new way of living and thinking. All women admitted having realized at the very beginning of their journey that the reality in the foreign country was quite different from what they expected it to be prior to their arrival, paving the way to a strong feeling of social and moral discomfort. It is also the moment when the employees start to do their best to ‘be accepted’ as full members of this new society. The most apparent impediment for the successful integration with the locals is the language and it is the first thing that the workers start to learn. The Italian professor, who used to deliver language lessons to the members of “Together” association, told us that their learning capacity was exceptionally high compared to her American clientele whose condition in Italy was quite different. While the former need to learn the language to get a job, the latter came to Italy as tourists or to take up pre-arranged jobs. For the self-initiated international worker, acquiring the language skills becomes a question of survival: the faster you learn the farther you get in your goals’ achievement.

Then, significant changes occur in the internal world of the employee in the second place, when she starts experiencing a harsh psychological discomfort being caused by strong perceptions of her underemployment. It is the moment when she is torn by her feelings of not having the same social status as she had in her home country, situation that is thought to be completely unfair. In fact, the most important distinguishing feature of the ‘reality shock’ stage that surfaced from all our interview is the worker’s search of identity. “Who am I? A teacher? A cleaner? A professional? A housekeeper? What am I doing here? Why am I here?” The answers to those questions are not easy to get. The worker gets frustrated, her perception of herself is downgraded, being also conditioned by the
opinions that the locals make about her and her home country. It is at this point that the ‘brain waste’ phenomenon takes effect, when the worker begins realizing that she “cannot give the best of herself” neither to the home country nor to the host one. As the need to find an internal equilibrium becomes prevalent, she starts struggling ‘to accept’ this downgrading of her social status. It seems that this stage is crucial for deciding whether to stay in the new society or return home. We hypothesize that for those who do not manage to accept their new position in the receiving country, the self-initiated foreign experience is likely to be abruptly terminated during the second stage. We call those people ‘prematurereturners’ because they decide to go back home, despite of the fact that their pre-established objectives for the foreign journey were not yet achieved.

The third stage – new status acceptance – allows the worker to accept the new role she is assuming in the host country, even though it is not commensurate with her professional qualifications and intellectual capabilities. Within this stage, our sample allowed us identifying two types of self-initiated international employees, namely ‘resignators’ and ‘sublimators’. The former type refers to someone (like Galina or Aliona) who adopts a passive attitude demonstrating an uncomplaining acceptance of her status in the receiving country without any desire to continue knowing, discovering and growing. Oppositely, the latter type (that we attributed to Natalya, Angela and Maria) accepts the new status actively directing all her energies into useful channels: she does not forget being in a foreign and unknown for her society and takes advantage of each opportunity she has to discover its traditions, learn its prevailing rules, visit its historical places and thus continue growing intellectually. For ‘resignators’, this third stage is likely to last infinitively or until they decide to interrupt their experience and return home, while for ‘sublimators’, it lasts just a couple of weeks getting them closer to the last stage of their experience.

It may however appear surprising that our two ‘resignators’ did not return home and decided to continue their self-initiated foreign experience in the long run. In our opinion, this becomes possible due to a better understanding by the employee of the host country functioning, along with the change in the home country perception that begins to occur in her mind. In fact, the most striking characteristic of all our respondents, whose international journey is now extending over more than six years, is what we called ‘the syndrome of home-host country foreignness’. At this point of their self-directed experience, all women who participated in our study had the opportunity to travel back home on several occasions. While they still felt foreign in their host country, they started to feel foreign in their home country as well. Although all of them still believed having a purely Moldovan soul, they started looking on Moldovan realities through different lenses: the personal relationships they left behind several years ago have been lost (Maria), the economic and political situation in Moldova did not get better (Angela), their tolerance of Moldovan difficulties has diminished (Natalya), the perception the locals made of them downgraded from an intelligent person to a ‘money making machine’ (Aliona), making their willingness to quit the home country shortly after their arrival to appear again (Galina). The symptoms of this syndrome were the most apparent in the following citations: “For Moldovans I am Italian, for Italians I am Moldovan. I am living in two worlds, but none is mine at 100%. The roots in Moldova are deep, but they dry...
because of my absence. In Italy I did not spent enough time to have sufficiently deep roots” (Maria); “When I am in Italy, I want to be in Moldova; when I am in Moldova, I want to go back to Italy” (Aliona).

We hypothesize that for those workers who reached the third stage of their journey, the ‘syndrome of home-host country foreignness’ represents the main factor determining the total length of their self-directed foreign experience. Both ‘resignators’ and ‘sublimators’ in our sample suffering from this syndrome are likely to continue their experience over longer periods of time, with no specific plans for return. However, their inherent motivations to stay in the host country differ. A ‘resignator’, who believes that she “will always be their [Italians’] servant, there is nothing to do about it”, finds exclusively economic reasons that explain her prolonged foreign experience. According to Galina, “when you get used to being paid 20 or even 30 times more than what you were getting in Moldova, you think twice before taking such kind of decision”. The resignators will therefore let the ‘brain waste’ effect to dominate throughout their remaining self-initiated international experience. On the contrary, a ‘sublimator’, who is “fighting for her place under the sun”, finds psychological reasons for her stay in the host country. Her main motivation is to reach the fourth and last stage – that of personal accomplishment – which is the longest in duration and the most challenging stage of her journey. The ‘personal accomplishment’ refers not only to worker’s social integration in the host country, but also to her professional inclusion in the foreign labour market. ‘Sublimators’ have to demonstrate to themselves that they are able to defy the reality, seeking proactively better personal and professional opportunities that allow them to move further towards self-accomplishment. It is during this last stage that the ‘brain waste’ effect in both home and host countries, is transformed into the ‘brain gain’ phenomenon, as sublimator’s brain starts to be used at its fullest capacity for the host country’s benefit.

One could legitimately wonder whether the rational or the desperate traveller (from the first stage of our model) have any predisposing characteristics to transform into either ‘resignator’ or ‘sublimator’ worker (from the third stage of our model). Although it is generally thought that better preparation leads to better results, this statement was not confirmed in our sample. In other words, being a rational traveller (that is, taking time to prepare for the experience) during the ‘virtual trip’ was not an automatic guarantee that the worker would arrive to the ‘personal accomplishment’ stage, even if this seems to be the case of Natalya. And vice versa, being a desperate traveller (that is, leaving the home country without any serious preparation for the foreign experience) does not predetermine the worker’s blockage at the ‘new status acceptance’ stage, although it happened in the case of Aliona. Indeed, the desperateness of both Angela and Maria did not prevent them from reaching the ‘personal accomplishment’ stage, while the rationality of Galina did not help her to go beyond the ‘new acceptance status’ stage. Hence, our analysis reveals the existence of several hybrid types of self-employed international workers where both the rational and desperate traveller could evolve into either a ‘resignator’ or ‘sublimator’.
Finally, similarly to what Inkson et al. (1997) and Suutari and Brewster (2000) did in their studies, our evolutionary approach to the self-directed international experience allows us confronting this type of journey with the more traditional one undertaken by expatriates. Those comparisons are illustrated in Figures 2 and 3. Scientific literature on expatriate managers has traditionally analyzed how they adjusted over time to the foreign culture and general environment in the host country. According to Black and Mendenhall (1991), the expatriate journey begins after the worker’s arrival to the destination and his adjustment corresponds to the U-curve logic. In the case of self-initiated international workers, the first stage of their journey into the new culture (‘virtual trip’) begins when they are still at home, while the last three stages develop once they arrive to the host country. Contrarily to an expatriate whose primarily concern is to adjust to the local culture, the self-directed international worker seeks integration with the new society by struggling ‘to be accepted’ (by locals) and ‘accept’ (her new status). The unsuccessful expatriate adjustment determines his premature return to the home country, as opposed to self-initiated foreign transferees, where those who have both successfully (‘sublimators’) and unsuccessfully (‘resignators’) integrated with locals do not return to their home but continue to stay in the host country.

Conclusion

In this paper we have explored the cases of five Moldovan women who involved in self-initiated foreign experiences. Our in-depth analysis of the case material allowed us identifying four distinctive stages through which those experiences evolve (virtual trip, reality shock, new status acceptance and personal accomplishment) and several types of self-initiated foreign assignees according to their urgency to migrate (‘rational travellers’ and ‘desperate travellers’), their lack of resistance to the shock of reality (‘premature returners’) and their attitudes towards personal accomplishment (‘resignators’ and ‘sublimators’). Given the emergent understanding of these issues and the limitations of our sample, further research is needed to verify our preliminary findings. For instance, it is worth mentioning that all our respondents headed abroad on their own initiative in the period immediately following the Russian and regional economic crisis from 1998. Future investigations can extend our analysis by focusing on larger and more diversified
samples that would include individuals who have undertaken their self-directed international experiences more recently.

As suggested by Inkson et al. (1997) and argued in this paper, self-initiated foreign experiences play an important role in economic development of both sending and receiving countries and as such are worthy of further consideration by academics and policy makers at the national level. We believe our study made a contribution towards creating a knowledge base on these types of Moldovan workers and their involvement in less formal labour market processes in Italy, that should enable both Moldovan and Italian governments to develop innovative schemes and programmes to enhance security and protect the interests of these workers in national settings. Indeed, the mass emigration that Moldova is currently facing becomes a severe impediment to its economic and political modernization. Therefore, the Moldovan policy makers have to approach the issue more seriously, making some systematic, official attempts to court the members of Moldovan Diaspora and persuade them to return. As far as the Italian counterparts are concerned, there are debates about whether that workforce inflow from poorer to richer regions of the world is good or bad for the receiving country. Some argue that this phenomenon will result in unemployment of locals, others say that the richer countries of the European Union benefit the Europe in general by going for cheap labor within the European continent (as opposed to for example India or China) thus fostering its economic development and securing its external borders, still others suggest that the receiving countries attract foreigners in those sectors where the is a significant lack of local workforce. Given these advantages, the host country governments should also undertake more initiatives to provide those self-initiated international employees with more secure life and working conditions.

References


Globalization and the importance of Strategic Technology Management in the Industrial Development of Bahrain – A Proposed Framework

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Abstract: Strategic technology management (STM) approach, which places technology in a strategic context, emerged in the late eighties in response to failure of more traditional techniques for exploiting technology. STM in this study included aspects of both technology strategy (content) and technology management (process). Many studies in strategic management research have investigated the relationship between technology strategy, technology management and firm performance, but largely from a western viewpoint. The dramatic increase in cost of producing goods and services in the midst of ever increasing cost of oil and other raw materials places huge pressure on the economies of newly developing countries. Unless there is a shift in the mind set of the senior executives whereby technology management is alleviated at the business level, performance enhancements can not be achieved. This study analyses the gap in literature where there is paucity of studies in analysing STM application in the countries in the East. A conceptual framework has been proposed for both the manufacturing and services sectors in Bahrain. The framework is based on the results achieved by a similar study by the author in a developing country in SE Asia. The paper proposes certain hypotheses, which need to be tested. The survey instrument comprises of unique new variables developed by the author which need to be explored and determine which of these could contribute to performance. The conceptual model would then be modified to develop a STM model for Bahrain. The results of the research could then be used by the National Policy Planners to develop specific technology policies for the manufacturing and services sector. This would be one of the first attempts in Bahrain to manage change using STM based on the research carried out in a global context.

Introduction

To gain competitive advantage in the midst of changing technologies, the firms need to evaluate their technological policies and integrate it with the business strategy. Poor technological choices by management may severely affect firm performance (Zahra 1996A, Zahra 1996B). The failure of the traditional techniques for exploiting technology like R&D has emphasised the need to address technology at a strategic level (Drejer 1996). Almost invariably, all studies on Strategic Technology Management share common features, they generally employ different industry perspectives, research methodologies and study dimensions, which makes it difficult to make comparison among them (Herman 1998). Very few of these studies focus on both the content and process aspect of strategy. Like the business strategy formulation and implementation, it is useful to analyse technology strategy formulation and implementation with a business focus. There is a paucity of empirical studies on the process by which content of technology policy is defined and its linkage with business strategies. Since then few studies were done to analyse the technology strategy types in high tech sector of the
Western Countries. It was decided to explore the significance of STM issues in the East, consequently an in-depth research was carried out in an Eastern country which experienced tremendous growth. The results of the study have provided unique strategies applied by the firms in the high technology sector which contributed to their remarkable performance. The attributes developed for the East has provided a foundation and starting point to test them in various similar economies. This study attempts to address this issue and recommends techniques and methods to evaluate the suitability of these technology strategies for Bahrain. The research would enable identify specific technology strategies which could be applied by the firms in the manufacturing sector.

The two components of STM: “Technology Strategy” (TS) and “Technology Management” (TM) have been operationalized by strategy and management variables. Data will be gathered from the Senior Executives of the relevant firms through a survey questionnaire. Statistical tools will used to perform Factor and Regression analysis on the variables representing various dimensions. The resulting technology strategy and management factors will then be analysed using SPSS software to determine their relation with firm performance, firm type, firm size and R&D.

This research will contribute empirical support to the field of strategic management research by developing more comprehensive technology strategies, relevant to a culturally different environment - Bahrain.

**Development of Strategic Technology Management**

The technologies are changing at a very rapid rate. In order to gain a competitive advantage in this dynamics, the firms need to evaluate their technological policies and integrate it with the business strategy. Poor technological choices by management may severely affect firm performance (Zahra 1996A, Zahra 1996B). The failure of the traditional techniques for exploiting technology like R&D has emphasised the need to address technology at a strategic level (Drejer 1996). Technology strategies are being viewed today as the key drivers of business strategies, especially for technology intensive firms. Technology strategy considerations in the development of business level strategies, however, should not drive a company to have a technological strategic orientation (Ansoff 1986).

Technology offers operational efficiencies and potential competitive advantages that can result in cost containment and lead to increased revenues. Identifying which processes, products, resources and technologies are right for a business can be challenging and, for some, overwhelming. The key to effective technology and business integration is aligning the technology resources with the business needs and service levels. This includes matching technologies, skill sets, resources, and IT priorities to business operations, processes, and priorities (RSA Corp, 2007).

Clarke, Ford and Saren (1989) used the term technology management to refer to organizational issues and processes involved in developing and implementing a strategic approach to technology. Through this approach, technology management issues can be operationalised and integrated into normal management activities of the firm. Strategic
Technology Management (STM) did not emerge as a distinct area of managerial and academic interests until late 1980s. The key managers may initiate efforts to gain access to newer technologies, but the question is whether the approach they adopt is strategic or a series of ad hoc decisions (Quinn 1988). STM is synonymous to Technology Policy in the context of this study and defined as developing technology strategies and then evolving methods to implement and manage them.

Linstone (1984) highlights that the technological, organizational and personal perspectives are frequently used by scientists to analyze complex phenomenon. The technological perspective is of interest in this study.

This research will contribute to the strategic technology management literature by utilizing the dimensions of previous studies in evolving a set of dimensions relevant to a culturally different environment. This will also enable to test the suitability of a new instrument while making a comparative analysis of application of STM in Bahrain and should add considerably to the existing knowledge in this field.

The strategies evolved, though applied by a variety of firms but mostly unknown to them in the context they have been evolved based on this research, could help in improving the performance of firms in Bahrain. The results would be utilized to develop a strategic management approach (model) by National Technology Planners to help identify the strategies needed to be employed by the firms.

From a business perspective, there is a great potential to apply the research findings in any manufacturing sub-sector for which certain local moderating variables need to be accounted for.

**Literature Review**

Development strategies for industrialization can be broadly divided into import substitution and export orientation, strategies not mutually exclusive (Chen et al, 1997). Import substitution aims at replacing the imported products by those produced by newly developed industries for consumption in the domestic market. Export orientation is a strategy in which newly developed industries produce for overseas markets. Import substitution is achieved by policies which are designed to protect the infant industries and discriminate against exports. Such measures include overvalued exchange rates, import controls, high tariffs etc. These force import prices of inputs above the world level, which the exporters have to face. Export orientation can also be divided into a first stage of exporting manufactures that are more labour intensive and a second stage of exporting products that are more capital and technology intensive (Chen et al, 1997).

The Asian NIEs (Newly Industrialized Economies) industrial policies differ both in nature and in approach. These can be divided into two categories, namely mission-oriented (M-O) and diffusion-oriented (D-O) (Chen et al, 1997). M-O economies have three characteristics: 1) there must be centralization of decision-making 2) the government has a mission to pursue at one point in time and 3) the research focuses on a small number of priority industries. Singapore, Korea and Taiwan and to some extent...
Malaysia fall in the category of M-O economies. The D-O industrialization seeks to provide a natural industrial structure for facilitating the diffusion of production and technology (Chen et al, 1997). Hong Kong economy falls in this category. The M-O strategy is an integrated approach to industrial development. South Korea's industrial development policy during the past several decades is its integrated approach to industrial development. Trade policy, human-resource development policy, and technology policy were well coordinated and complementary to industrial policy. An integrated policy approach to industrial development appears still to be relevant today for developing countries (Kim 2005).

**East and South East Asian Regional Perspective**

East and South East Asian economies achieved high growth rates between the period 1965 and 1990. The World Bank 1993 report highlights eight Asian countries as high performers – Japan, the first tier four industrializing economies (NICs) of South Korea, Taiwan, Singapore and Hong Kong, and the three second tier NICs of Malaysia, Thailand and Indonesia. These have been regarded as miracle economies by the World Bank. The report concludes “The high growth has been by getting the basics right and largely due to superior accumulation of physical and human capital” (World Report 1993). The manufacturing sector growth in the SE Asian countries have been impressive and contributed to their GDP increase. However “these figures do not tell us much about the actual nature and process of industrialization which requires a close scrutiny of the manufacturing sector …..”(Jomo et al, 1997). This study in part addresses this issue.

Within the Asian context, industrial policy instruments have been employed extensively in Northeast Asia compared to South and Southeast Asia. In South and Southeast Asia, arbitrary state interventions have taken place by the politicians to suit the interest of politically influential business people and for interethnic considerations. These interventions have to some extent also masked some important technology plans (Jomo et al, 1997). A study by the author was carried out recently to uncover this mask whereby a sub-sector in the manufacturing sector of a country in Southeast Asia was selected, its performance in terms of technology strategies (management and implementation) employed was analysed and compared with similar strategies in the West. Based on the analysis of data, STM attributes were developed which contributed to performance. The relationship of these attributes with the performance of firms and their type was also examined. The results are not yet available for publishing.

Jomo (1997) has stated that the rapid growth of East Asian NICs has brought our attention to the role of cultural factors in industrialisation. In the Northeast Asian NIC’s there has been a national consensus behind accelerated industrialization due to the relative homogeneity of cultures in those countries. This is evident from the fact that there have been no major ethnic troubles in these countries compared to East Asian countries of Malaysia and Indonesia where the societies are more ethically divided. Some writers argue that in the Southeast Asian countries politically dominant indigenous ethnic elites have emphasized interethnic redistribution at the expense of other priorities. Consequently, alternate policy agendas more conducive to late industrialization efforts
have been thwarted. But there is no denial of the fact that cultural practices (social relation, cooperation etc) in East Asia have been crucial for the development of business networks which do not rely on the state and have contributed towards capital accumulation (Jomo et al, 1997). The technology strategies leading to success of the manufacturing sector in the West is well researched and documented, however the culture had an important impact in their evolution and implementation. The industrial policy instruments too in the West have been responsible for this success. So in the East, despite state interventions and selective policies (e.g. heavy industrialization in Malaysia in mid-1980s), the remarkable progress must have been influenced by similar strategies applied in a different cultural context or evolution of new strategies pertinent to the local culture. This aspect was studied by the author and the results compared with those from the West.

Technology Policies and Strategies
Technology is recognized as potentially the single most important source of competitive advantage. Not all applications of technology management are, however, strategic (Messina, 1989). Technology leadership therefore does not automatically yield competitive advantage. The strategic content of technology should then ensure that it is sustainable for a long time and produces visible effects to the customers. A useful technology strategy must address the critical technologies vital for the attainment of strategic business objectives and the ways to achieve this domination.

Japanese firms have long emphasized technology management. In Japanese firms “need-oriented” ideas that flow from the marketplace are more important than “seed-oriented” ideas generated by research staffs (Earl, 1992). It is believed that adherence to strategic plans promotes firm sales growth rate (Cowin, 1998).

Industrial development is a process of acquiring technological capabilities in the course of continuous technical change. Kim (1998) has proposed two frameworks—technology trajectory framework and technology strategy framework which can be used to analyze technology policies and strategies in developing countries (Kim, 1998). Representation of technology strategies numerically is of concern to many authors. The problem of judgment in constructing such models for policy analysis severely limits the interpretation of outputs from such models (Watson, 1999).

Gap and the Opportunity
These efforts by the author in undertaking an in-depth research in this filed has been the guiding factor in undertaking this study to investigate the technology policies in the high-tech manufacturing sector of Bahrain. The objective is to identify the technology strategy “types” adopted by the firms which contributed to their success. Identification of such strategies would be a useful contribution to the field of strategic management application in a high-tech sector of the economy. The link between the strategy types and performance of the firms in the manufacturing sector would provide a useful result to determine the effect on economic development of Bahrain. Extension of this research to include testing the appropriateness of these strategy types (model) in other manufacturing...
sectors could provide the national planners and researchers with an extremely useful tool for comparative analysis of the growth process in the entire manufacturing sector.

Some work to explore strategies in the hi-tech industries in USA was done lately (Wilbon, 1999) but the study utilized published data from firms "prospectus". The study done by the author addressed the above limitations that existed in literature and in similar studies. These results will now be used to develop a survey questionnaire for exploring the Technology strategies in Bahrain.

**Proposed Framework for Bahrain**

A hypothetical framework has been developed based on the results of a similar research in a country in the East (Fig 1). The attributes will be tested and the hypothetical framework modified to develop a working model for Bahrain.

**Figure 1: Hypothetical framework of strategic technology management in Bahrain**

Developed for this thesis from the literature review and doctoral dissertation (Sikander, 2008)

**Hypotheses**

The testable hypotheses for this study aligned to the objectives are given below:
Hypothesis 1. The technology strategies employed by the firms are influenced by the National Technology Policy.

Hypothesis 2. The technology management processes employed by the firms are influenced by the National Technology Policy.

Hypothesis 3. The performance of the firms is dependent on the technology strategies employed.

Hypothesis 4. The performance of the firms is dependent on the technology management processes employed.

Hypothesis 5. The technology strategies employed by the firms has a significant relationship with the type of firm.

Hypothesis 6. The technology strategies employed by the firms has a significant relationship with the size of firm.

Hypothesis 7. The technology strategies employed by the firms has a significant relationship with the R&D focus of the firms.

Hypothesis 8. The technology management processes by the firms has a significant relationship with the type of firms.

Hypothesis 9. The technology management processes by the firms has a significant relationship with the size of firms.

Hypothesis 10. The technology management processes by the firms has a significant relationship with the R&D focus of the firms.

Pilot Study

The data for this study will be obtained through a survey questionnaire. The questionnaire has been developed in line with the objectives of the research and to maximize information extraction from the respondents (Kinnear 1991). The dimensions and variables for the questionnaire will be selected from the results of the survey done by the author in his latest research in another country. The survey questionnaire will be developed and tested in a small pilot study to assess the clarity of the questionnaire items.

Five types of data will be gathered for the study:
- Individual's Profile Data
- Organisation/Business Data
- Competitive Environment Data
- Technology (Strategy and Management) Data
- Management Issues

Advantage will also be taken of prior research results to select the dimension variables. The data on five strategy and five management dimensions is in line with that suggested by Herman (1998). Individual profile and Organisational data will be used to check for response bias and content validity. Competitive environment data will be gathered to get an indicative idea about the markets in which these firms operate. Technology data will provide the existence or else wise of technology policies and the level of knowledge about technology of the respondents. Comments will be invited for any specific management issues faced, these comments will then used to develop appropriate variables. The survey questionnaire will be pre-tested in a pilot study to assess the clarity
of its direction and the questionnaire items. The pilot study will include face-to-face interviews with CEOs of selected companies. Based on the Pilot Study and CEOs responses, the questionnaire will be revised to develop the final format. The results are planned to be entered into the SPSS software.

The Technology Strategy dimensions include the elements of: key positioning, leading in discovery of new technologies, introducing innovative products at the right time, and incorporation of new technologies in firm’s plants and facilities, whereas Technology Management dimension employ: keeping abreast with emerging technologies, formal processes to plan and select technologies and in-country external acquisition of technology. Each of these elements are represented by items. A likert scale has been utilized to tap the items of interest to the respondents.

The background variables will be analysed after the data is entered in SPSS. The data from the main survey instrument would also be utilized to perform multiple regression analysis to observe the influence of the items on the elements and dimensions. It will also be used to predict the differences in responses to selected dependent and independent variables and predict the magnitude of elements and responses of the different firms. Factor analysis will be used to transform the variables into a new set of linear combinations called the principal components. The proposed conceptual model for STM in Bahrain would then be statistically tested using the PCA. A new model would be subsequently developed after naming the new factors at the item level. The new factors which define the dimensions will be discussed in detail. STM which is the combination of all the 32 variables will be discussed in relation to the background variables and the two new dimensions of TM and TS defined by the evolved factors. The new dimensions of TM and TS will also be used to determine the relationship with firm size, firm type, R&D efforts and firm performance. The various hypotheses will be tested based on the above relationships.

Conclusions

STM studies to evolve the strategy types have particularly focused on developed countries. No studies to date have been found which explored the nature of technology strategies applied by the firms in the manufacturing sector of developing countries and whether they were influenced by the National Technology Strategies. To be more precise many multi-national countries are operating in these countries and it would be worthwhile to note if the strategies they apply are similar to those in their parent countries or have been adapted to the local environment, which is culturally different.

Through a detailed examination of the previous studies and a research carried out recently in a country in Asia, the author will develop a new instrument developed incorporating the results of the research and subsequently apply it to Bahrain. The questionnaire will be piloted in order to improve its validity and before being administered in the final survey. A modified model will be evolved and it will be argued whether the National Technology Policy which provides impetus for the economic growth and structural transformation of the manufacturing sector, influences the strategy
formulation and implementation at the firm level or not. It will also be argued if there is a difference in the strategies with respect to firm size, firm type. A final goal is to explore the performance of the firms were affected by the strategies or not.

Limitations of the Study

To keep this study within the objectives set down, boundaries will be placed around the problem. In determining the various factors on technology management, some exogenous (moderating) variables like culture, financial structure, training philosophy, human resource etc (Jantan & Srinivas, 1999) will be omitted. The study will initially be limited to one high-tech sub-sector. The study will use variables from prior research, which were evolved for manufacturing firms in not a similar environment, both culturally and technology wise. There will also be limitations as a result of measures to be used as well as the data analysis techniques to be employed.

References


Consumers’ Shopping Motivations: An Investigation of Indian Retail Shoppers

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Abstract: A stream of research has investigated the reasons which motivate consumers to shop and has offered some interesting insights into consumers’ motivations for shopping. Unfortunately, most of the existing literature is North American in origin and application. The paper uses data from Indian retail shoppers to profile them into different segments. Using Cluster Analysis, the paper identifies and discusses five homogeneous groups with different emphasis on different shopping motives. The paper is part of a research which is still in progress and seeks to highlight the significance of studying consumer behaviours in different cultural contexts. The paper discusses implications for brand managers and suggests future research directions.

Keywords: Shopping Motivations, Profiling, Retail Shoppers, Retail Strategy

Introduction

There have been many attempts to segment consumers using their motivations in order to explain the consumer psyche and subsequently the retail strategy formulation (Bloch et al., 1994; Reynolds et al., 2002; Reynolds and Beatty, 1999). While some of this research has focused on the utilitarian aspects of the shopping experiences (Babin et al., 1994), others have focused on hedonic and experiential aspects of shopping (Arnold and Reynolds, 2003; Hirschman and Holbrook, 1982). Still others have attempted to segment consumers on the basis of their decision making styles, which is considered to be a mental orientation characterizing a consumer’s approach to making choices (Lyonski et al., 1996; Sproles and Sproles 1990; Sproles and Kendall, 1986). The underlying idea is that consumers engage in shopping with certain fundamental decision making styles including rational shopping, brand conscious, quality conscious and impulsive shopping.

However, most of the existing shopping literature is North American in origin and application. There remains a need to investigate consumes behaviours in non Western contexts and the current paper is one such attempt to provide insights into some of the psychological reasons which appear to motivate consumers in India. The need is highlighted through the fact that many of the successful retail organizations have expanded in different geographic regions of the world contributing towards the globalization of the consumer marketplace. The paper is based on a research project which is still in progress and which aims to answer a number of important research questions: What are some of the key factors that motivate the Indian consumers to shop? Do the shopping motives that drive consumers to shop in the West also drive consumers in the Indian market? How is the Indian shopping behaviour structured in terms of
frequency of shopping, number and types of stores visited, amount of money spend during each trip, retail shopping expertise and retail patronage behaviour? Answers to these questions are likely to be relevant to not only the multinationals operating in India but also to the local businesses in terms of understanding of the dynamics of Indian consumer behaviour.

**Conceptual Background**

A number of researchers have sought to highlight the utilitarian and hedonic aspects of shopping experiences (Arnold and Reynolds, 2003; Babin et al., 1994; Batra and Ahtola, 1991; Langrehr, 1991; Roy, 1994; Wakefield and Baker, 1998). The utilitarian aspects of shopping experience are often characterised as task-related, rational and whether or not a product acquisition related mission is accomplished (Arnold and Reynolds, 2003; Batra and Ahtola, 1991; Babin et al., 1994). On the other hand, the hedonic aspects reflect shopping’s potential entertainment and emotional worth and can involve increased arousal, heightened involvement, perceived freedom, fantasy fulfilment, and escapism (Arnold and Reynolds, 2003; Babin et al., 1994; Bloch and Richins, 1983; Holbrook and Hirschman, 1982). In a recent study, Arnold and Reynolds, (2003) while focusing on motivations that are primarily hedonic and non-product in nature, identified and validated six broad categories of hedonic shopping motivations. These included adventure shopping (to seek stimulation, adventure, and feelings of being in a different world), social shopping (for enjoyment of shopping with friends and family, socializing while shopping and bonding with others), gratification shopping (for stress relief, to alleviate a negative mood and as a special treat to oneself), idea shopping (for keeping up with trends and new fashions and to seek new products and innovations), role shopping (for getting enjoyment as a consequence of shopping for others) and value shopping (reflecting shopping for sales, looking for discounts, and hunting for bargains). Similarly, an earlier work by Tauber (1972) highlighted the importance of personal and social motives related to shopping behaviour. The personal motives include the needs for role playing, diversion, self-gratification, learning about new trends, physical activity and sensory stimulation. The role playing motive highlights activities that are learned and are expected as part of a certain role or position in society such as mother, housewife or husband. Diversion highlights shopping’s ability to present opportunities to the shopper to escape from the routines of daily life and therefore represents a type of recreation and escapism. Self-gratification highlights shopping’s potential to alleviate depression as shoppers can spend money and buy something nice when they are in a down mood. Physical activity highlights consumers’ need for engaging in physical exercise by walking in spacious and appealing retail centres, particularly when they are living in urban and congested environments. Sensory stimulation highlights the ability of the retail institutions to provide many sensory benefits to consumers as they can enjoy the physical sensation of handling merchandise, the pleasant background music and the scents. The social motives identified by Tauber (1972), on the other hand, include the needs for social experiences, communication with others, peer group attractions, status and authority, and pleasure for bargaining. The social and communication motives highlight the shopping’s potential to provide opportunities to socialise meet and communicate with others with similar interests. The peer group attraction highlights consumers’ desires to be with their
reference group whereas status and authority reflect shopping’s ability to provide opportunities for consumers to command attention and respect from others. The pleasure of bargaining reflects consumers’ desires and abilities to make wiser decisions by engaging in comparison shopping and special sales. The present paper mainly focuses on the hedonic shopping motivations identified recently by Arnold and Reynolds (2003) and seeks to utilise their framework in an effort to understand shopping motivations of Indian consumers.

Methodology

First, a questionnaire in English was drafted containing Likert-scaled items scoring from 1 (strongly disagree) to 7 (strongly agree) to measure seven shopping motivations: adventure shopping, value shopping, role shopping, gratification shopping, social shopping, idea shopping and utilitarian shopping (Reynolds et al., 2002; Babin et al., 1996). The motivations were selected on the basis of our prior understanding of Indian society, its cultural values and a review of the relevant literature. Measures were also included to capture frequency of shopping, number and types of stores visited during a typical shopping trip, amount of money spent, and demographics. Measures for other factors such as attributes associated with shopping centres, shoppers’ levels of expertise, store satisfaction and behavioural intentions were also included. A total of 20 pilot tests were then conducted with consumers who were seen as similar to the population for the study. The purpose of the pre-testing was to refine the questionnaire and to assess the validity and applicability of measures; corresponding amendments were made to the questionnaire after the pilot tests.

Following Reynolds et al., (2002), a mall intercept procedure was used to collect the data in Delhi whereby shoppers who had finished their shopping and were leaving the shopping mall were randomly approached and asked to fill in self administered questionnaires. Data was collected over a three-week period covering both busy days (e.g. weekends) and normal weekdays. All of the shopping malls had a movie theatre, restaurants, food courts, parking facilities, branded stores and a variety of other stores. The procedure resulted in 271 usable questionnaires. Overall, the sample is primarily aged 20-39 (71%); 53% single and 47% married; highly educated (81% had college or university degrees), covered different occupations (46% professionals or senior managers, 27% students and 14% housewives), and 53% male and 47% females.

Data Analysis and Findings

Exploratory Factor Analysis

The 26 items used to measure the seven shopping motivations were all subjected to exploratory factor analysis with principal axis factoring and varimax rotation with scree test criterion and Eigen values used to confirm the number of factors to extract (Hair et al., 1998). The main purpose of the exploratory factor analysis was to confirm whether items loaded correctly to the corresponding factors as identified by previous research. The procedure resulted in the estimation of a final seven-factor model, while none of the
items exhibited low factor loadings (<0.40) or high cross-loadings (>0.40). The seven factor solution accounted for 73.4% of the total variance, and exhibited a KMO measure of sampling adequacy of 0.805. In order to quantify the scale reliabilities of the factors identified, Cronbach alpha coefficients were computed; all of the alpha coefficients easily passed the minimum level of 0.70 recommended by Nunnally (1978) indicating acceptability and reliability of all of the scales. Results of factor analysis together with the percentage of total variance for each of the factor and calculated Cronbach alpha scores are shown in Table 1.

[Insert Table 1 here]

Cluster Analysis

In order to classify respondents into groups based on their responses to the shopping motivations, a multi-step cluster analysis was utilized (Hair et al. 1988; Reynolds and Beatty, 1999). Using Ward’s method in hierarchical clustering procedure, clusters were formed based on factor scores. An examination of the distance between two clusters for three, four, five and six cluster solutions resulted in the determination of a five-cluster solution (Sharma, 1996; Reynolds et al. 2002, Reynolds and Beatty, 1996). Then a K-means clustering procedure with the initial seeds provided by the hierarchical analysis solution was conducted to obtain the final clusters. The results of cluster analysis are reported in Table 2. We interpreted the clusters as follows:

Stylish Role Performers: This is the first group of shoppers, which makes up the second largest percentage (24%) of the respondents scoring the first highest on role shopping and the second highest on idea shopping. However, they scored gratification shopping as the lowest followed by value shopping as the second lowest.

Highly Rationalists: This is the second group of shoppers, which makes up the smallest percentage (11%) of the respondents scoring the lowest on idea shopping, value shopping and role shopping, but scoring the highest on utility shopping.

Role Oriented Bargainers: This is the third group of shoppers, which makes up 15% of the respondents scoring the lowest on utility, idea and social but moderately highest on value, role and adventure shopping.

Self Oriented Idealists: This is the fourth group of shoppers, which makes up 13% of the respondents scoring the lowest on role, utility and social and moderately highest on idea shopping.

Happy Shopping Lovers: This is the fifth group of shoppers, which makes up the largest percentage (38%) of the respondents scoring every aspect as above average and in particular the gratification, value and utility.

[Insert Table 2 here]
Discussion, Conclusions and Implications

The five segments that emerged from our analysis are quite different from one another and are significant for marketers in a number of important ways. For example, the happy shopping lovers, report their primary shopping motivations to be gratification, value, utility, and social. An important point to note about this segment is that they did not score any aspect of the shopping environment in a negative manner. It might be that they feel happy and appear to enjoy the shopping surroundings so much so that they ignore any negative aspect of shopping. Like respondents in Babin et al.’s (1994) study, respondents in this segment appear to recognise the shopping activity as a self-gratifying and therapeutic activity. This suggests that these customers view shopping as an escape mechanism to get their minds off their problems and as a way for relieving stress and alleviating negative mood. The implications are that the retail managers need to focus on improving store atmospherics, introducing recreational and fun activities adding to the entertainment and emotional worth of shopping experiences (Wakefield and Baker, 1998). Since these customers also appear to actively seek value and utility, managers need to make sure that their products are not very expensive and that they provide sales promotional opportunities to their customers on a regular basis. The segment can best be targeted emphasising the overall shopping experiences using experience-based advertising by focusing on what it feels to use a brand or service as these customers are likely to value messages that are perceived to be not only self relevant, self fulfilling and idealistic but also contributing to their overall shopping experiences.

Similarly, the second largest segment, stylish role performers, report their primary shopping motivations to be role and idea shopping with least value attached to gratification seeking and value seeking. Therefore, these shoppers appear to see shopping as a leisure activity (Martin and Mason, 1987), fulfilling some important role in family and social life. They also appear visit the marketplace seeking for new ideas and to keep up with trends and new fashions. Since they do not value social aspect of shopping, one might argue that they appear to fulfil the family roles as part of their responsibilities and may not engage in fashion and style consumption for the sake of others but rather for self fulfilment and self enhancement. The best way to target these customers, therefore, is to emphasis the connection of brands to their self concept while depicting new fashion ideas and trends in communication messages.

Role oriented bargainers, on the other hand, appear to be quite unique because while they seek value, role, and adventure, they do not attach importance to utility and social aspects of shopping. In other words, the segment is largely motivated to shop for sales looking out for discounts, promotions and bargains. They appear to do so as they may have a role in their families to do the shopping and feel a need to seek bargains while they are shopping for other family members. Marketing communication messages offering price promotions and reinforcing family related roles are likely to be effective for this segment.

Similarly, self oriented idealists are also unique because while value shopping to keep up with trends and new fashions, they do not value other aspect of shopping encounters. In other words, the only reason they like going shopping is when they are seeking out for...
new products, new trends and new fashion items but only for self consumption. They place very low value to role shopping which might be due to the fact that they might be unmarried, single and students. The best way to attract this segment is to use self relevant imagery in advertising emphasising the novelty and newness of shopping experiences.

Finally, the highly rationalists, represent a very unique set of customers: those who view shopping as a purely rational and task related activity that needs to be done as soon as possible. They appear to have a work mentality and might use shopping lists to reduce their shopping fatigue. In other words, they appear to perceive shopping to be a routine and a habitual activity. They are very likely to evaluate brands very carefully and pay great attention to product benefits and features while shopping. They might may feel happy when they realise that their particular shopping need was accomplished in an effective and efficient manner. They are likely to finish off their shopping quickly by patronizing same brands and stores to minimize their cognitive efforts. The implication is that the brand managers have to make sure that they improve the store layout to make it easier for such consumers to shop and by training the staff to provide additional information needed by such group of customers. A message strategy using highly rational information processing approach (with high information content) would suit best for this segment.

As with all research projects, the findings presented are characterized by limitations that restrict the extent to which they can be reliably generalized. The paper is based on a research project which is still in progress and has not reported here the cluster validation procedures due to shortage of space. However, despite the limitations, the current study has provided significant insights into the nature and types shopping motives that drive consumers to shop in a different cultural context such as India. This is highly significant in the context of the recent geographic market expansion of successful retail organizations and the development of a global consumer market whereby marketers and retail brand managers are keen to learn and understand the dynamics of buying behaviour patterns of consumers of different cultural backgrounds (Jamal, 2003).

References


### Table 1: Results of Exploratory Factor Analysis

<table>
<thead>
<tr>
<th>Items</th>
<th>Factor Loadings (n=271)</th>
<th>Variance Explained</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Factor 1 – Idea Shopping</strong> (Alpha Reliability = 0.90)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>IS1 I go shopping to keep up with the trends</td>
<td>0.817</td>
<td></td>
</tr>
<tr>
<td>IS2 I go shopping to keep up with new fashion</td>
<td>0.849</td>
<td></td>
</tr>
<tr>
<td>IS3 I go shopping to see what new products are available</td>
<td>0.890</td>
<td></td>
</tr>
<tr>
<td>IS4 I go shopping to experience new things</td>
<td>0.829 11.9%</td>
<td></td>
</tr>
<tr>
<td><strong>Factor 2 – Value Shopping</strong> (Alpha Reliability = 0.89)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>VAL1 For the most parts, I go shopping when there are sales</td>
<td>0.839</td>
<td></td>
</tr>
<tr>
<td>VAL2 I enjoy looking for discounts when I shop</td>
<td>0.859</td>
<td></td>
</tr>
<tr>
<td>VAL3 I enjoy hunting for bargains when I shop</td>
<td>0.845</td>
<td></td>
</tr>
<tr>
<td>VAL4 I go shopping to take advantage of sales</td>
<td>0.849 11.9%</td>
<td></td>
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<tr>
<td><strong>Factor 3 – Social Shopping</strong> (Alpha Reliability = 0.88)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SOC1 I like shopping with my friends or family to socialize</td>
<td>0.814</td>
<td></td>
</tr>
<tr>
<td>SOC2 I enjoy socializing with others when I shop</td>
<td>0.849</td>
<td></td>
</tr>
<tr>
<td>SOC3 To me, shopping with family and friends is a social experience</td>
<td>0.836</td>
<td></td>
</tr>
<tr>
<td>SOC4 Shopping with others is a bonding experience</td>
<td>0.815 11.7%</td>
<td></td>
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<tr>
<td><strong>Factor 4 – Role Shopping</strong> (Alpha Reliability = 0.87)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ROL1 I like shopping for others because when they feel good, I feel good</td>
<td>0.735</td>
<td></td>
</tr>
<tr>
<td>ROL2 I feel good when I buy things for the special people in my life</td>
<td>0.870</td>
<td></td>
</tr>
<tr>
<td>ROL3 I enjoy shopping for my family and friends</td>
<td>0.812</td>
<td></td>
</tr>
<tr>
<td>ROL4 I enjoy shopping around to find a perfect gift for someone</td>
<td>0.859 11.2%</td>
<td></td>
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<tr>
<td><strong>Factor 5 – Adventure Shopping</strong> (Alpha Reliability = 0.84)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ADV1 To me shopping is an adventure</td>
<td>0.808</td>
<td></td>
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<tr>
<td>ADV2 I find shopping stimulating</td>
<td>0.750</td>
<td></td>
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<tr>
<td>ADV3 Shopping is a thrill to me</td>
<td>0.820</td>
<td></td>
</tr>
<tr>
<td>ADV4 Shopping makes me feel I am in my own universe</td>
<td>0.761 10.5%</td>
<td></td>
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<tr>
<td><strong>Factor 6 – Gratification Seeking</strong> (Alpha Reliability = 0.83)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>GF1 When I am in down mood, I go shopping to make me feel better</td>
<td>0.818</td>
<td></td>
</tr>
<tr>
<td>GF2 To me shopping is a way to relieve stress</td>
<td>0.845</td>
<td></td>
</tr>
<tr>
<td>GF3 I go to shopping when I want to treat myself to something special</td>
<td>0.794 8.7%</td>
<td></td>
</tr>
<tr>
<td><strong>Factor 7 – Utilitarian Shopping</strong> (Alpha Reliability = 0.75)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>UT1 While shopping, I try to accomplish just what I want to as soon as possible</td>
<td>0.760</td>
<td></td>
</tr>
<tr>
<td>UT2 While shopping I try to find just the items that I am looking for</td>
<td>0.856</td>
<td></td>
</tr>
<tr>
<td>UT3 I feel happy when my shopping trip is over quickly</td>
<td>0.792 7.7%</td>
<td></td>
</tr>
<tr>
<td><strong>Total Variance</strong></td>
<td>73.4%</td>
<td></td>
</tr>
</tbody>
</table>
### Table 2: Results of the Non-Hierarchical Cluster Analysis (n=271)

| Shopping Motivations       | Cluster 1 (Stylish Role Performers) | Cluster 2 (Highly Rationalists) | Cluster 3 (Role Oriented Bargainers) | Cluster 4 (Self Oriented Idealists) | Cluster 5 (Happy Shopping Lovers) | F-value | P <  
|----------------------------|-------------------------------------|---------------------------------|--------------------------------------|-------------------------------------|-----------------------------------|---------|------  
| Idea Shopping              | .53709                              | -1.45759                        | -.82535                              | .63435                              | .18258                            | 57.094  | .000  
| Value Shopping             | -.56831                             | -.61484                         | .49171                               | -.28630                             | .43530                            | 20.631  | .000  
| Social Shopping            | .06598                              | -.15952                         | -.50736                              | -.46444                             | .35329                            | 8.775   | .000  
| Role Shopping              | .72074                              | -.46419                         | .39677                               | -1.51290                            | .02118                            | 56.629  | .000  
| Adventure Shopping         | -.20341                             | -.30124                         | .31262                               | -.22470                             | .16595                            | 3.577   | .007  
| Gratification Shopping     | -.64865                             | -.35680                         | -.33043                              | .11973                              | .59860                            | 24.551  | .000  
| Utility Shopping           | .07013                              | 1.07551                         | -1.10124                             | -.90744                             | .38014                            | 57.546  | .000  
| Cluster Size               | 65.000                              | 29.000                          | 40.000                               | 34.000                              | 103.000                           |         |       
| Percentage of respondents (%) | 24%                                | 11%                             | 15%                                  | 13%                                 | 38%                               |         |       

Processes of EU Enlargement and Ongoing Fragmentation of its Internal Market

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Abstract

The paper deals with some experiences as gathered from our research and lecturing in the area of internal market of the EU. The general development trend in this one of the key areas of the EU has been that the bigger is its Internal market, the bigger is becoming also its fragmentation. Accordingly, the EU member states are becoming also members of various categories of members according to their role, place and functions in the functioning of the EU. The main focus of our paper is on this process as developing after the last two enlargements from the recent “old” EU-15 to the current EU-27

Introduction

Just very recently, in the end of March 2007, the EU has - with its traditional pomp and sense for magnificence – celebrated the 50th anniversary of the Rome Treaties that among others have established not only two new European Communities i.e. European Atomic Energy Community (Euratom) and the European Economic Community (EEC) but also the Internal market of the European Communities or of the current European Union. According to the same basic treaties “… the internal market shall comprise an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of this Treaty”. Originally, the same EEC Treaty has stipulated that the particular internal market has to be established within the so-called transitional period of 12 years i.e. that till 1970 the Internal market of the EEC has to be not only existing but also to be fully functional. Unfortunately, as in many other similar cases also the history of the Internal market of the current EU has not been as simple and as straightforward as it has been originally expected and signed by the EU member states heads of states, etc.. Although originally its creation had to be completed by the year 1970, even now after more than 50 years since its inception we can state that the Internal market of the EU has not been completed as yet and it is still an open question when if ever it could be completed according to the particular Article 14 (ex Article 7a) of the basic treaties as quoted above. In the following parts of this paper we will deal in more details with some aspects and/or problems that are doing the entire process of the internal market development more complex and difficult than it has been originally anticipated.

2. Some of the main problems and difficulties that have also caused the Internal or Common(?) or Single(?) market of the EU has not yet been completed even after more than 50 years since its inception

One of the first problem areas that are related to the issues of the Internal market of the EU is the problem of its name. Since its initial definition in the above Rome Treaty as an internal market there exist in the basic treaties and other official documents also another two names used for the
same purpose. So in the basic documents we could find altogether three different names for the same object, viz.:

- internal market
- common market
- single market.

Although in principle all three of them denominate the same object or entity, we could say that they at the same time have been stressing some different features of this one of the most important parts, goals and symbols of the entire European integration:

- internal market - as we have stated already above, the original definition according to the Rome Treaty on the EEC has been underlining the fact that this market is internal i.e. without any internal frontiers or borders and thus has to be existing and operating within some external borders that at the same time have also to protect this internal market against any distortions and/or an unauthorized entries from the outside of the EU. In this connection it is interesting to point out that the particular external border is not directly mentioned in the particular initial definition and legally has not been done so until year 1992.

- common market – although according to the basic Treaties there is no explicit definition of the common market, there is in the Article 3 (a)-(d), (g) and (h) of the EC Treaty stated that the common market is “…a customs union in which in addition to the free movement of goods also the free movement of persons, services, capital and payments, the freedom of establishment and undistorted competition are guaranteed…”. In this respect, the common market represents an extension of the internal market from its original four basic - or as often being marked – fundamental or constitutional freedoms to some additional freedoms that specifically mean the freedom of establishment i.e. a right to apply these fundamental or constitutional freedoms anywhere within the internal market i.e. not only e.g. in own member state but universally inside the external borders of the EU together of course also without any undistorted competition or otherwise in other words without any discrimination. This aspect of non-distortion or non-discrimination is in this context very important as it is right this fundamental and/or constitutional right that is most often not respected and most widely violated depending upon the EU member states nationality of the particular subject no matter if it is a physical or a legal one.

- single market – since of its inception more than 50 years ago in 1957, the internal market of the EU has gone through various development stages, reforms, action plans, etc. in order to accelerate to make more efficient its completion and/or practical implementation. One of the most significant in this respect has been the so-called Single European Act adopted in 1986 that has amended the particular EEC Treaty and stated also the new, more realistic deadline for the completion of the internal market by 1 January 1993. Since that time also a new term of a Single market has been introduced in order to stress and underline that within the EU there has been only one single market.

However, these legal and terminological uncertainties regarding the EU internal market still do not represent the major problem in this problem area although it is fact that on the other hand they also document how it is difficult and complicated to transfer such an important part of the European integration from the texts of treaties into the daily practice of the EU. The more important fact in this respect is the problem that even after 50 years of its development, the EU...
internal market has still not been a fully functioning reality for various reasons. Some of the most general problems in this respect have been the following ones:

- although the year 1970 has been originally defined as a target year for the completion of the EU internal market, until 1992 i.e. adoption of the Maastricht treaty on the EU there has not been defined an external border of the EU i.e. the border that as an external border has been responsible for the protection of the EU internal market. And unfortunately even until now this external border in principle has not been existing to the full of its extent and thus in some respect it has been more dividing than protecting the EU internal market. The problem is that the so-called Schengen external borders of the EU and thus also of its internal market are not fully corresponding to the actual borders of the EU and/or its member states. For example as of today in this connection we could see several paradoxes. On the one hand, not all member states of the current EU-27 are within this external borders of the EU although formally they are also integral parts of the internal market of the EU. In fact out of current EU-27 member states only 13 old EU-15 member states i.e. without Ireland and the UK are “protected by the Schengen border. It means that most of the current EU member states i.e. 14 are outside the borders of the EU Internal market although of course they are integral parts of the EU Internal market and on their “internal” borders with other EU member states are free of any customs controls but of course not of passport controls for all passengers irrespective if they are or are not citizens of the EU-27. In order the reality of the Internal market would be even more confusing, there are some non-members of the EU like e.g. Norway, Iceland that are parties to the Schengen agreement and thus enjoy also free movement of persons including their own citizens who although not being EU citizens can fully enjoy what EU citizens from the above 14 member states simply just can not?! And in order to make it even more complex, citizens of some overseas “territories” of some EU member states have also a kind of privileges regarding their free movement within the EU territory although they not meeting even the most fundamental precondition for European integration i.e. to be from or in Europe as stipulated the initial treaties regarding who is eligible to become a part of the initial European Communities i.e. “any European country can apply…”

- a mutual recognition (e.g. of goods for free movement within the EU Internal market) difficult in practice – although since adoption of the so-called “Cassis de Dijon” in 1979 has already elapsed more than 27 years, the problem of a mutual recognition of goods has been still one of the most frequent obstacles in the truly and fully free movement of goods. Most of the member states of the EU still do not miss any opportunity to protect their national market against any “unnecessary” imports and thus of course for various reasons protecting their own national producers e.g. especially in agriculture where they always find enough reasons for suspending free movement of goods on the grounds of BSE, a cow disease, a bird flu, etc.

- transposition delays – it is a problem that for various reasons the member states are “unable” to adopt and implement the community legislation into their national legislative system. Among the most frequently quoted reasons are that there is too much of EU legislation adopted too quickly and with insufficient deadlines for its implementation on the national level, administrative structures especially in the new member states are not always able to absorb so much legislation in such a short time especially because of their internal institutional, administrative and other deficiencies. In many cases there is misinterpretation of the EU legislation, what in many cases means that the national
administrations either underestimates the importance of the adoption of the EU legislation and/or they interpret it differently than it has been originally adopted on the EU level. So in many cases they use the EU legislation as a cover up or “objective justification” for achieving their narrow and selfish national interests and not those of the community significance. Especially in the case of the EU directives that enable a kind of national interpretation of the basic principles of the particular legal act it is quite common that the same directive has quite wide and different interpretation in different member states what again is to some extent distorting the functions of the EU internal market. Not to mention that it has to be not only an internal but also a common or even a single market as we have defined it above. Another and very often problem with the functioning of the EU internal market on the national level has been the problem of the enforcement of the already adopted and implemented EU legislation. In the next part of this paper we will illustrate at least some of these problems in connection with the current situation regarding the four basic or constitutional freedoms or free movements.

3. The key problems of the EU internal market regarding four basic, fundamental or constitutional freedoms or free movements – goods, services, capital and in particular of persons/EU citizens

As we have already stated above at the beginning of this paper, since its inception more than 50 years ago by the Rome treaty, the current EU internal market has to be based on four basic freedoms that as they are defined by the basic treaties have at the same time to be interpreted as fundamental or constitutional freedoms. In this respect their functions in the EU internal market are far more important and significant than some other legislative acts as we have mentioned them in the end of the previous part. Analogically as on the national level, the constitutional rights and freedoms are always above or are superseding the “ordinary” legislation. Of course that the same principles have to be respected also on the community or the EU level. As the EU has not have still its own Constitution – as we know the particular EU Constitutional treaty has not been approved in the referendum in France and the Netherlands – then the existing basic treaties serve as a part of a rather complex and not very logically organized, but still an officially adopted and ratified kind of a “constitution”.

Unfortunately, in view of the above, the current situation in the EU has still been far from the above acquired respect for and adherence to the particular basic fundamental constitutional freedoms as enshrined in the basic treaties already for more than 50 years. If we take any of these basic freedoms, no one of them could assess as a fully functioning one.

Free movement of goods

Some still existing problems in this respect we have already mentioned also in the previous part of this paper. In addition to those already mentioned above, we could add that there exist the whole range of various others that are not just simply consequences of the misinterpretation of the community law, or its delayed implementation or interpretation. There are existing distortions to the truly and fully existing free movement
of goods that are directly sanctioned - by an evident paradox – by the community legislation i.e. the same legislation that has to be in the front-fore of protection of a fully functioning free movement of goods as enacted by the basic treaties. In this respect we cannot find a better example for illustrating this paradox situation than the CAP – Common Agricultural Policy. The largest, oldest and at the same time the most expensive common policy that during the period of fifty years since its inception has completely lost any kind of objective justification for its existence. While in time of its inception in 1950s, shortly after the 2nd World War, the CAP was a common policy that had to help member states to overcome at that time still existing shortages in food supplies, in quality of food, etc. Nowadays there has not been any justification for this kind of common policy that annually has been swallowing almost the half of the total budget of the E. Moreover, this enormous financial means have been serving to a sector that has already for long nothing to do with any of the new challenges of the contemporary EU like e.g. the Lisbon strategy on e-Europe and information society, or its newer version of i2010, or problems of energy self-sufficiency, a modern life-long education, new and better jobs instead of still existing a rather high unemployment especially among some categories of the EU citizens, etc. This enormous amount of the EU budget has been still used to serve to a still smaller part of the EU population that currently achieves not more than about 5% of the total workforce and contributing to the GDP on the union level by not more than about the same share. Moreover in a long already existing overproduction of all basic categories of foodstuff. With some exaggeration we could say that currently this enormous sum of community money are used directly or indirectly by the EU itself for distortion of its own internal market! All those various subsidies and direct payments to farmers for their agricultural production or on the opposite for not producing some crops, or for liquidation of the existing production capacities like currently e.g. for closures of sugar mills, destruction of wine yards, etc. have nothing to do with any market economy and not at all with any free movement of goods, etc. Moreover, in all those various kinds of subsidies there exist relatively high differences e.g. currently between old EU-15 and new member states. The latter ones have been receiving only a fraction of subsidies (25-35%) of what has been paid to farmers from the old EU-15 member states. And this differentiation between “old” and “new” members has been so strict that it has not been even allowed to equalize these this differences from the national budgets of the new member states. It is then no surprise that an important segment of the EU internal market i.e. one dealing with agricultural goods has had totally nothing with any elementary requirements of the free movement of particular goods. And the negative consequences are already evident especially in the new member states. The prices of basic foodstuffs are no much higher than they were before they joined the EU less than three years ago., because simply most of them are nowadays not home grown but imported from the old EU member states and thus also cheaper than they could be produced by the less subsidized domestic farmers but in general more expensive for consumers as their prices correspond more to much better paid citizens of the old EU-15 countries than consumers from the new EU member states.

Some evident distortion of the current EU internal market exists also in respect of the free movement of goods across the borders between the new and old EU member states. While there have been abolished any customs check points on these internal birders
between old and new EU member states yet on 1 May 2004 when the EU has enlarged from the former 15 to then 25 member states, i.e. almost three years ago, there is still evident a kind of distortion in the free movement of goods especially from the new to old EU member states. It is enough just to travel from Austria to Slovakia or vice versa through the border crossing Berg – Bratislava and one can see those never ending long waiting cues of loaded trucks for their “free crossing of the internal border of the EU internal, common or single market”. As we have already mentioned above there is always something what has to be checked, verified or just simply something like that in that respect on that and other similar internal borders of the EU. If it is not for infected meet, then for potential illegal emigrants or if for nothing else then for the technical conditions, weight, overloading or whatsoever similar “technical or security or any other reasons”. If we take into account that in addition to the above already mentioned distortions of the current enlarged EU internal market that the free movement of goods is further distorted by various quantitative quotas in production or storage e.g. again in agriculture products or steel and other industrial products then it is clear that the current EU internal market is definitely not anything similar to the common or single market. In fact within the current EU internal market due to its above ongoing fragmentation there exists several partial internal markets for free, less free or more free movements of goods. If we take again only the sector of agriculture as an example we could see that there exist several segments of the EU internal market as e.g. one consisting of old EU-15 member states with high subsidies, completely free movement of goods, etc. Then there exists a relatively separated segment of the EU internal market consisting of 10 NMS with less generous subsidies but various restrictive quotas that do not exist e.g. in the EU-15 as e.g. regarding production of sugar (all “redundant” production capacities in that respect have been recently eliminated in the NMS but on the other hand generously compensated from the EU funds to their foreign owners), beer, but also in the segment of energy, steel, etc. And then there is the newest segment of EU internal market consisting of the latest entrants of Bulgaria a Romania that are now in the stage of the same subsidies as previous 10 new entrants were in year 1994.

Also from this rather brief analysis of the ongoing fragmentation of the EU internal market it is quite evident that as for free movement of goods it is neither common nor at all a single but more and more fragmented internal market. Nothing in this respect could be changed by the fact that the CAP is officially exempt from the EU internal market where any unfair competition, excessive state aid, subsidies, quotas, etc. are strictly prohibited by the community legislation, etc.

Free movement of services

In principle the same problems as we have listed them in the previous part in connection with the “free” movement of goods could be t the same extent applied also in the case of the second fundamental or constitutionally provided and/or by the basic treaties provided a free movement of services. Again as in the case of the free movement of goods there exist an ongoing process of fragmentation of the common internal market as a consequence of the ongoing and especially the latest two enlargements of the EU from the original EU-15 to EU-25 and quite recently to the
current EU-27. In principle there are again at least two segments of the common EU internal market i.e. one consisting of the old EU-15 countries that in principle have in fact an existing free movement of services within all 15 member states. However, again completely different situation exists regarding services provided by the entities from the EU NMS. The most vivid and most famous case in this respect has been the enormously publicized case of a “Polish plumber” who just because has offered his services in plumbing promptly on the spot and for much more reasonable price than his French counterparts has become a symbol of an unacceptable danger from the East destroying labour market, taking jobs to local experts and specialists, etc. Not surprisingly he has become a symbol of the anti-campaign against the Draft of the Constitutional treaty that has finally been not approved in the referendum in France and subsequently also in the Netherlands and thus sending not only the particular treaty but also the entire EU into the deepest crisis never before existing. And the entire case is just nothing more or less than a practical example of application of one of the basic constitutional freedoms of movements and rights of citizens in practice. Nothing more than an attempt to fully utilize all the potential of the EU internal market in the free movement of services that on paper has been existing nowadays already for more than 50 years! Unfortunately, the “Case of Polish plumber” has not been the only, although the most publicized symbol of the ongoing fragmentation of the EU internal market in its segment of free movement of services. Many more other examples could be brought up regarding e.g. various restriction against service providers from the NMS in the area of truck services, taxi services (taxi drivers from the NMS are e.g. not allowed to offer their services in the old EU-15 member states even in cases when their first leg service has been carried out from the territory of the NMS to the territory of the old EU-15 member state?! However, on the other hand, there exists some exemption also in this respect. If one happens to provide nurse services in hospitals, or for elderly, or happens to be providing certain ICT related services, then there are no restriction for providers of them in the old EU-15 member states even by nationals from the NMS. And of course, so far there are no existing any such exemptions for service providers from the countries of the latest two entrants to the EU.

In summary to this part we could again just to state that the EU internal market in its segment of free movement of services has again been fragmented into several relatively isolated parts strictly according to the three basic categories of the EU-27 member states i.e. old 15, new 10 and the newest 2. Or otherwise, the current EU-27 internal market in the area of free movement of services is not common or single or on the other hand in fact as fragmented as it suites to the needs or preferences of the old EU-15 member states! One only can wonder where in this case are all those proclaimed basic principles of the European integration on mutual respect, benefits, assistance, solidarity between EU member states of course also old and new ones!

Free movement of capital

In principle this kind of free movement is relatively less controversial or fragmented within the current EU-27 internal market than in the case of the three other of them. But
again after the last enlargements also in this respect we can witness some fragmentation tendencies of the EU internal market especially again along the lines or internal borders between the old EU-15 and NMS respectively. In principle there exist at least two tendencies towards its fragmentation and they are:

- regarding the common European currency – Euro
- in the capital flows in the form of FDI

As for the common European currency – Euro the last two enlargements have substantially changed the position of this “common currency. While within the old EU-15 all but three member states (Denmark, widen and the UK) have switched to this new European currency, after the last two enlargements out of the total of EU-27 member states only 13 i.e. less than half of members have been using this “common” currency. It is quite evident that this problem is not only a technical one but has also many very practical adverse effects on the free flow of capital especially again between the old and new member states as of 12 new members only one (Slovenia) has already qualified to the Euro zone. And quite logically those more negatively affected in this fragmented capital movement are those NMS that have not yet met the particular Maastricht criteria as prescribed by the Maastricht treaty on the EU for eligibility of the country to become a part of the new Euro zone within the EU. As in various other areas also in this respect exists some differentiation between the old and new member states. While in the case of original old EU member states the consideration of the readiness of the country to join the Europe zone has been more than generous (except perhaps of Greece) and most of the countries even until now have never met the particular Maastricht criteria. In many cases it was enough just to show the so-called some positive development tendency in the particular criterion and the country was approved for joining the Euro zone. Thus it happened that among the first Euro countries have been approved also at least two countries that have exceeded the total debt Maastricht criterion of 60% of the GDP by more than 100% on the levels of over 120%. Until now their all the positive development tendency in meeting this one of the fundamental four criteria has improved to not more than to around 110% what has been still almost the double of the required threshold of 60% of the GDP. And since introduction of Euro almost a decade ago, many Euro zone member states are unable to meet various Maastricht criteria especially those on the budget deficit on the level of 3% of the GDP. And what was the result? The particular countries instead of being punished according to the treaties have managed that the particular articles of the Maastricht treaty have been adjusted in such a way that there has not been any punishment at all. In order the paradox with the particular criteria for introducing Euro would be even bigger, it has to be mentioned that Euro has been used also by the countries that have never had or never will have to meet any such criteria and are not even EU member states as e.g. Montenegro, Province of Kosovo, but also all various tiny neighbours of the EU like e.g. Vatican (even being allowed to mince its own Euro coins?!), San Marino, Monaco, Andorra and of course also again various overseas departments of some EU member states. On the other hand some of NMS that have already met the particular Maastricht criteria and/or are much closer to meeting them than some of the existing Euro zone members have not yet been allowed to join the Euro Club as reputedly they are not-yet-ready to meet all the necessary criteria?! In any case the Euro common currency so far has been more dividing, further fragmenting the EU-27
internal market than making it more common or single as it has been its main objective and also undisputed potential

As for capital flows in the form of FDI, these flows are so far much more one way flows from the old EU-15 members to NMS than anything else. In principle it could be a positive trend as it is one of the ways how to more equality and cohesion among the old and the new EU member states. But again, in many cases these FDI are more dividing and fragmenting the EU internal market of the EU than unifying it. The main reason is that the foreign investors very soon discovered that for various historical but also other development trends, the cheap NMS are the best place for placing in them various productions and activities that are less sophisticated, requiring less qualified workforce, less value adding so in this respect the particular gap between old and new members of the EU has been rather widening than narrowing. While sectors and activities related to the latest ICT applications, R&D, etc. have been mostly placed and/or remained in the old EU-15 member states various laborious, hazardous or environmentally more risky productions have been placed in the new member states for the overall costs being just a fraction of the costs required in the old EU-15 countries. The typical example is a recent incident with huge explosion in a plant in Slovakia where semi-qualified workers have been dismantling obsolete ammunition for the monthly salaries on the level of only 200-300 Euro per month?! In case of more attractive productions like e.g. car industry, the foreign investors have expected such locally provided incentives that in many cases raised the total costs for creation of one job to several times multiplied expenditures than have been normally needed or offered to local employers, etc. Not to mention various other direct perks to the foreign executives, managers or even ordinary specialists like accommodation in newly built villas, free air transport, education of their children in foreign language schools, recreational facilities, etc. In some other cases as e.g. in case of privatization of banks through foreign banks has required the incoming FDI required such “preparatory” national investments into the “cleaning” process of their portfolio from bad loans (it is quite interesting that there was no much effort to find out who was behind those “bad loans” that again their final sale to foreign investors has been just a clean loss for the particular new member state and especially its citizens who have been the largest losers from all these processes of privatization, rationalization, modernization, etc. through so often over heralded FDI. They are again contributing more to the fragmentation of the EU internal market to its high tech segment in the old EU member states and its low tech portion in the NMS than to its integration towards a truly and fully common or single market of the entire EU. What is in this overall FDI flows most remarkable, it is the fact that in spite of all problems with them there is one significant development trend. The outflows of profits, dividends and various other benefits for foreign investors have been permanently growing. While for example in the case of Slovakia just ten years ago the total repatriation of dividends has been only about 10 billion Slovak Koruna (1 US$ is currently about 25 Sk) in just finished year 2006 it has been over 70 billion Sk what is almost the same amount as the total amount of the incoming FDI into the country for the same year?! Hence, the free flow of capital between the old and new EU member states has had really some unwanted and unpleasant consequences not being in line with the principles of mutual benefits, solidarity, assistance, etc.
Free movement of persons

All the above distortions of the EU internal market regarding its fragmentation due to problems with the free movement of goods, services and capital have negative impact on overall functioning of the EU, but this last fourth free movement being also guaranteed directly to the citizens of the EU by the basic treaties has even more damaging effect. It is simply because of its nature. Although all three previous free movements have negative effect on the overall functioning of the EU and thus finally negatively effecting also each and every citizen of the EU, but most of them are not so directly effected by some problems in the free movement of goods, services or capital as most of them neither exporters nor importers. Most of them are not providers of various services and even less they are involved in the free movement of capital. After all, none of these free movements belongs among the fundamental human rights guaranteed by the most universal act of international law. By their substance they belong to the responsibility of various specialized UN and/or other international agencies like WTO, World Bank, IMF, UNCTAD, etc. However, the free movement of persons on the other hand belongs among the fundamental human rights i.e. something what has been guaranteed to every human being irrespective of what is his/her nationality, gender, race, social or marital status, religion, etc. as it is expressed also by their character – they are universal and as such they belong to all people without any restrictions, necessity to claim them, etc.

In view of this its universality it is then absolutely unacceptable that a part of the EU citizens has been deprived of this kind of one of fundamental human rights as it has been currently in the case of the EU citizens from the NMS.

Due to the above universality, there is no legal way that any human being could be stripped of this right. No national or international act of law, treaty, agreement can have that effect even in case if the particular citizens would “voluntarily” agree with that. In view of this universality it is then no surprise, that the citizens of the NMS are very sensitive about any restrictions imposed over them regarding their free movement within the EU territory i.e. territory of the Union of which they are also “full fledged” citizens with otherwise all the same rights and obligations as they belong to the EU citizens from the old member states. In view of this, any restrictions imposed in this respect over them by the accession treaties that among others have introduced also the so-called transitional period in this respect with the total length up to seven years i.e. till year 201. Especially, for the citizens of the EU from the former ten socialist countries this restrictions regarding free movement of persons has been clearly seen as their totally unacceptable and unjustified discrimination. Basically they see it as a kind of the same continuing unjustified discrimination they were subjected during their former totalitarian communists regimes when right the restrictions on travelling abroad (i.e. to the West) had been seen as one of the biggest deprivations. And by the certain paradox, the same countries that for decades were encouraging citizens of the former socialists countries to get rid with their totalitarian regimes nowadays are doing the same what those undemocratic totalitarian, dictatorial regimes?! It then no surprise that in the first ever elections into the EP the turnout of electorate was in some NMS on the level of the historical lowest levels of only e.g. 16% in the Slovak Republic. That is just a result of
their frustration in this respect. They have become citizens of the EU but only of the second category. The EU citizens from the NMS are now also holders of the EU passports but that passport does not help them much in their free movement as guaranteed to them not only by the basic EU treaties but also by the UN Universal human rights, by the Council of Europe etc. Basically, within the EU they do not need the EU passport as an ID card is enough – but in the most of the old EU-15 member states they can till travel only as tourists on the same grounds as citizens of various other countries from the outside of the EU. And outside the EU, their new EU passport also do not help them as their visa and other related statuses are depending upon their national passport or citizenship and definitely not on their EU passport or citizenship.

In principle we could say, that the current situation in the free movement of persons as in one of the “constitutional” freedoms has created such a situation that the citizens of the EU are nowadays divided into at least the following eight categories of citizens:

- citizens of 14 old EU member states that have a complete free movement not only within the Union but also outside
- citizens of one old EU member states, notably Greeks have some restrictions regarding travel abroad e.g. to the USA where they as only citizens of the old EU-15 countries need visas
- citizens of the 10 NMS have limited free movement within the EU-15 member states where they fully depend upon the generosity or non-generosity of the particular EU member states. For example the UK, Ireland, Finland have opened their labour market to them without any restriction since their entry into the EU. All other old member states are opening it at their will as they like and/or need migrant workers from the East e.g. according to some professions, etc. This “pick-up” or “a la carte” system of opening their national labour market is even more discriminatory than in case that the country has not opened its labour market at all as it makes of the NMS just a source of wanted or unwanted labour! In this case the EU failed to achieve at least that little for its citizens from the NMS that no country could choose what categories of professions they will accept or not. The minimal equality of the citizens requires a consequent principle of either all citizens or none of them as otherwise the current system is a double discrimination!
- Moreover, also in the old EU-15 countries that have opened their labour market for citizens from the NMS, the situation of these new workers is not an ideal one. Although in principle the EU rules and legislation on the equality, equal workers rights, benefits, etc. has been formally guaranteed, in practice there are various kind of hidden discrimination. These workers have e.g. an equal pay as their counterparts but mostly it is not according to their qualification but because of their initial language deficiencies they are assigned to mostly menial jobs of servants, janitorial staff, etc. so they pay is equal with semi-qualified immigrant workers from the third countries, etc. In this connection it is again a big question, what for exists the portfolio in the European Commission with responsibility for education and multi-languages, etc. If Canada or Australia are able to provide a
language preparation for their immigrants for free why the EU is not able to provide the same for its own citizens within the EU itself?!

- Citizens from the last two NMS i.e. Bulgaria and Romania do not have any opened labour market in any of the old EU-15 member states

- Although the EU as also all international organization are very active in protection of national minorities, there are minorities in the current EU-27 that although formally they are eligible to be citizens of the EU as they were born on the territory of the particular member states and have permanent residence in the member state they are not eligible to become citizens of the particular member state e.g. because they do not pass test in the official language of the particular country?!. On the other hand there are citizens of other EU member states that do not speak the language of the particular member state but they are citizens of that state. Hence it would be necessary to have a common Union rules and regulations that would clarify this kind of issues and problems with citizenship, minority status, etc. There are still big differences existing also between old EU-15 member states e.g. between France and the FRG,

- Another problems with the free movement of persons exists between Schengen and non-yet Schengen member states. By a certain paradox (unfortunately not unusual in the European integration) in some case non-citizens of the EU but citizens of the Schengen have more rights for the free movement of persons and free right for establishment than it is in the case of the EU citizens from the NMS. Similarly, also in some EU member countries immigrants from their former colonies have more favourable treatment than citizens from the EU NMS, etc.

In this list of problems and weaknesses in the current free movement of persons within the EU we could continue further on but we suppose that for illustration we have brought up enough examples that call for a very fast and efficient solution in this one of the principal human rights also for the citizens of the EU irrespective if they are citizens of the old or new EU-27 member states. There should be no discrimination whatsoever and this constitutional right of the EU citizens has to be guaranteed directly by the EU institutions and not being left in the hands of the national administrations of individual member states. Otherwise, could happen again very soon that in the next elections into the EP in year 2009 the turnout of electorate will achieve another new historic record in the low level of those who will exercise their right to vote. The solution of the free movement of persons strictly according to the basic treaties could bring the EU closer to its citizens than all various existing campaigns, slogans, declarations, etc.

4. Conclusions and recommendations

As we have stated in the previous parts of this paper, in spite of the fact that the EU internal market has just very recently celebrated its 50th anniversary, there has still been a lot of work needed in order to bring it into line with the provisions of the basic treaties. The existing and to some extent continuing fragmentation of the EU internal market requires a more consequent approach than it has been so far. Especially it is needed to increase the role of EU institutions in the entire process of the EU internal market development in particular the European Commission has to act in the protection of the
EU internal market more strictly according to the basic treaties and without taking into account if that or other group of member states has some other national priorities, etc. Otherwise, it could happen very soon that there very soon will be no internal common and single market of the EU but only a rather inconsistent gathering of individual and fragmented national markets or their sub-regional groupings.

References


Credit Crunch in Thailand and After the Economic Crisis: Myth or Reality?

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Abstract: It is widely speculated that Thailand witnessed a credit crunch situation after its severe economic crisis in 1997. In this paper, we study the prevailing dispute regarding existence (or lack of it) of credit crunch after the 1997 economic crisis. The results of the analysis using both macro and micro level data do not support this existence. The Micro level data includes fourteen industries enlisted under the Stock Exchange of Thailand (SET). The results show that credit extension just changed its form from short-term to long-term. Both exporting and non-exporting industries had the similar pattern in this regard. The paper recommends revision of leverage studies which were based on assumption of existence of credit crunch in Thailand.

1. Introduction

A credit crunch is generally defined as a decline in the supply of credit when lending rate is not immediately adjusted with banks lending willingness. According to US Council of Economic Advisors (1991), a credit crunch is “a situation in which the supply of credit is restricted below the range usually identified with prevailing market interest rates and the profitability of investment projects” (Quoted by Ding, Domac, and Ferri [1998]). It means that credit crunch is a disequilibrium situation where lending rate is not at the intersection of the demand and the supply curve of credit. Theoretically, for tightened monetary policy, the equilibrium shifts to another point where a reduction in loan is observed for an increase in the lending rate. This is not a sufficient evidence for credit crunch. In credit crunch situation, credits are rationed to the borrowers irrespective of their credit worthiness. The fall in actual credit to the private sector may reflect declining demand for credit, contracting supply, or both. It is thus the demand and the supply level of credit that determines the existence of the credit crunch.

Historically, credit availability to Thai firms from banking sector, observed a systematic cyclical variation except a sudden credit decline after the 1997 economic crisis in Thailand. Subhaswasdikul and Nakornthab (2003) examined 50 years of credit history from 1953 to 2001 using detrended ratio. It shows that a credit cycle has started since 1988 when the Thai economy embarked on a spectacular growth path. Compared to all the cycles in the past, the present cycle had a different nature in its variation. The
previous growth in the credit never went below 5%, while it is observed negative during 1998. The other phenomenon such as private credit to GDP ratio, which was sharply increasing during 1992-97, saw a sharper decline afterwards. These evidences do not support a symptom of an end of the present cycle. The decline in the credit thus raises a question if it is caused by the credit crunch after the economic crisis.

Most studies related to use of leverage post-crisis in Thailand were built on the assumption of existence of credit crunch. In these studies, credit crunch was simply defined by the declining credit level. Validity of these studies is in question if credit crunch were actually not in place. This study investigates if credit crunch actually occurred based on the accepted definition. The study also identifies its magnitude and the way it was transmitted to the Thai firms if there was any credit crunch. The study finally investigates the policy mechanisms by the banks that managed or bring down the outstanding credit at the point of the crisis.

2. Literature Review

A number of researchers have investigated the credit crunch situation immediately after the 1997 economic crisis in Thailand. The studies could be divided mainly into three categories. Some studies investigated only the borrowers’ demand side, others investigated only the supplier’s ability and intention to extend credit, and the rest used both demand and supply sides of the credit. These studies consequently reached to different conclusions.

Dollar and Hallward-Driemeier (1998), whose study was based on corporate survey of more than 1200 firms in Thailand, reported that firms’ demand for borrowings declined after crisis and hence the connection between the declining credits with credit crunch was highly dubious. Despite the large devaluation, even large exporters were operating at lower capacity in the first half of 1998, compared with a year earlier. Firms producing for the domestic market were in worse shape.

Ding et al. (1999) measured credit crunch by means of some key monetary and credit variables and found no evidence of credit crunch in Thailand. They claimed that for credit crunch to occur there must have reduction of credit growth and a widening spread between the lending rate and the risk-free rate. However, due to inadequate data, they used some proxy indicators to come to the above conclusion. They observed that investors’ confidence, measured by stock market index declined from January 1996 to January 1998. Industrial production declined drastically and registered a year-on-year growth of -13.7% in February 1998. These two variables indicate a possibility of reduction in loan demand. However, domestic credit growth showed an opposite trend during the same period, indicating that loan that was received by the borrowers were not for the purpose of future investment or production, but it was for prevention of further increase in non-performing loans. The evidence of no credit crunch in Thailand was further supported by the fact that spread between prime lending rate and the risk free yield shrunk after the crisis.
Ito and Pereira De Silva (1999) examined the supply side of credit by surveying seven Thai private and ten foreign commercial banks to know about their ability and willingness to extend credit. The study found strong evidence of a credit crunch immediately after the crisis. The conclusion was based on two necessary conditions and three sufficient conditions. It found that the two necessary conditions - a severe cut in lending and a hike in interest rates – were observed after crisis that implies a shift in the bank loan supply function. The study also found that exporters who were expected to benefit from depreciation were restricted in their access to bank lending as well. Large banks had capacity to lend but they lacked willingness to lend as they had a preference of higher liquidity and lesser risk in investment. These banks preferred buying FIDF (Financial Institutions Development Fund) notes, relatively risk free and liquid assets, from Bank of Thailand (BOT). Smaller banks on the contrary had very low lending capacity. They obtained loans from BOT from their FIDF proceeds, as part of their survival. The study further identified that most commercial banks were unable to evaluate the risk to extend credit particularly after crisis. Information related to the credit worthy borrowers was not complete.

Kotikula, et al (2001) projected the existence of Thai credit crunch post-crisis based on credit supply and credit demand pre-crisis. Their result shows that the path of the credit supply and credit demand takes turn in dictating overall credit post-crisis. Specifically, they found that supply of credit was a significant constraint in the fourth quarter of 1997 and the demand of credit became a significant constraint during 1998-1999. Demand dropped this time because of high interest rate and tight fiscal policy prescribed by IMF (International Monetary Fund). The above evidence does not show a clear picture of credit crunch in Thailand.

More recently, Subhaswadikul and Nakornthab (2003) employed both demand and supply functions to investigate the root cause of bank lending contraction after crisis in Thailand. The study found an existence of credit crunch. More specifically, it found that the decline in the estimated credit supply function preceded the decline in estimated demand by about three months. However, from the second half of 1998 onwards, both estimated demand and supply appeared to be more or less moving together.

The literature therefore varies in their findings with respect to the existence of credit crunch in Thailand. Moreover, Agenor et al. (2000) mentioned that the survey-based studies are less reliable in measuring credit crunch. They argued that having acknowledged or anticipated tight credit supply, firms tend to reduce their demand for their loans. Thus, the observed reduction in credit growth is resultant of the firms demand and consequently it does not reflect any credit crunch. The following section verifies the credit growth for the overall situation and it examines if that conforms to the available dataset from Stock Exchange of Thailand (SET).

3. Indicators of Credit Crunch

According to the Keynesian view, bond, money, and bank loans are perfect substitute. In this view, effect of monetary policy is transmitted to the demand for money or bank loans
through a single bond interest rate. An expansionary monetary policy reduces bond interest rate that leads to less bond and more money or bank loans available in the market. In this view, commercial banks or economic activities do not play any direct role for the bank loans. Bank loans are affected by the policy of the central bank.

A new credit view, introduced by Bernanke and Blinder (1988), opposed the Keynesian view by arguing that bond and bank loans are not perfect substitute. The imperfect substitution causes bank loans not obtained directly with the expansion of money supply. Economic activities work inside the channel of the loan transmission. After facing a monetary policy stance, commercial banks allocate loans to firms through assessment of lending risk. Thus, credit instruments available to large firms are different from those available to small firms. In this view, two channels, namely balance sheet channel and bank lending channel, are recognized through which loans are transmitted to firms.

In balance sheet channel, with an increase in money supply, balance sheets of the borrowing firms get affected by the increase in the equity price or net worth. This reduces the problem of distinguishing good risk borrower from bad risk borrowers and lenders difficulty to monitor the borrowing firms before making a loan.

In bank lending channel, as the money supply increases, bank deposit also increases, which in turn increases the lenders’ lending capacity and encourages more loans.

Considering the two views, the second view is more appropriate for analyzing credit in the context of 1997 economic crisis in Thailand. The effect of the crisis changed borrowers’ net worth by a decline in the profit and assets and that increased risk premium perceived by the lenders. The crisis also brought a change in the bank lending channel by a shift of the depositors and banks to Government securities, which are relatively risk-free. The balance sheets of the banks were also affected by the increase in total amount of loan in local currency due to devaluation and non-performing loans after crisis.

Based on the definition of credit crunch and the two credit channels above, it reveals that severe cut in lending is a necessary condition for credit crunch but it is not sufficient to prove the occurrence. The cut in lending only reflects the bankers’ lending channel or the supply side of the credit alone. To examine the strengths and weaknesses of the borrowers’ balance sheet, we require additional indicators

### 3.1 Necessary Condition

**Credit Slowdown:** It is the credit supply schedule by the private commercial banks, when the credit demand schedule of the private firms is constant. Wide range of interest rate or any non-price mechanism such as bankers’ asymmetric information about the borrowers’ investment situations may cause slowdown of credit.
3.2 Sufficient Conditions

SET (Stock Exchange of Thailand) Index is affected by the value of common stocks, which in turn is based on market performance, and the forecast of the company performance. The index affects credit demand both positively and negatively. SET index reflect a better company outlook and hence it has a positive impact on credit demand. On its negative side, higher index value gives firms a better opportunity to tap equity financing and reduces credit demand.

Lending Rate (LR) refers to the interest rate at which a lending commercial bank charges its borrowers on loans. There are three lending rates in Thailand depending on credit worthiness of the borrowers. International Financial Corporation (IFC) reports only one rate by averaging the rates. Higher LR is expected to motivate the lenders to lend more, while it apparently causes lesser demand for the loan from the corporate sector. Hence a rise in the lending rate with the declining supply of credit is a sufficient condition for credit crunch.

MPI (Manufacturing Production Index) is the indicator of actual production level in the manufacturing sector computed by Bank of Thailand by surveying about 255 producers each year. Higher MPI indicates firms’ ability to pay their debts. It is thus assumed that higher MPI caused firms to have higher demand for credit and obtain more credits. However, higher MPI may also provide better motivation to managers for obtaining retained profit and other non-bank loans. In that case MPI may be insignificant with credit demand.

Inflation is a general rise in the price levels of goods and services that arises due to stronger force of demand or higher production costs. A sharp rise on inflation causes volatility in the production level and poses problems on the demand for the credit. It is expected that in this volatile situation, producers demand for credit will be higher to produce more to meet consumers’ demand or to meet increased expenses for production. The relationship between inflation and credit demand resulted in negative sign for Indonesia and Korea (Ghose and Ghose, 1999) and positive in the case of Thailand (Subhaswadikul and Nakornthob, 2003) without being statistically significant in either case. In Thailand, the inflation rate is measured from changes in the consumer price index, which is a weighted average of prices of goods and services regularly consumed.

4. Credit Crunch Evidence from Macro Level data

Table 1 presents the aggregate credit data extended by the commercial banks and international banking facilities (IBF). It shows that there had been a slowdown in the growth of the credit extension since 1998. Total loaned amount went up in 1997 as foreign currency borrowings got affected by the higher exchange rate. BOT Literature shows that finance companies stopped lending almost completely from June 1997. Commercial bank’s overall bank lending increased only marginally. IBF loan in dollar
volume also contracted from 27.6% growth in 1996 to -3.1% in June 1997. Data also shows that the loaned amount took a positive turn in the year of 2002 onward.

Table 1: Overall Credit Extension in Thailand, 1992-2003

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Credit including loans from IBF (Million Baht)</th>
<th>Percentage Change from Previous Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>1992</td>
<td>2,182,358.7</td>
<td>-</td>
</tr>
<tr>
<td>1993</td>
<td>2,671,117.5</td>
<td>22.4</td>
</tr>
<tr>
<td>1994</td>
<td>3,457,707.3</td>
<td>29.4</td>
</tr>
<tr>
<td>1995</td>
<td>4,250,824.5</td>
<td>22.9</td>
</tr>
<tr>
<td>1996</td>
<td>4,855,687.5</td>
<td>14.2</td>
</tr>
<tr>
<td>1997</td>
<td>6,059,956.0</td>
<td>24.8</td>
</tr>
<tr>
<td>1998</td>
<td>5,238,683.8</td>
<td>-13.6</td>
</tr>
<tr>
<td>1999</td>
<td>5,132,804.5</td>
<td>-2.0</td>
</tr>
<tr>
<td>2000</td>
<td>4,606,297.2</td>
<td>-10.3</td>
</tr>
<tr>
<td>2001</td>
<td>4,309,360.3</td>
<td>-6.4</td>
</tr>
<tr>
<td>2002</td>
<td>4,613,564.0</td>
<td>7.1</td>
</tr>
<tr>
<td>2003</td>
<td>4,746,808.6</td>
<td>2.9</td>
</tr>
</tbody>
</table>

Note: Loans from IBF are in US Dollar, which has been converted into Baht by the exchange rate of the corresponding year.

Source: Bank of Thailand

Pearson’s Correlations are presented in the Table 2 to show the strength of relationships between the credit extension factors and total credit extended by banks to the corporate sector during 1992-2003. The result shows that all the factors except the lending rate have significant correlations with the total credit extension. The negative correlation between the SET index and the credit extension puts an idea that there was high credit availability during low SET index after crisis. But this notion does not hold true if the extension is seen post-crisis.

Table 2: Correlations between Credit Extension Factors, 1992-2003

<table>
<thead>
<tr>
<th>Factor</th>
<th>Correlation with Total Credit Extended</th>
</tr>
</thead>
<tbody>
<tr>
<td>SET Index</td>
<td>-0.546**</td>
</tr>
<tr>
<td>Lending rate</td>
<td>-0.052</td>
</tr>
<tr>
<td>MPI</td>
<td>0.586**</td>
</tr>
<tr>
<td>CPI</td>
<td>0.805**</td>
</tr>
</tbody>
</table>
In the subsequent analysis, the total credit has been transformed into a basis of 100 with 1995 as the base year with a view to contrast the movement of the two indexes over the year. BOT measures most of the indicators based on 1995. Figure 1 shows that after the 1997 economic crisis, both the SET index and the supply of credit was decreasing and they did not take a positive turn until 2001. The falling index indicates a bleak picture of the firms during the period. Dollar’s (1998) survey supports the fact that firms at this time were underutilized heavily and they had less demand for loans. However, the supply was also constantly declining during 1997-2001. Consequently, SET index does not provide a sufficient evidence for credit crunch after crisis.

![Figure 1: Credit Index and SET Index (1995 = 100)](image)

Relationship between lending rate and credit supply is statistically insignificant (Table 2), indicating credit availability did not depend on the lending rate. After crisis there was a tightened monetary policy for which lending rate was relatively higher. Thereafter the rate declined after the policy was eased. However, the supply of credit continued to decline for the period (Figure 2). It shows that after crisis both the demand and supply of loans were decreasing. Hence, it provides no evidence of credit crunch.
The positive correlation between MPI (Manufacturing Production Index) and credit supply has been observed significant in Table 2. The pattern reveals that both MPI and the credit index had increasing trend before the year 1996 and after the year 2001. However, during the crisis years and immediately thereafter MPI was increasing and the loan supply was decreasing (Figure 3). It indicates that after crisis, both demand and the supply for loans declined showing no evidence of credit crunch during the period. The increasing MPI after 1998 is expected to have higher demand for loans. But actual demand for bank loan declined after 1998 and it was substituted by equity financing. A recent survey of manufacturers by Bank of Thailand supports the argument by the finding that many firms form their capital by retained earnings and non-bank loans after crisis (Subhaswadikul and Nakornthob, 2003). Consequently, a lower demand and a lower supply for a bank loan after crisis do not show any evidence of existence of credit crunch.
A positive significant correlation between CPI and credit index indicate higher credit availability during high inflation after crisis (Table 2). But the pattern of relationship between the two variables as seen in the Figure 4 does not say so. Inflation is seen to have increased constantly over the years. It causes an expectation of higher credit demand. But the decline in the credit immediately after the crisis indicates that inflation does not really affect the demand for the credit. The decline of credit supply after crisis is not transmitted through the inflation channel and it is consistent with the findings in Thai context that found no statistical relationships. Thus there is no sufficient evidence of credit crunch in Thailand.

With the devaluation after crisis, exports were supposed to lead the way to recovery. In fact, after growing robustly in the second half of 1997, exports in dollar terms stagnated in the first quarter of 1998. Many exporting firms were running under capacity and had low demand for the bank loans. Bankers’ were also unwilling to lend to these firms despite several exports guarantee facilities by the Government. Most banks preferred giving loans to the FDIF and money markets, which pay higher interest than government-backed export loans and carry less risk. Since Thai banks became more unwilling to give money to Thai companies, foreign banks were not so enthusiastic about issuing and accepting Thai letters of credit.

5. Credit Crunch Evidence from Sampled Firm Data

5.1 Description of Sample

The data for this study was obtained from the CD-ROM produced by the Stock Exchange of Thailand (SET). The study includes firms from 14 industries, namely Agribusiness,

There are several views on when exactly the Thai financial crisis set in. We take the year 1997 as the one when the crisis started (Tower, 1997; Tirapat and Nittayagasetwat, 1999). The first balance sheet after the crisis is the one as at 31st December 1997.

Table 3 shows the number of firms from each of the 10 years in our sample. The changes in the number of firms across years have been either due to new firms being listed or existing firms being delisted.

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Firms in</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Previous Year</td>
<td>-</td>
<td>152</td>
<td>170</td>
<td>191</td>
<td>203</td>
<td>218</td>
<td>218</td>
<td>212</td>
<td>197</td>
<td>189</td>
</tr>
<tr>
<td>Number of New</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Firms (+)</td>
<td>19</td>
<td>22</td>
<td>13</td>
<td>16</td>
<td>2</td>
<td>1</td>
<td>-</td>
<td>1</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Delisted (-)</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>2</td>
<td>7</td>
<td>15</td>
<td>9</td>
<td>5</td>
<td></td>
</tr>
<tr>
<td>Total Firms in</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Present Year</td>
<td>152</td>
<td>170</td>
<td>191</td>
<td>203</td>
<td>218</td>
<td>218</td>
<td>212</td>
<td>197</td>
<td>189</td>
<td>185</td>
</tr>
</tbody>
</table>

Source: Adapted from SET CD-ROM Data

Though the number of firms varies between 152 and 218 across the years, our sample includes 218 firms. Average bank loan is based on the formula:

\[ \sum_{i=1}^{218} BankLoans \]

Thus, the averages of bank loans for some firms may be based on less number of years of data than for other firms. This method was adopted to ensure inclusion of as many firms as possible in our sample. The alternative of choosing only the firms for which data is

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2 This sector covers firms that are not included in the total of 30 sectors in the SET and they include businesses related to manufacturing, procurement, import, export, and distribution of stationary goods, wastewater treatments, and tannery.
available for all years would have reduced our sample to 118 firms. Balance sheets of all sample firms were taken as at December 31.

5.2 Credit Crunch Evidence

Comparing the above credit situation between the sampled firms of the Stock Exchange of Thailand and all firms in the national level show a similar picture in the slowdown of the credit (Table 4). The decline in the credit is observed in 1998. Data in this study has been selected based on the fact that effect of the crisis was up to 2001.

Table 4: Average Total Bank Loan and Equity for Each Sampled Firm, 1992-2001 (Million Baht)

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Bank Loan</th>
<th>Bank Overdraft</th>
<th>Long-term Loan</th>
<th>Retained Earnings</th>
<th>Owners’ Equity</th>
</tr>
</thead>
<tbody>
<tr>
<td>1992</td>
<td>942.1</td>
<td>470.2</td>
<td>471.9</td>
<td>384.6</td>
<td>1,042.8</td>
</tr>
<tr>
<td>1993</td>
<td>1058.7</td>
<td>546.3</td>
<td>512.4</td>
<td>380.9</td>
<td>1,143.9</td>
</tr>
<tr>
<td>1994</td>
<td>1250.6</td>
<td>629.5</td>
<td>621.1</td>
<td>439.6</td>
<td>1,303.0</td>
</tr>
<tr>
<td>1995</td>
<td>1836.4</td>
<td>816.8</td>
<td>1019.6</td>
<td>471.4</td>
<td>1,579.8</td>
</tr>
<tr>
<td>1996</td>
<td>2189.8</td>
<td>979.1</td>
<td>1210.7</td>
<td>455.2</td>
<td>1,629.0</td>
</tr>
<tr>
<td>1997</td>
<td>3543.7</td>
<td>1516.2</td>
<td>2018.0</td>
<td>-976.2</td>
<td>1,107.8</td>
</tr>
<tr>
<td>1998</td>
<td>2429.5</td>
<td>1423.4</td>
<td>1006.1</td>
<td>-781.0</td>
<td>1,524.7</td>
</tr>
<tr>
<td>1999</td>
<td>2793.1</td>
<td>1265.9</td>
<td>1527.2</td>
<td>-1002.5</td>
<td>1406.3</td>
</tr>
<tr>
<td>2000</td>
<td>2565.7</td>
<td>868.2</td>
<td>1697.5</td>
<td>-1234.4</td>
<td>1347.4</td>
</tr>
<tr>
<td>2001</td>
<td>2840.7</td>
<td>681.5</td>
<td>2159.2</td>
<td>-887.6</td>
<td>1687.7</td>
</tr>
</tbody>
</table>

Retained earnings turned negative after the 1997 economic crisis. Shareholders’ equity decreased in 1997 and it experienced some degree of fluctuations after the period. It all indicates that firms’ total asset was not financed by equity but by loans after crisis. Bank overdraft and long-term loan provides an interesting insight in this regard. In 1998, both the short-term and long-term loans went down due to the bad economic condition of the firms. After this period, while short-term bank borrowing was going down, long-term loan was going up. This reflects that credit crunch did not take place and the loan changed its form from short-term to long-term.
Table 5 presents a ratio of short-term bank borrowings to long-term loans for all the sampled industries during post-crisis period to examine if the loan swap took place. It shows that for most of the industries, the ratio became smaller in the later years. In 35 out of 56 cases (4 periods x 14 industries), the ratio is observed decreasing between years. A chi-square goodness of fit test for the changing ratios produce significant statistical evidence in support of the decreasing ratios (Table 6). It indicates that proportion of long-term loan became more dominant over the short-term bank borrowings. The increasing total long-term loan and declining total bank overdraft after 1998 support the reason.

From the Table 5, it appears that firms in all the industries are facing a shift from short-term to long-term loan. Exporting firms which were benefited from currency devaluation after crisis were also facing the shift. Dekle and Hoontakul (2004), in examining post-crisis capital flows in Thailand, categorized Agribusiness, Electronic products, Electronic components, and Textiles as exporting industries. Following the categorization, Table 7 presents exporting and non-exporting industries behavior to obtain bank credit. Figures 5 and 6 are representing visual patterns of the loans.

Table 5: Short-Term Bank Borrowings/Long Term Loan for Manufacturing Industries (1997-2001)

<table>
<thead>
<tr>
<th>Industry</th>
<th>Short-Term Bank Borrowings/Long Term Loan in Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agribusiness</td>
<td>2.27</td>
</tr>
<tr>
<td>Building</td>
<td>0.64</td>
</tr>
<tr>
<td>Materials</td>
<td></td>
</tr>
<tr>
<td>Chemicals</td>
<td>0.38</td>
</tr>
<tr>
<td>Electrical</td>
<td>1.77</td>
</tr>
<tr>
<td>Electronics</td>
<td>3.15</td>
</tr>
<tr>
<td>Food</td>
<td>3.45</td>
</tr>
<tr>
<td>Household Goods</td>
<td>0.65</td>
</tr>
<tr>
<td>Machinery</td>
<td>0.80</td>
</tr>
<tr>
<td>Packaging</td>
<td>1.19</td>
</tr>
<tr>
<td>Pharmaceuticals</td>
<td>7.17</td>
</tr>
<tr>
<td>Pulp &amp; Paper</td>
<td>0.34</td>
</tr>
<tr>
<td>Textile</td>
<td>1.31</td>
</tr>
<tr>
<td>Vehicle</td>
<td>1.64</td>
</tr>
<tr>
<td>Others</td>
<td>7.52</td>
</tr>
<tr>
<td>All</td>
<td>0.75</td>
</tr>
</tbody>
</table>
Post-crisis loan behavior of the both exporting and non-exporting industries was alike. In both type of industries long-term loans, which was constantly increasing pre-crisis, saw a decline in 1997 and that increased again after 1998. However, for the short-term bank borrowings, which had an increasing trend pre-crisis, saw a constant decline after the crisis. It shows that short-term loans were denied by banks to both exporting and non-exporting firms after crisis and instead long-term loans were extended (Table 5).

Table 6: Chi-Square Test: Changing ratios

<table>
<thead>
<tr>
<th>Ratios Changes in the Subsequent Years</th>
<th>Observed Cases</th>
<th>Expected Cases</th>
</tr>
</thead>
<tbody>
<tr>
<td>Decreasing</td>
<td>35</td>
<td>28</td>
</tr>
<tr>
<td>Increasing</td>
<td>21</td>
<td>28</td>
</tr>
<tr>
<td>Total</td>
<td>56</td>
<td>56</td>
</tr>
</tbody>
</table>

Chi-Square Value = 3.500
Df = 1
Significance = 0.061

Table 7: Credit to Exporting and Non-Exporting Industries (Million Baht)

<table>
<thead>
<tr>
<th>Year</th>
<th>Exporting Industries</th>
<th></th>
<th></th>
<th></th>
<th>Non-Exporting Industries</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total Bank Loan</td>
<td>Bank Overdraft</td>
<td>Long-term Loan</td>
<td>Total Bank Loan</td>
<td>Bank Overdraft</td>
<td>Long-term Loan</td>
<td></td>
</tr>
<tr>
<td>1992</td>
<td>711.0</td>
<td>464.9</td>
<td>246.1</td>
<td>1085.9</td>
<td>473.5</td>
<td>612.4</td>
<td></td>
</tr>
<tr>
<td>1993</td>
<td>790.0</td>
<td>541.7</td>
<td>248.3</td>
<td>1247.1</td>
<td>549.6</td>
<td>697.5</td>
<td></td>
</tr>
<tr>
<td>1994</td>
<td>923.8</td>
<td>629.7</td>
<td>294.1</td>
<td>1469.5</td>
<td>629.4</td>
<td>840.1</td>
<td></td>
</tr>
<tr>
<td>1995</td>
<td>1337.3</td>
<td>806.3</td>
<td>531.0</td>
<td>2155.5</td>
<td>823.5</td>
<td>1332.0</td>
<td></td>
</tr>
<tr>
<td>1996</td>
<td>1453.2</td>
<td>919.1</td>
<td>534.1</td>
<td>2635.0</td>
<td>1015.3</td>
<td>1619.7</td>
<td></td>
</tr>
<tr>
<td>1997</td>
<td>1876.7</td>
<td>1203.5</td>
<td>673.2</td>
<td>4546.4</td>
<td>1704.3</td>
<td>2842.1</td>
<td></td>
</tr>
<tr>
<td>1998</td>
<td>1332.2</td>
<td>892.2</td>
<td>440.0</td>
<td>3117.4</td>
<td>1756.4</td>
<td>1361.0</td>
<td></td>
</tr>
<tr>
<td>1999</td>
<td>1157.1</td>
<td>726.0</td>
<td>431.1</td>
<td>3758.6</td>
<td>1584.5</td>
<td>2174.1</td>
<td></td>
</tr>
<tr>
<td>2000</td>
<td>1164.9</td>
<td>591.6</td>
<td>573.3</td>
<td>3386.9</td>
<td>1030.4</td>
<td>2356.5</td>
<td></td>
</tr>
<tr>
<td>2001</td>
<td>1135.7</td>
<td>372.6</td>
<td>763.1</td>
<td>3836.5</td>
<td>861.9</td>
<td>2974.6</td>
<td></td>
</tr>
</tbody>
</table>
6. Policy Mechanism of Banks

To swap the loan from short-term to long-term, Thai banks attempted to roll back the short-term credit from the firms. Most Thai firms borrowed heavily on short-term prior to the crisis and did not use them for their core businesses. Instead, these firms misallocated the borrowed funds into such activities as long-term real estate speculation. Borrowings in foreign currency were also used in equivalent manner. With the hit of the 1997 economic crisis, the wrong allocation of the borrowed funds became a trouble for them as the loan was recalled by the creditors. It resulted in a large number of non-performing loans (NPL) immediately after the crisis. To resolve the NPL problems, Bank of Thailand (BOT) came forward and issued some guidelines for corporate debt restructuring.
The Corporate Debt Restructuring Advisory Committee (CDRAC) was formed by the members of creditors and debtors association and was headed by the Governor of BOT. The committee arranged a voluntary negotiation between the debtors and the creditors for debt restructuring. Debtor-Creditor Agreement (DCA) was used for large debtors and Simplified Agreement (SA) was used for small and medium sized debtors. To attract the relevant parties in negotiation, the committee coordinated with Department of Land, Department of Revenue and related agencies, for amending laws for tax exemption and reduction of land transfer fees. Purpose of this negotiation was to seek sincere commitment from the debtors and creditors toward the procedure and the timeframe to settle the loan. Total NPL status during October 1999 and June 2001 is shown in the Figure 7.

![Figure 7: NPL Status during October 1999 - June 2001 (Billion Baht)](image)

This procedure faced many obstacles as the debtors and creditors had misunderstanding about the motives and the financial statements. Despite the obstacles, the committee could settle more than 1 trillion Baht, which is about 37% of total NPL by the mid of 2001 (Dasri, 2001).

In the debt restructuring process, sub-quality assets were disposed first and debtors’ principal loaned amount was reduced. Secondly, interest rate was reduced and the remaining debt repayment conditions were relaxed. Some of the debtors’ debt was converted from short-term to long-term by transferring it to the disposal of asset management companies. Consequently, short-term loans were reduced and the lower interest rate could not further attract the debtors to borrow.
7. Conclusions

The results of this study do not support the claim that there was a credit crunch in Thailand after the economic crisis in Thailand. It shows that new loans were stopped and old loans were settled from short-term to long-term. It caused long-term loans to increase and short-term loans to decrease after crisis. Firms stopped borrowing because of their bad business condition and also banks were reluctant to extend new loans.

From macro level data, it is seen that there was a slowdown of credit to the corporate sector that satisfied the necessary condition of credit crunch. However, none of the four sufficient indicators SET index, lending rate, MPI, and inflation were satisfied to show that credit crunch existed after the crisis. Declining SET index after the crisis was an indicator of poor financial health of the firms and less demand for the loans. Relatively lower lending rate after crisis could not raise higher credit for the firms. Manufacturing production was increasing with higher retained earnings. Constantly increasing inflation could not increase the level of credit to the firms either.

The micro level data that consist of SET listed manufacturing sector saw a similar decline in the credit after crisis. However, retained earnings were negative during this period indicating demand for loans for financing total assets of the firms. Reviewing the bank overdrafts and long-term loans shows that these loans went down in 1998 due to the bad economic condition of the firms. After the period, while short-term bank borrowing was going down, long-term loan was going up. This reflects that credit crunch did not take place and the loan changed its form from short-term to long-term. The swap has been seen in the banks’ policy mechanism that stopped any new loans and settled the new timeframe for the non-performing loans. Exporting firms which were supposed to get benefits of devaluation after crisis were also affected by the slowdown of credit. Nonetheless, it does not indicate a credit crunch.

In many leverage studies credit slowdown was considered only from the supply side without considering the borrowers condition. Consequently firms’ leverage behavior is not revealed. This study recommends reviewing the studies from actual credit crunch perspectives.

References


Facing Change through I.T. Intervention: The Case of Sabah State Government

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Abstract: The paper examines the role of technology as part of an “electronic government” initiative in the Sabah state public administration, and explores its influences on organizational strategy, structure, leadership and performance after a two-year implementation. Qualitative methodology was utilized involving in-depth interviewing with 18 subjects. Triangulation of data involving unobtrusive observation and archival records was employed. Content analysis was performed. Findings suggest that social structures have been created and power relations distributed where the conventional view of leadership has been redefined with technology being used as a buffer between authority and compliance. “Electronic government” has led to a proliferation of how information is to be used, disseminated and retained. The research brings to light a paradigm deemed critical for cross-boundary exposure and competition in a developing country. For the Sabah state, “electronic government” has become a vision more than a tool.

Key words: Technology, Public Sector Management, Organizational Change, Malaysia, Interviewing

Introduction

The faults of a superior person are like the sun and moon. They have their faults, and everyone sees them; they change and everyone looks up to them.  

In 1996, the Malaysian government announced the establishment of the Multimedia Super Corridor (MSC) as a first step towards achieving “electronic government” aimed at transforming the country to a global nation. Under the MSC, seven distinct applications were to be developed: smart schools, telemedicine, research and design cluster, worldwide manufacturing webs, borderless marketing and the intelligent multi-purpose card (Johare, 2001). In response, the public administration of Sabah, an Eastern state of

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Malaysia, launched a comprehensive range of technological applications within the purview of the Sabah.Net architecture. These include internet homepages, directory service, calendar of events, electronic tender notices, electronic statutes and laws, electronic circulars and government gazette. In addition, more applications had to be progressively developed based on local content to enhance the existing Sabah.Net services, including a customer helpdesk system, Sabah State Government e-portal and a one-stop public feedback system.

This move started in 1989 when a comprehensive work-culture movement was introduced in Malaysia through a series of guidelines known as the Development Administration Circulars (DACs). The DACs were introduced as a process of reforming and transforming the mindset of public servants as well as institutionalizing a culture of excellence. Under the DACs, various strategies and programs were introduced including such total quality management initiatives as quality control circle ISO 9000 (Asli, 1998). According to Sarji (1993), the objectives of the reforms are threefold: First, to create a civil service which is efficient, effective, dynamic and innovative; second, to create a civil service with a high level of discipline and high standard of integrity; and third, to create a civil service that is action-oriented, people-oriented and customer-focused. All state governments, including the State Government of Sabah, subsequently adopted these circulars.

“Electronic government” as an initiative in transforming the technological landscape of Sabah serves as a change intervention agent in the state’s public organizational reform. The initiatives undertaken are aimed at improving the performance of service delivery by the government to the people. For instance, people will be better served because of improved customer service just as the introduction of the electronic applications will contribute significantly to the socio-economic development of Sabah, especially when the current state of technological infrastructure is still at its infancy. In this study, we will assume that the public administration of Sabah as a macro-organization that has undergone the transformation of organizational change as a result of the strategic influence of technology on organizational life. By “electronic government”, we refer to it as more than a subliminal concept; it embodies the sophisticated applications of technology as deemed essential to the improvement of organizational life, and suggests an openness to embrace changes in routines and norms as a different dimension to work efficiency and effectiveness.

In line with the starting quote by Confucius, “electronic government” is likened to the sun and moon, which would lead to disruptions and polarities in terms of acceptance and rejection as associated with change. However, through the test of time, the “superior person” (electronic government personified) will (re)organize the chaos in ways that enforce “change” and “improvement” as mutually implicating processes and outcomes (Schein, 1993). In particular, we raise two important questions that constitute our Research Problem (RP) for this study: (RP) How and why does “electronic government” influence organizational change, particularly in the areas of strategy, structure and people in the State Government of Sabah? How will “electronic government” lead to organizational performance?

An Overview of the Literature
The theoretical foundation of change management is governed by three distinct perspectives: individual internalization, group dynamics and systems archetypes (Burnes, 1996). Firstly, the individual perspective suggests that the process of change is related to behavior, environment and reason, as interpretation and understanding of self and the lived experience stem from a fundamental rationality that ultimately leads to modifications in behavior (Smith et al., 1982). Secondly, the group perspective emphasizes organizational change as contingent upon the roles, values and cultures around which teams and workgroups operate (Bernstein, 1968; Cummings and Huse, 1989). In this context, individuals are seen modifying and changing their behaviors as a result of a group’s prevailing practices and norms (French and Bell, 1984; Lewin, 1958). Thirdly, the systems perspective posits that an organization is constituted of a number of inter-connected subsystems where any change in one part will have an impact on the wider system affecting its overall performance (Scott, 1987). Further, internal systems are susceptible to the influences of the external environment and vice versa (Buckley, 1968). As supported by open systems theory, this perspective is concerned with the understanding of organizations as organisms which function holistically and in entirety (Burnes, 1996; Galbraith, 1973).

Two organizational change models have been found to dominate the literature, that of planned and emergent change. Conceptually, these models have been used to explicate change processes that occur in shifting contexts while the three perspectives of change are crucial for the description of areas pertaining to change. For instance, the planned change model is used when the operation of an organization is in a stable and predictable environment where changes driven by a top-down approach through a linear conception (Gardner and Ash, 2003; Styhre, 2002). On the other hand, the emergent change model is more appropriate for organizations operating in an unpredictable and complex environment where changes occur qualitatively and continuously, often driven by a bottom-up approach (Burnes, 1996).

The Planned Change Model

This model assumes that structures, processes, technology and human skills, capabilities and knowledge can be changed to support or optimize the achievement of identified strategic organizational goals (Gardner and Ash, 2003). An example is the three-step model developed by Kurt Lewin (1958), which consists of such phases as “unfreezing”, “moving” and “refreezing”, providing a general mental schema for the understanding of change processes (Cummings and Huse, 1989; Styhre, 2002). “Unfreezing” is required to reduce the forces that maintain the organization’s behavior at its current state. This requires the relearning of entrenched habits and routines through team building and management development. On the other hand, “moving” acts on the outcomes of unfreezing by analyzing the current situation and identifying the most appropriate alternatives. Consequently, action is required to move the organization to a more desirable state where new behaviors, values and attitudes will develop. Yet, “refreezing” aims at stabilizing the organization in achieving a new level of equilibrium in order that new ways of working are fully imbued. This is often realized through the use of such mediating agents as organizational culture, norms, policies and practices (Cummings and Huse, 1989).
The emergent change model

This model is associated with learning process rather than a method of change as influencing organizational structures and practices. It operates on the assumption that change is not linear but involves complexity and ambiguity. Within this perspective, leaders are seen as highly competent and adaptable, capable of switching from being controllers and coordinators to facilitators and collaborators. Employees are believed to be willing to take responsibility for identifying deficiencies and implementing change. However, those adopting this model are well aware of the unpredictability in managing organizational transitions. Individuals adopting the emergent change model tend to provide alternatives as a means for challenging planned change perspectives. As such, although these two models have fundamentally opposing systems of ideas, they can be viewed as interdependent approaches that apply to complex organizational environments (Bamford and Forrester, 2003, Burnes, 1996).

“Electronic Government” as a paradigm

Although change management theories and concepts were developed as early as the 1930s, the use of “electronic government” as a paradigm in facilitating organizational change has not been comprehensively researched on. A possible reason could be due to the applications associated with its development and implementation being perceived as chaotic and unmanageable (Layne and Lee, 2001). Moreover, studies have shown that the positive aspects of this (emerging) paradigm have not been very encouraging (Teicher et al., 2002).

Applying the planned and emergent models to the technological manifestations of “electronic government” has led to two fundamental assumptions in relation to change. Uppermost is change being viewed as an ongoing process rather than an event that can be terminated at some point where the organization can be expected to achieve a state of equilibrium. Secondly, it is assumed that technological and organizational changes made during the ongoing process cannot be anticipated ahead of time. An example to support this view would be the use of electronic mail to facilitate increased and faster communication among organizational members during a planned change. Conversely, the use of electronic mail might be manipulated during conditions of emergent change when it serves as an informal information channel in disseminating less official content to different people of the organization, such as the transmission of rumors. In essence, the use of technology involves a series of planned and emergent changes that are intertwined in great complexity as a direct response to uncertain conditions, events and outcomes that have arisen from experimentation and manipulation (Abraham et al., 1999; Orlikowski and Hofman, 1997).

A Conceptual Framework

In conducting this exploratory study, we developed a conceptual framework which served as a prior theory for this research. According to Yin (1994), the use of theory is not only an immense aid in defining appropriate research design and data collection; it also
functions as the main vehicle for generalizing the results of qualitative studies. In addition, comparing the prior theory with the existing literature to identify any similarities or differences that need explanation is useful in increasing the internal validity, generalizability, and theoretical rigor of theory building (Eisenhardt, 1989). As a theory-building research, our focus is on the case of Sabah state public administration. In support of the research problem, we further developed four Research Questions (RQ):

(RQ1) How has the implementation of “electronic government” affected the strategy, particularly the long-term objectives of the organization?
(RQ2) Why does the implementation of “electronic government” affect the structure of the organization such as the level of authority?
(RQ3) How do people, particularly organizational leaders, influence the change process through “electronic government”?
(RQ4) How and why has the implementation of “electronic government” affected the overall performance of the organization?

As represented in Figure 1, we have developed a framework that places emphases on the key aspects of the RP and RQs. Such variables as “strategy”, “structure”, “people” and “performance” are well suited for studies in organizational change processes. For instance, Martin (2001) posits that technology could be utilized to have an influence on the structure, people and task. Similarly, Cummings and Worley (2001) describe how technological change has led to modifications in organizational strategy, structure and process. Further, Gardner and Ash (2003) associate the planned change model to such variables as structure, process, technology and human skills as contributing to organizational performance.

![Figure 1. Preliminary framework of the “electronic government” intervention in organizational change process](image-url)
Strategy

Strategy is commonly associated with the short and long-term objectives, mission and vision of an organization. In normal circumstances, an organization will not change its mission and vision; however, short and long-term objectives can sometimes be affected by uncertainty caused by the internal and external environments (Baines, 1998). As Gardner and Ash (2003) would argue, modification to such objectives could lead to changes in organizational strategy, structure and culture. Changes in strategy would influence the courses of action and the allocation of resources necessary for achieving these objectives. As a type of planned organizational change, strategy would entail a series of managed interventions to achieve a desired outcome.

In responding to such a change, organizations might encounter dilemmas associated with adaptive or generative approaches to process improvement and transformation. As such, two approaches to change would be considered: the “soft” approach where change is associated with organizational culture, continuous improvement and empowerment; and the “hard” approach which involves structural change, radical transformation and strong leadership (Stace and Dunphy, 1997). Ultimately, strategy should be viewed as a process of developing a sense of direction for the organization, monitoring the internal and external environments to ensure that some order is maintained, and keeping resources as flexible as possible as a means of helping the organization respond swiftly to changing developments (Walsh et al., 2006).

Structure

Grundy (1993) defines structure as associated with roles, relationships, activities, authority, responsibility, communication and control. For over thirty years, the emphasis of management theory has been on the design of structures and how they evolve as a response to their immediate environments (Gardner and Ash, 2003). For instance, studies have shown that organizational structures should be adapted to comply with various environmental conditions or contingencies (Burnes and Stalker, 1961; Lawrence and Lorsch, 1967). It has been found that if the environment is stable and predictable, as was the case for many organizations in the 1960s and 1970s, a bureaucratic or mechanistic structure is likely to be most suitable. In contrast, if the environment is more dynamic and unpredictable, a more adaptable organic type of structure would be desirable. It was not until the 1980s when Peters and Waterman (1982) popularized the idea of fast, flexible and flat structures for dynamic market environments. As an extension, Kanter (1999) further introduced the importance of lean and efficient structures with reduced layers of hierarchy. In practice, some of these concepts have been more commonly known as the restructuring, de-layering and flattening of hierarchies. Other implications involve such downsizing consequences as the elimination of jobs and the outsourcing of non-core activities. Practical examples of these circumstances can be seen in the Australian and New Zealand public and private sectors during the early 1990s (Litter et al., 1994).

Structural change can also be in the form of formalization, centralization, span of control and/or networking. According to Stace and Dunphy (1997), structural intervention
involves the restructuring and redesign of office layout, the introduction of new technology and/or the replacement of leaders. Modification of rules, policies and procedures are possible consequences of a structural change (Johns, 1996). As an example, infiltration of technology in the form of automated operations that ease organizational processes would transform a bureaucratic structure into an organic one through the removal of simple and repetitive tasks, and the people involved in performing them (Baines, 1998). As such, technology and structural change occur hand in hand, providing two possible scenarios: Firstly, change affects the interdepartmental cooperation reducing the level of formality and hierarchy in human relations; secondly, change leads to a bottom-up decision-making from an authoritarian top-down model. In addition, effective structuring is a critical variable in producing effective organizational performance.

**People**

Although organizational behavior has its origins in the Mayo experiments in the 1930s, it was only in the 1980s that researchers began to recognize the significant role of people in organizational change (Nutt, 1986). Two important aspects of people are of concern to change: The first is individualistic with a focus on the impact of knowledge, skills, self-awareness and self-esteem; the second is concerned with the type of leadership, culture, environment and the perceived consequences of success or failure within the organization (Zeffane, 1996). As such, the capability of an organization to achieve change depends on its people because they can either hinder or develop the change as required (Smith, 2004). For instance, the resistance to change by people has been one of the major problems in achieving organizational success (Nadler, 1988). Resistance to change could be due to such reasons as past personal investments, uncertainty, identification with previous routines and firmly-held ideologies (Thornhill et al., 2000).

In the case of public organizations, the biggest challenge in any change initiative has also been associated with people. Conditions of overstaffing and an oversupply of highly-structured systems, rules and regulations have had a serious impact on organizational outcomes (Mustafa et al., 2000). As well, the role of leadership is a critical consideration for organizational change as leaders function as unifying agents in facilitating change and restoring fragments of change into some form of order. Without effective leadership, change processes would become chaotic as a result of environmental pressures (Stace and Dunphy, 1997). Essential leadership functions should include the establishment of direction, the communication of shared values and the motivation of people to overcome barriers that might obstruct change.

**Organizational performance**

Organizational performance is more than an image that resides in the minds of organizational members; it signifies both tangible and intangible possibilities that can be achieved by an organization in the long run. Common determinants of organizational
performance include effectiveness, efficiency, productivity, flexibility and creativity as evaluated both in terms of process and outcome (Gardner and Ash, 2003; Ree, 2002). However, a more conventional perspective of organizational performance is related to financial outcomes including budgets, assets, operations, services and human resources as determining the tangible bottom-line of an organization (Dixon, 1999; Smith, 1999; Thurbin, 1994).

From the organizational perspective, performance involves a wider dimension and includes the specification of goals, the strategic position of people and processes, and organizational culture to support the various transformational initiatives (Thomson, 1999). Hence, apart from financial measurement, organizational performance also embodies such non-financial measures as attitude, commitment and the way individuals acquire knowledge. For instance, knowledge and competence are regarded as examples of intangible assets where employee competence, internal structure and external structure are of concern to organizational processes (Yeo, 2003). The intangible perspective of performance is largely relevant to the public sector as complexity in organizational processes makes quantification of actual performance problematic (Smith, 1993). For instance, customer service, and the utility of public services including extent of usage and frequency are commonly used as criteria for measuring performance. In other cases, performance is evaluated on the basis of administrative efficiency such as time taken to process an application, error rate and promptness in answering phone calls (Macpherson, 2001). In essence, organizational performance should be viewed as yielding long-term quantitative outcomes through continuous qualitative processes (Osborne and Gaebler, 1992).

Methodology

We adopted an exploratory approach in the data collection through multiple methods including interviews, annual reports, and unobtrusive observation. Qualitative methodology offers richness in the phenomena and issues being investigated. According to Yin (1994), this approach would be appropriate if the research deals with problems of how and why probes and would be preferred “when the investigator has little control over events, and when focus is on a contemporary phenomenon within some real-life context” (p. 130). In support of this perspective, Rowley (2002) comments that qualitative studies are suitable to the researching of new areas for which existing theory seems inadequate.

In our research, a pilot study was conducted to refine the interview protocol and this involved a small sample of five respondents from the Sabah State public administration division. These included a director, two middle management officers and two I.T. officers. In the main data-collection stage, three internal sample groups constituting a total of 18 respondents were chosen. According to Yin (1994), subjects chosen should constitute different groups of people who have prior knowledge of the phenomenon under investigation. In our study, each group was selected based on the various key units of people who had direct experience with the conceptualization and implementation of “electronic government”.
We limited each group to six participants for practical concerns of control and quality of interviewing and a purposive sampling plan was adopted (Eisenhardt, 1989). Group 1 consisted of department heads and permanent secretaries while group 2, middle management and division or section heads. Yet, group 3 included I.T. officers or systems analysts. The subjects were selected based on their nature of work and the scope of their involvement in “electronic government”. A fundamental consideration was that they should have had direct experience with this initiative for a minimum period of five years and retained with them adequate records to help verify their views on the phenomenon under study. This is an important criterion for the triangulation of data where historical records are concerned (Yin, 1994). Further, we excluded subjects who were not proficient in English as this could influence the validity of the data as some of the words used in the interview questions could not be directly translated into the Malay language.

The pilot semi-structured interviewing was a crucial aspect of the research as it helped us to be more familiar with the context and the issues involved (Hussey and Hussey, 1997). During each of the five interviews lasting between 30 and 60 minutes, we managed to identify complex issues and ambiguous questions which helped us refine the final interview questions. In the main stage, we employed structured in-depth interviewing with 18 respondents. During the interviews each lasting between 45 and 60 minutes, we used the research questions and interview protocol to guide us closely in the data collection. However, we also allowed spontaneity to emerge when the respondents were forthcoming in sharing their experiences. The interviews were tape-recorded and subsequently transcribed. For triangulation, we depended on reports, documents including official publications and unobtrusive observation of workplace activities.

To achieve construct validity, we utilized multiple sources of evidence to establish a stream of evidence. For internal validity, we provided within-group and cross-group analysis and matched our findings to the literature. In terms of external validity, we identified three independent groups from within a macro-organizational context to realize replication logic. Finally reliability was achieved through the use of a systematic and consistent coding mechanism in the data analysis with constant reference to the research questions and literature (Hsu, 2005; Krippendorff, 1980).

During content analysis, data were carefully coded and grouped into smaller categories allowing patterns and themes to emerge. The process was a highly systematic yet rigorous one as we disintegrated the messy data into meaningful categories (Saunders et al., 2000). In ensuring inter-coder reliability, we separately analyzed the transcripts, compared and contrasted the findings from each interview. When individual themes and patterns were interpreted, we adopted a systems perspective in reducing the data to obtain a clear set of collective responses (Jassawalla et al., 2004). In the process, we used the prior theory to guide us in the analytic procedure to achieve pattern-matching (Miles and Huberman, 1994).
Findings and Discussion

(RQ1) How has the implementation of “electronic government” affected the strategy, particularly the long-term objectives of the organization?

Mintzberg (1990) posits that strategy takes the form of a blueprint which contains specified objectives, budgets, programs and operating plans; it is integral to the planning process. Our findings for RQ1 are closely aligned to this perspective with one respondent (M1) associating strategy with the intended policies or functions required to move the organization towards its desired direction and goals. Another respondent (T3) referred to strategy as action plans that are related to work processes and human resources for future development. As such, strategy is taken to refer to a conscious effort to modify routines by transforming the individual consciousness of actors so as to promote the intended behavioral outcomes that, when executed collectively, will lead to the ultimate change of the organization.

An interesting observation made by a respondent (M2) suggests that by incorporating electronic features into a “government”, it is a representation of change at the strategic level with long-term consideration where the Sabah civil service is seen as globalizing. For instance, technology has helped the organization to unlearn old ways of doing things by relearning new skills and applications. An expected outcome is a shift in focus from capacity to competence. Previously, performance was evaluated on the basis of the amount of laborious work rather than the efficiency and creativity of work done through the support of technology. This observation has led to several implications for human resource management and development, as represented by the following quote:

(H2) “At the macro (state) level, change [is] from bureaucratic-oriented to results-oriented management…with process being the focus. At the organizational level…change for example has led to a shift from the traditional mode of training to performance or competency-based.”

Changes in strategy have been perceived as the transformation from an old to a new system, suggesting a shift from a paper-based labor-intensive environment to one that is almost paperless and less-labor-dependent environment. According to Gardner and Ash (2003), strategic change requires the modification of long-term goals and objectives by considering current and future resources, and their potential for facilitating and sustaining the change. Examples of a long-term objective for the Sabah civil service include the following:

(H5) “The strategy will be in the form of speed of communication…a key benefit is outreach…reaching people in rural areas.”
(M3) “Electronic government…has facilitated knowledge sharing and information integration.”

Based on one of the researchers’ unobtrusive observations of the daily operations in the different departments over a two-year period, it was found that work processes had been altered to an extent that many employees were seen juggling between old ways of doing things and new ways of undoing things. At times, unexpected situations caused
employees to be reactive rather than responsive to potential learning, as exemplified in the following quote:

(T3) “Customers have complained that the systems are not user-friendly… this has led to additional paper work to compensate for the inefficiency of technological glitches…”

As a result, group learning was, to a large extent, induced in circumstances of change as both virtual and physical teams were developed to handle emerging issues and procedures. Reflected in a respondent’s account is an interesting quote on the role of team creation:

(T5) “One strategy is to use technology to create, maintain and develop teams in the organization. We want a culture that promotes collaborative working and learning.”

In this context, learning occurs through change or adaptation based on experience. As such, “electronic government” reflects the need for organizations to adopt forms that allow continuous adjustment and learning (Mintzberg et al., 2005; Senge, 1990). As described, the disruption and complexity brought about by “electronic government” are legitimate side effects of organizational life where the propensity to change is inevitable. Here, organizations that are mechanistic in their approach to strategizing the use of technology would not reap the rewards as much as those that imbue an organic paradigm (Bennis, 1969). In volatile times like these, the need to embrace spontaneity and flexibility in less certain contexts cannot be overemphasized.

(RQ2) Why does the implementation of “electronic government” affect the structure of an organization such as the level of authority?

An organizational structure largely imbues characteristics of a social system as manifested in rules and resources that mediate social action through three dimensions: facilities, norms and interpretive schemes (Giddens, 1984). As summarized by a respondent, structure consists of people, values and systems that have an interrelation with organizational policies and procedures. Enacting these policies would require strong leadership, as represented in the following quote:

(H5) “…structure is just symbolic…Good leaders are important. Structure is static and whether is positive or negative depends on leadership. The main concern is how people create the system as collectives.”

Within this perspective, “electronic government” is seen as supporting a structure that allows dynamic exchanges in social practices such that organizational members can interpret tacit and explicit knowledge based on prior and current experiences. In guiding ongoing actions, employees will draw on the technological facilities for the application of knowledge in order to challenge routines and norms, and allow emerging actions to be structured (Johns, 1996; Orlikowski, 2000). As such, expectations in terms of roles, relationships, authority and responsibility will be reshaped according to new actions (Grundy, 1993).
As observed, “electronic government” has led to an open work environment where senior officers can communicate with employees at multiple levels simultaneously compared with a much more bureaucratic approach previously. As information can be misappropriated easily, users need to be responsible for and accountable to their actions. In this context, employees are empowered to utilize information resources in ways that benefit themselves and the organization, as highlighted in the following quote:

(H1) “Empowerment has been channeled down to the individuals…allowing everyone to execute his/her own creativity and innovativeness in getting work done.”

Although most respondents highlighted that “electronic government” had affected the structure, none referred to the Intranet being used for file sharing, online internal transactions or application integration as a source of narrowing the knowledge-dissemination structure. One of the reasons could be that the Intranet was used to link departments at the same level rather than divisions across the Sabah public sector. This suggests that people are still operating within existing organizational hierarchies where release and channeling of information are still subject to approval and screening. Also, the fear of losing control of how information might travel is one reason why “electronic government” applications have not been fully accepted and utilized (Teicher et al., 2002).

Observably, the “electronic government” paradigm has led to a more lateral distribution of middle-management power structure. This concerns the level and speed of approval in work processes and procedures particularly when the electronic medium serves as a buffer between supervisors and subordinates in their power relations. As information can be made available to the relevant parties electronically, the level of transparency in documentation and decision-making is gradually increased. Although “electronic government” has led to an increased complexity in configuring work processes and human relations, it has narrowed the organizational world for employees as technology has helped mediate social and power relations.

(H2) “In terms of accountability, the senior management of [the] organization will be responsible… Besides that, we need a basic level of trust and empowerment to better facilitate approvals of electronic applications. We are in the business of de-layering our organization [through electronic government].”

This perspective further reinforces our earlier proposition that technology facilitates an emergent change by transforming a mechanistic organizational structure to one that is organic in nature (Baines, 1998). This involves the reduction of repetitive tasks by challenging existing routines and norms. Mustafa et al. (2000) highlighted an example of an organization in Sabah that had successfully provided a friendly working environment using IT-based facilities. This organization was able to modify the hierarchical structure by reducing several layers of reporting to incorporate flexible and cross-border functions.
While “electronic government” has demonstrated little impact on the physical structure of the organization, it has affected the social structure to a large extent. As evident in the following quote, it is the people who will function as mediating agents in the structuring and restructuring of organizational life, which involves recognizing both positive and negative behaviors:

(M5) “You may have the best technology...if people are not committed, it won’t work. It is the human factors such as abusing internet usage that will work against the organization.”

(RQ3) How do people, particularly organizational leaders, influence the change process through “electronic government”?

We have observed that “electronic government” has led to changes in staffing practices, task deployment, customer relationships and communication strategies (Galbraith, 1995). According to Smith (2004), people are a crucial factor in change processes as they can either facilitate or truncate change. As highlighted by a respondent, “electronic government is not necessarily embraced by all employees:

(H3) “Resistance to change...people do not want to move away from [the] comfort zone.”

Among the various reasons for employees’ resistance to change, two dominant themes have emerged from our data: fear of disrupting defensive routines and lack of leadership commitment. These observations are also reinforced in the studies of Kotter (1996) and Nadler (1988) who found that over 60 per cent of failure that occurred in any change initiative was caused by a lack of direction and assurance from the top management. The following quote exemplifies the sentiments of employees on the negative influence of “electronic government” on organizational leaders:

(T1) “We still have leaders in the organization that do not like using technology. Some prefer to use the old ways and they are not very keen to learn [new things].”

Our findings further reveal that leaders should function as unifying agents in facilitating change processes. For instance, one of the recurring and dominant themes that emerged from the responses of the senior management (H1-H6) attests to the need for collective commitment among leaders so as to conceptualize and develop the appropriate types of “electronic government” applications. As recounted by a respondent, one of the deterrents to transforming the Sabah state public administration is the lack of concerted interpretation on the role of “electronic government” as an emerging paradigm:

(T2) “People do not value technology...the concept [of technology] needs to be corrected. Do the top officers care about technology? What is lacking [at the moment] is the failure to appreciate the value...of technology.”

If viewed positively, “electronic government” could yield significant outcomes as highlighted by a respondent on how it was effectively used in the selection process of officers under the succession-planning program.
“...if electronic government is viewed in the right spirit, we (organization) will experience transformation changes. Since its implementation, we have seen some positive results not only in daily functions but in strategic functions as well.”

Leaders also act as sponsors of change, constantly utilizing their power and authority to sanction and legitimize change. They facilitate the change process by assessing the threats and opportunities, and identify alternative solutions to alleviating obstructions and ensuring expected outcomes (Abdul Karim and Mohd Khalid, 2003). As such, leaders need to communicate a sense of urgency and build appropriate platforms for change (Appelbaum et al., 1998; Chapman, 2002). In the case of the Sabah civil service, the change sponsors include the State Secretary, permanent secretaries in the various ministries and heads of departments. “Electronic government” is expected to affect the organization and reduce the many capacity deficits. Hence, leaders need to acknowledge that it is more than a change in technological and work processes; it is a transformation of employees’ attitude as well as their readiness to unlearn and relearn. In this regard, leaders need to imbue a long-term perspective of “electronic government” on how it might enhance organizational life at various stages:

(M1) “Leaders perceive electronic government as an agent of change in terms of how it can assist the organization in achieving better performance and enhancing the civil service of the (Sabah) state.”

According to Appelbaum et al. (1998), leaders must connect with the minds and hearts of the people in order to bring about lasting change. The challenge is to maintain a delicate balance in serving internal and external customers insofar as public service transformation is concerned. A study conducted on 700 senior civil servants in twelve countries reveals that human performance was ranked as the most important source of competitive strength, ahead of productivity and technology (Abdul Karim and Mohd Khalid, 2003). Similarly, Yeo (2003) found that senior management support and the collective involvement of individuals are critical considerations for organizational change and development.

(RQ4) How and why has the implementation of “electronic government” affected the overall performance of the organization?

The classical perspective of organizational performance is concerned about financial outcomes. However, recent literature has concentrated on the intangibility of performance including goal-setting, the strategic alignment of people and processes, and the monitoring of progress and organizational culture to support various change initiatives (Halloway et al., 1999; Tvorik and McGivern, 1997; Yeo, 2003). As such, in considering organizational performance at a broader level, attention should be given to individuals, processes and purposes. However, public sector organizations operate in a different frame of reference from private organizations. The public sector has a different objective when evaluating organizational performance as it is not driven by profits; rather, the focus is on service orientation due to social responsibility. In this regard, performance of public organizations is harder to measure as they are subject to public inquiry and scrutiny in...
addition to the pervasive influence of politics and accountability to political appointees (Teicher et al., 2002). As a consequence, our study has shed light on the intangible aspects of organizational performance rather than financial achievements.

Our findings reveal that “electronic government” has led to a change in the work culture and mindset of individuals. For instance, there is a growing interaction between lower-level staff and the top management through electronic exchanges. Although the dynamics are not immediately noticeable from a social perspective, there is an underlying willingness to share information which motivates more timely actions not previously evident. Although authority associated with hierarchy is not completely lateralized, power relations have been simplified through the minimization of unnecessary physical contact between employees in approval or decision-making processes. This is attested in the following recurring responses:

(T6) “…a lot of information can be easily accessed; therefore we become more knowledgeable and this has helped me to make better decisions.”

(M1) “The networking of officers has improved and the staff are no longer afraid to voice their views because they can do so via email.”

Invariably, the way information is used, processed and disseminated has contributed to a fundamental level of job satisfaction as the laboriousness of task execution through manual paper-based means has been gradually reduced. As reinforced by another respondent:

(T4) “People are now becoming…dependent on technology and therefore, [there is] a change in [human] behavior…the competence of staff seems to have increased.”

As the daily performance of individuals improves with increasing familiarity in the use of “electronic government” applications, the byproducts, as observed, are efficiency in task execution and effectiveness in problem solving. Our study is line with the research of Mustafa et al. (2000) who found that the drastic improvement in the speed of communication has caused defensive routines to be disrupted in allowing relearning to take place. In the following quote, a respondent shared how “electronic government” had helped enhance employee competence:

(T6) “…a lot of information can be easily accessed; therefore we become more knowledgeable and this has helped me to make better decisions.”

As observed, there is a marked improvement in the performance and delivery of services in both quality and productivity. Further, communication among other governmental departments has improved irrespective of geographical locations.

(H3) “When customers get immediate response, they become more enthusiastic. Overall, there is impact…The citizens have become encouraged and less doubtful of governmental services, for example in applying for licenses or passports.”

Ultimately, the emerging features of “electronic government” have allowed both internal and external customers to be better served. Internally, there is a stronger sense of shared consciousness in goal orientation and a preparedness to embrace challenges as the
Malaysian economy globalizes. A fundamental concern of the Sabah state public administration is to develop a responsive delivery system that can handle potential challenges brought about by the external environment.

(M4) “Performance has improved…in terms of monitoring, planning and execution. When you have access to [useful] information, you can benchmark your performance against other outstanding governmental departments at the national and perhaps the global level.”

Implications for theory

Based on our findings, the earlier conceptual framework (Figure 1) will need to undergo some modification. For instance, “electronic government” as a change agent does not affect the variables of strategy, structure and people linearly. Changes that have occurred in the Sabah state public administration are far more complex than anticipated. Findings from our cross-group analysis further reveal that there are distinct perceptions and assumptions which the subgroups imbue when evaluating “electronic government” as an emerging change paradigm. For instance, the senior management’s (H1-H6) view of strategy signifies a long-range orientation with “electronic government” being perceived as an intermediary of organizational globalization necessary for continued renewal. On the other hand, the middle management (M1-M6) would adopt a more pragmatic view of aligning departmental goals and objectives to organizational vision and mission. Yet, for the technical specialists (T1-T6), strategy is the maintenance of the infrastructure and anticipation of its unpredictability to ensure efficient operations.

These interconnected yet subtly diverse views further impinge on the role of leadership as mediating social structure, learning and performance at both the individual and collective levels. While leaders would like to maintain the same level of hierarchy even with the minimizing of physical interactions due to an increase in virtual connections, employees generally welcome opportunities for the lateralization of relationships and formalities. The senior management (H1-H6) would view “electronic government” as restoring organizational structure in a paradigmatic way with leaders being viewed as active organisms in re-ordering complexity. On the other hand, the middle management (M1-M6) perceived themselves as stewards in reinforcing social structure, and facilitating learning and problem solving. Ground-level employees represented by T1-T6 tended to view structure and leaders as intimately bound armed with the capacity to order change, and integrate ambiguities.

Consequently, organizational performance was viewed with a macro perspective by leaders as an intrinsic response to competitive survival and globalization. Hence, there is a theme of collectiveness associated with what is deemed performance at the organizational level. Almost all leaders agreed that “electronic government” is a paradigm that seeks short-term convergence for long-term divergence; the former suggests that technology as a connecting tissue is necessary for the consolidation of internal processes while the latter, a mediating agent necessary for cross-boundary collaboration, development and growth. General employees, on the other hand, provided a more micro perspective by associating organizational performance with collective work
efficiency and effectiveness with a focus on immediate output rather than possible opportunities for future development. Because of the dynamics created between these variables, a modified framework has been developed (see Figure 2).

Figure 2: Modified theoretical framework of “electronic government” in organizational change process

An underlying theme of this new framework is that the interacting variables function in mutually-implicating ways with “electronic government” being the main catalyst of change. Although the people factor has been perceived as a dominant influence of change (see for example Martin, 2001; Mustafa et al., 2000, Stace and Dunphy, 1997), our study reveals that people function as unifying agents of change where the extent of change is determined by how strongly organizational vision is communicated to and imbued by all levels of employees. Until a shared consciousness of what it is that necessitates change is constituted, no real change is likely to take place at the organizational level.

According to Nyström and Starbuck (1981), in order for any change initiative to be successfully institutionalized, organizational redesign must be carefully considered to allow genuine change and improvement of the existing order to occur. With the introduction of “electronic government” in the Sabah state public administration, a delicate balance is needed to achieve mechanistic organizing while allowing less formal approaches to emerge. This suggests the need for maintaining routine tasks efficiently in stable environments while allowing anticipated disruptions for growth and development in turbulent environments (Argote, 1982). The proposition brings to our earlier discussion on organizations as having the potential to be either structured mechanistically or organically. In the view of Vaast and Levina (2006), there needs to be a greater interplay between the two structures to produce a synergy for any emerging organization to succeed in volatile environments. As such, our proposed framework further seeks to explore a more considered relationship between “electronic government” and the potential of routines that affects unlearning, relearning and ultimately learning. As
encapsulated in yet another quote by Confucius, change is a necessary condition for inner fulfillment:

They must often change, who would be constant in happiness or wisdom.
- Confucius

Conclusions

The current study was limited by a non-cross-sectional sampling plan to elicit a more diverse range of responses on “electronic government” as a change agent. Although triangulation from archival records was employed, it was too time-consuming for us to go through the details extensively. As some of the interview responses were provided in the Malay language due to ease of reference on certain issues, parts of the translation to English could have been too literal. We do not rule out the possibility that some of the crucial information could have been lost in the translation. We did, in the course of data verification, rescue some of the mistranslated or misinterpreted information through thorough follow-ups. The absence of longitudinal data also prevented us to gather periodic data to track the actual change process during the two-year period.

For future studies, views could be sought from a wider sample including external customers to evaluate the role of “electronic government” as a change agent in service delivery. For a wider understanding of “electronic government” in organizational change processes, the transactional process of government with businesses and citizens could be examined. Longitudinal studies would be appropriate in change management research as causal relationships could be established and time-lag effects controlled over periodic timeframes (Gill and Johnson, 1997; Sekaran, 2000). As an example, longitudinal studies could be employed to examine the effects of change brought about by “electronic government” in other developing countries over five to ten years or even longer periods.

Future lines of study could also include in-depth analyses of change as associated with organizational culture and human behavioral patterns. Culture is a critical intervening variable that determines if change is to be accepted, truncated or modified. Culture will also influence the way change processes are to be facilitated and developed with a focus on employee commitment, motivation and an openness to handle disruptive routines (Abdul Rashid et al., 2004; DeLinsi, 1990; Driscoll and Morris, 2001; Parker and Bradley, 2000). We conclude with several Hypotheses (H) for future development:

(H1) The more complex the strategy used in maximizing “electronic government” applications, the greater the employees’ resistance to change.
(H2) The more hierarchical the structure in the organization, the greater the employees’ reliance on past experiences in handling routine tasks during an “electronic government” intervention.
(H3) The higher the level of interaction between leaders and employees through “electronic government”, the greater the chances of collective learning and knowledge acquisition.
(H4) The more dynamic the change processes in “electronic government” intervention, the greater the intangible outcomes leading to organizational performance.
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Perception of Corporate Branding in a Middle Eastern Context

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Abstract: Corporate image and reputation are regarded as the most critical, strategic and enduring intangible asset for a company. A favorable corporate image and reputation can be an effective form of differentiation and a source of competitive advantage ensuring long-term success. This research focuses on the customers’ perception of the corporate image and reputation of large commercial banks in Saudi Arabia. It seeks to develop an appropriate way of measuring corporate image and reputation by identifying a set of specific factors and scale items. Questionnaire survey was employed in the data collection. Results, explaining 73% of the total variance, indicate that three factors significantly influence perception: “financial prospect”, “corporate management”, “publicity and corporate communication”.

Keywords: brand management, customer value, integrated marketing communication

Note: Author names are arranged in alphabetical order. Both authors contributed equally to this research project.

Introduction

The banking system in Saudi Arabia is one of the strongest in the world. According to the International Monetary Fund (2006) report, Saudi Arabia prides herself as having a diverse financial system compared with other countries in the region. The financial system is largely focused on the banking sector where assets of 11 commercial banks operating domestically account for about one-half of total system assets. Further, all commercial banks hold universal banking licenses and manage mutual investment funds. Assets of the joint Saudi-foreign banks accounted for 49 percent of total banking sector assets at end 2003, compared with 53 percent in 1998.

Given the financial landscape of Saudi Arabia, it is of utmost importance that their commercial banks maintain a positive corporate image and reputation so as to communicate to banking customers that they are capable of handling any challenges caused by negative developments in the global banking system (Jasimuddin, 2001).

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Although Saudi banks possess a substantial amount of financial power, not every customer is aware that these banks have the unique opportunity of providing any form of financial product or service such as commercial banking, investment banking, security brokerage, and management of investment companies relating to open-end mutual funds and closed-end funds (Essayyad & Madani, 2003). This could be due to the lack of appropriate and extensive corporate communication efforts that confront most Saudi banks, influencing their overall corporate image and reputation.

Companies must closely monitor how customers perceive their corporate image and reputation and their main drivers. Although researchers such as Spector (1961), Dowling (1986), Fombrun (1996), Craven, Oliver and Ramamoorti (2003), Lee (2004) and Schwaiger (2004), have worked on the development of a scale to measure the intangible equity of a company, i.e. its corporate image and reputation, there is still a lack of consensus on valid scales (Nguyen & LeBlanc, 2001). This is especially so for scientific research on corporate image and reputation in the Middle East. In particular, our study will illuminate the understanding of corporate image and reputation in two ways: First, it will contribute to the body of knowledge in the field of corporate or marketing communications research, and especially to the knowledge of corporate image and reputation management of the banking industry in Saudi Arabia. Second, this research will shed light on customers’ perception of the corporate image and reputation of large Saudi commercial banks and identify the key influencing factors.

This research serves two purposes: First, it seeks to develop an appropriate way of measuring the corporate image and reputation of large commercial banks in Saudi Arabia by identifying a set of specific factors and items that contribute to the formation of the perceptions of banking customers. Next, it seeks to determine the perception of the customers on the corporate image and reputation of these institutions, by identifying the dominant factors that influence these perceptions and their implications. In addition, this study will attempt to answer the following question which serves as the Research Problem: (RP) How do customers assess the corporate image and reputation of large commercial banks in Saudi Arabia and what are the implications of building a good corporate image and reputation for these financial institutions?

We have further developed the following Research Questions (RQs) in support of the RP, as follows: (RQ1) What are the factors that affect the customers’ perception of the corporate image and reputation of large commercial banks in Saudi Arabia?; (RQ2) What are the dominant factors that determine if customers in Saudi Arabia perceive these financial institutions as having a good or bad corporate image and reputation?

**Overview of the Literature**

The literature reveals a variety of views or definitions of corporate image and reputation. The different schools of thought on corporate image and reputation over the past few decades, as provided by Gotsi and Wilson (2001), all focus on the notion that corporate image is: (a) the equivalent of reputation; (b) an important component within reputation; or (c) a broader term that encompasses reputation. There is no doubt that the two are
“closely allied elements and one is necessary for the other to be developed” (Markwick & Fill, 1997: 398). For example, Marziliano (1998: 5) believes that image answers the question “what do we believe we are?”, while reputation answers the question “what do we know about what others think we are?”. Balmer and Greyser (2003: 4) refers to corporate image simply as “how are we perceived now?”, and corporate reputation as “how are we perceived over time?”. It is difficult to specifically distinguish image from reputation as the perception of corporate image is formed “at a single point of time” whereas the perception of corporate reputation is formed “over time” (Cornelissen, 2004: 25). In this study, we will assume that the overall perception of banking customers of large Saudi commercial banks includes corporate image and reputation. As such, we adopt an integrative approach to defining corporate image and reputation by referring to Gotsi and Wilson’s (2001) definition of the two terms with reference from Gray and Balmer (1998), as follows: Corporate image and reputation is people’s overall evaluation of a company over time. This evaluation is based on any form of communication that provides information on the company’s actions, including a comparison with the actions of competitors.

Previous research indicates that having a favorable corporate image and reputation can provide a company with a distinctive and credible appeal (Greyser, 1999; Markwick & Fill, 1997), as well as a more effective form of differentiation and a source of competitive advantage (Dowling, 1993; Gray & Balmer, 1998). It is believed that corporate image is not just a matter of window dressing but can be a leading indicator of whether a company will survive in the future (Marziliano, 1998). A strong reputation gives rise to competitive advantage which is enough to guarantee stronger long-run financial returns (Fombrun, 1996). Roberts and Dowling (2003) reinforce this belief by suggesting that companies with a relatively good reputation are better able to sustain profitable outcomes over time. Greyser (1999) further summarizes the three key strategic benefits for companies with a good name: company preference, support in troubled times and value in the financial marketplace.

Lewis (2001), Wartick (2002), Schwaiger (2004), Cornelissen (2004) as well as Berens and van Riel (2004) have reviewed the different approaches to measuring corporate image and reputation. Berens and van Riel (2004) conducted an extensive review covering the period from the 1950s to the 2000s, identifying three main streams of thought. The first deals with the social expectation that people have regarding companies. The second considers the personality traits that people attribute to companies. The third examines the reasons that influence people to trust or distrust a company. On the other hand, the Fombrun Reputation Quotient is calculated using 20 attributes arranged in six major categories: emotional appeal, products and services, financial performance, social responsibility, vision and leadership, and workplace environment (Fombrun, 2003). Each dimension is then measured using three or four scales and the total reputation quotient is calculated by combining the ratings of all of the attributes. This is considered to be a direct and reliable way of measuring reputation. However, some scholars have pointed out that both the measurement approaches fail to consider the views of multiple stakeholder groups and appear to be primarily tapping into a firm’s financial performance and assets (Fryxell & Wang, 1994).
As early as the 1960s, Spector (1961) identified six dimensions of corporate image, which were empirically derived from evaluations of the personality characteristics of a company. These examined if the company was dynamic, co-operative, business-wise, of good character, successful and withdrawn. Davies, Chun, daSilva and Roper (2004) indicate that there is no general agreement on the validity of the use of personality traits in the case of organizations, but they use the personification metaphor as a measurement approach and draw up a list of possible characteristics from the psychology literature. Dowling (1986) argues that corporate image is formed by the company personnel and external groups encoding information related to both the actual company practices and its imaginary or attributed qualities, such as personal experience, interpersonal communication, and mass media communication such as advertising, and press releases, all of which project an image desired by the organization. Fombrun (1996) states that the elements of a company’s image include its relationships with the stakeholders, the marketing of brands, its financial performance and its interaction with the public during normal business operations and crises. According to Dowling (2004), the attributes of corporate image and reputation suggest two classes of factors; one is more factual in nature such as corporate capabilities and financial performance, while the other has a more emotional character such as social accountability and the distinctiveness or personality of the organization. Relying on such factors reduces the abstractness of the concepts (Bryman & Cramer, 2005), and a sound scale of measurement is important for any survey of corporate image and reputation. In short, the integrative definition of corporate image and reputation adopted for this study implies that corporate image and reputation is influenced by the “mental picture” the customers have of a company, and is also determined by the “consistent performance” and “effective communication” of a company.

A Conceptual Model

The conceptual framework shown in Figure 1 consists of four independent constructs. Two constructs, “Corporate Management” and “Financial Prospect”, are drawn from Lee’s (2004) study and one construct, “Market Presence”, is taken from Dowling (2004). The remaining construct, “Corporate Communication” is derived from the literature.

![Figure 1: Proposed Conceptual Framework](image-url)
Lee (2004) examines the reputation component of the corporate image of Hong Kong Telecom among young educated customers in Hong Kong. Her research explored seven factors of Overall Corporate Image, namely “Corporate Management”, “Quality of Products and Services”, “Treatment of Employees”, “Social Responsibility”, “Advertising and Marketing Activities”, “Corporate Dynamism” and “Financial Prospect”.

The construct, “Market Presence”, is taken from Dowling (2004) who combined several attributes from the Fortune corporate scorecard with others used in different systems of measurement to evaluate how journalists rated the corporate reputation of a small group of Australian organizations. The major contribution of Dowling’s work is the predictive ability of the four drivers of corporate reputation, namely “Market Presence”, “Corporate Capabilities and Performance”, “Social Accountability” and “Corporate Personality”.

The choice of these four constructs for this study is based on the unique characteristics of the banking sector in Saudi Arabia, whose portfolios are shaped by three factors based on the International Monetary Fund (2006) report. First, assets are substantially funded by low-cost demand deposits, accounting for up to 40 percent of total deposits where profitability is influenced by international lending rates. Second, the dependence of the economy on oil makes it difficult for banks to diversify risks domestically, particularly credit risk, necessitating high levels of capital and provisioning. Third, conservatism is further ensured by prudential arrangements that prescribe lending limits, including to connected parties, liquid asset ratios, require Saudi Arabian Monetary Agency’s approval for foreign lending, and impose statutory caps on individuals’ indebtedness. In this environment of “managed risks”, and with advanced asset-liability management by banks, stability has been assured but intermediation has remained modest.

The first three empirically derived attributes, “Corporate Management”, “Financial Prospect” and “Market Presence”, are factual in nature and have a reliability of $\alpha$ above the acceptable level of 0.7. The fourth independent construct “Corporate Communication” is supported by relevant theories on the formation processes of corporate image and reputation by such researchers as Abratt (1989), Van Heerden and Puth (1995), van Rekom (1997), Gray and Balmer (1998), Cornelissen (2000). This factor reflects the “mental picture” customers have of a bank and the “effective communication” between a bank and its customers, as described in the integrative definition stated earlier.

**Methodology**

We piloted the questionnaire to ensure both reliability and validity in two ways. First, we sent out the English version of the questionnaire to 56 respondents and with the data collected, we ran factor analysis and reliability test and the scores were acceptable. Second, we consulted seven academicians in the Accounting and Finance discipline to ensure external validity of the final instrument. The primary purpose was to obtain some
professional input on the suitability and utility of the survey questions (Sabate & de Quevedo Puente, 2003).

The finalized questionnaire contained 22 statements and these were translated into Arabic to ensure that a wide variety of banking customers could be approached. These items were submitted to the scale reliability procedure of SPSS 16.0. The Cronbach’s alpha for the entire construct was .94, a strong indication that the instrument is highly reliable and internally consistent. We further ran the reliability procedure with the option “the value of α if an item was deleted”. No increase of α was noticed if any of the items was deleted.

The questionnaire, presented in both English and Arabic, was conducted manually in the Eastern province of Saudi Arabia. A seven-point likert scale was used to help respondents evaluate their affiliated bank’s corporate image and reputation with “1” indicating “strongly disagree” and “7”, “strongly agree”. We invited respondents to rate any of the three largest commercial banks, namely Riyad Bank, National Commercial Bank and Saudi American Bank, as we believe most people would have an account with any of these banks. However, we also provided an option for the respondents to indicate a bank for which none of the three suggested banks would be an option. A total of 114 valid questionnaires were received.

We further tested the factor analysis assumptions to ensure the suitability of this technique in our analysis. KMO measure of sampling adequacy (.882) and Bartlett Test of Sphericity (chi-square = 1.668E3, df = 3, p<.001) support our use of factor analysis. The list of 22 items was submitted to factor analysis and the factor solution was rotated using a varimax rotation method. Three factors emerged, namely “financial prospect”, “corporate management” and a third factor which is a combination of “corporate communication” and “market presence” in addition to “overall corporate image and reputation”, the dependent variable.

Findings and Discussion

Our findings reveal that the way banks are managed and their communication with customers has a direct influence on the perception of corporate image and reputation of large commercial banks in Saudi Arabia. Comparing our findings with the literature, three of the constructs match Lee’s (2004) findings perfectly, namely “financial prospect”, “corporate management” and “overall corporate image and reputation”. As for “market presence”, our findings did not closely match those of Dowling’s (2004). Based on our small sample collected, only three of Dowling’s four items were loaded correctly with two additional items from “corporate communication” loaded in the same construct. For the purpose of discussion, we will label this combined factor as “corporate communication/market presence”. This suggests that customers are not sufficiently aware of the communication strategies employed by large commercial banks to enhance their market presence in Saudi Arabia.

We further modeled the relationship between the independent and dependent variables using multiple regression on “financial prospect”, “corporate management”, “corporate
communication/market presence” and “overall corporate image and reputation” respectively. Our findings show that the variables are highly correlated (.778). In addition, the coefficient of determination is .605, indicating that 60% of variation in the dependent variable is explained by the three factors. If the importance of the independent variables is rank-ordered, it is evident that “corporate management” (β=.454) takes the lead, followed by “corporate communication/market presence” (β=.342) and “financial prospect” (β=.141).

**Theoretical implications**

Although corporate communication has been regarded as an essential factor influencing the perception of corporate image and reputation (Cornelissen, 2000; Gray & Balmer, 1998), our findings suggest a different dimension to the relationship between “corporate communication” and “market presence”. Contrary to what the literature says, these two factors do not appear as separate variables in our study; they are somewhat integrated. Of the five items loaded in the combined factor, three belong to Dowling’s (2004) “market presence” and two from our literature-developed “corporate communication” construct. These two items, namely “news coverage about the bank is mostly positive” and “the bank has high media publicity” seem to suggest that publicity is an important determinant in a company’s market presence. Of the other two items belonging to “corporate communication”, only one observed variable is loaded as a standalone factor; hence, we have decided to drop it due to its insignificance as compared with the overall construct. Consequently, we propose a modified framework combining these five items into a new construct, “publicity and market presence”, as illustrated in Figure 2.

![Modified Conceptual Framework](image)

**Figure 2: Modified Conceptual Framework**

**Practical implications**

*Managing customer relationships positively in enhancing the image of corporate management.* Large commercial banks tend to be less personal because of their structured way of doing things, reflecting the level of flexibility of bank managers. As banking transactions become increasingly complex, there needs to be greater synergy between banking staff, especially frontline managers. This would require a top-town approach and
a strong buy-in to ensure strong participation, leading to a positive corporate management.

**Utilizing publicity strategies in enhancing market presence.** It is quite apparent that commercial banks are not publicizing enough to strengthen their corporate image and reputation. As more foreign-invested banks penetrate into the Saudi market, there is a greater need for existing banks to embark on a strategic publicity campaign to enhance their market presence. Being a leader in its field requires media and publicity support, requiring the marketing or corporate communications department to be fully attuned to market forces by working with leading advertising agencies to roll out a series of media activities.

**Communicating financial prospects as a means of enhancing customer confidence.** Although the financial growth of large commercial banks has been positive over the last five years in Saudi Arabia, these banks have not done enough to educate and disseminate the relevant information to the public. Information should be accurate and updated periodically, and be made available in a number of such channels as websites, brochures, newsletters and annual reports. In our study, it was found that the respondents were not fully aware of these publicity channels of large commercial banks. Even if the information was available in any of these outlets, it could be presented unattractively, deterring readership.

**Conclusions**

Our study is limited by the small sampling frame of the 114 valid questionnaires returned for the survey considering the potentially huge number of banking customers in the Saudi Eastern province. Further research could expand the sample size to cover a wider spectrum of customers in the other major cities such as Riyadh and Jeddah, which would be our next stage of model testing. This study is also limited by its use of quantitative data as the main stage of data collection to ascertain the perceptions of corporate image and reputation. The questions were not open-ended and this set limits on the scope of the information gathered.

A mixed-method approach, combining both quantitative and qualitative data collection techniques could have been integrated into the main stage as it would reinforce the empirical evidence produced by perception studies such as this one. According to Denzin & Lincoln (1994), using rich qualitative data would be a meaningful way of explaining, supporting and theorizing social science phenomena.

Recognizing the growing importance of corporate governance and social responsibilities for large commercial banks in Saudi Arabia, aspects which are not investigated in the present study, and how far behind these banks are in these aspects, the following research question is proposed for further empirical exploration: *How do customers assess the corporate governance and social responsibility of large commercial banks in Saudi Arabia and what are the implications for these institutions for the future development of their corporate image and reputation?*
References


From SERVQUAL to Competitive Advantage: A Higher Education Perspective

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Abstract: The paper explores the influences of service quality in higher education and their contribution to the overall performance of a higher learning institution in Singapore. It draws on the underpinnings of SERVQUAL, and discusses the dichotomy and interrelation between customer perception and expectation in response to current tertiary contexts. Long-term quality excellence of support services can be achieved by short-term measures such as training staff to be student-centered rather than task-driven. Service quality, therefore, needs to be evaluated on the basis of an integrated experience which occurs in a network of learning spaces created to promote dialogue, inquiry and reflection.

Key words: Course Delivery; Customer Satisfaction; Service Quality; Support Services; Higher Education

Introduction

Quality is not an act; it is a habit.
- Aristotle

Over the years, service quality has been regarded as the key to organizational progress and competitive survival. However, some organizations have realized that emphasis on products alone may not be the answer to survival and growth. In fact, technological know-how and continuous improvement have given organizations the impetus to increase their product quality by matching it to their customers’ expectations (Eisingerich and Bell, 2008; Lawson, 1992). Even so, it has come to a point where product quality is no longer the sole measurement of competitive advantage; what has been perceived to be of greater importance is service quality (Cronin and Taylor, 1992; Dagger and Sweeney, 2007). The underlying contention is one of an ongoing pursuit (habit) rather than a transitory outcome (act), according to Aristotle.

Competition in the service industry is driven by the perceived level of service quality offered to internal and external customers since there are no actual products involved (Babakus et al., 2003; Lewis and Smith, 1994). In this context, we regard higher education as being associated with the service industry since the primary focus in tertiary education

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Institutions is to provide quality learning experiences to students. As an example, the educational scene in Singapore is driven by much competition with institutions developing specialist and interdisciplinary courses to cater to a wide variety of students in addition to a gamut of competition projects, industry collaborative research and other community involvements to enhance the overall learning experience. Increasingly, institutional management and administration have become more systematized and efficient. For instance, in their quest for excellence, many institutions have adopted the benchmark systems such as the ISO 9000 and Singapore Quality Award (SQA) – two uppermost desirable service quality achievements commonly striven for by organizations in the commercial sector. The SQA was established in 1994 to help Singapore organizations attain world-class standards of business excellence. The business excellence model underpinning the SQA is based on universally accepted standards that are found in the US Malcolm Baldrige National Quality Award, the European Quality Award and the Australian Business Excellence Award (Quazi and Padibjo, 1998). A fundamental emphasis of ISO 9000 and SQA is being customer focused.

In this study, we will draw on the experience of a higher learning institution in Singapore, whose pursuit in service quality has been based on the guidelines of ISO 9000 and SQA to achieve management and administrative excellence. At the point of research, the institution had already attained ISO 9000 certification and was working towards achieving SQA. As a prerequisite to SQA, organizations must have attained the Singapore Quality Class and this intermediate award was achieved by the institution in July 1999. In working towards SQA, the institution’s aim is to diversify the service quality development strategies within each academic school yet to centrally monitor their outcomes periodically by referring to the SQA guidelines. For this research, we will focus on the Engineering School as it is the largest academic unit in the institution and has a strategic service quality plan leading to a number of initiatives. Hence, the purpose of this study is to explore the perceptions of service quality within the School and examine if these perceptions are aligned to its strategic objectives. In particular, we raise a pertinent question which serves as the Research Problem: (RP) What are the factors that influence service quality in higher education and how do they contribute to the overall performance of a higher learning institution?

Summary of the Literature

Is education a type of service?

Differentiation between products and services can be evaluated in terms of the level of tangibility, such that services are characterized by behavioral attributes including acts, deeds, performances or efforts (Rossi et al. 1999) and activities or processes (Grönroos, 2001). According to Parasuraman, Zeithaml and Berry (1988), characteristics associated with services include intangibility, perishability, inseparability of production and consumption, and heterogeneity. In contrast to products, services are usually short-lived as they are consumed as long as the activity or process lasts. Hence, service processes are perishable and cannot be stored in the way physical products can. Further, services are consumed at the same time as they are produced without any clear transfer of ownership.
As such, the customer plays an integral part in the transaction of most services. For instance, each customer’s expectation of service quality is different and this has led to a lack of standardization as it varies from situation to situation (Boulding et al., 1993; Widrick et al., 2002).

In this context, educational processes in the form of lesson delivery, advising, counseling and project supervising can be regarded as a type of service provided to students who assume the role of customers. The service quality of each learning experience, particularly in higher education, is unique as it is largely determined by the expectation of the student, also the individual customer. This expectation varies between experiences derived from intellectual engagement and outcomes of examination. As such, the need for an acceptable definition of service quality in higher education cannot be overemphasized. We first address this concern by discussing the notion of “customers” in higher learning contexts.

Rinehart (1993) offers two distinct views of students as customers; for instance, those who regard students as primary customers associate them as being involved in the input and output of the learning process. However, those who regard students’ potential employers as primary customers argue that it is important to consider the economic reality of the situation where lesson contents should be tailored to employers’ needs. Students, in both contexts, have been regarded as internal customers with the second group regarding future employers as external customers. Jaraiedi and Ritz (1994) as well as Clewes (2003) further argue that students have no conception of what they need to learn; as such, education is preparing them for the long-term benefits of the future. It is with this long-term view that potential employers are regarded as primary customers while students, secondary customers.

In another view, students have been categorized as the primary beneficiaries of education and hence should be treated as customers. This perspective stems from the understanding that educational institutions are highly competitive on the market with strategies being aggressively developed to satisfy student needs in order to attract a sustainable market share (Altbach and Knight, 2007; Joseph and Joseph, 1998). Secondary beneficiaries, in this context, would include parents, the marketplace and society at large. The interplay between the two beneficiary types is, to a large extent, time and event specific. For instance, within a classroom context, students are customers to teachers; however, when students are working on an assignment for teachers, the latter becomes the customer (Johnson and Golomskiis, 1999; Wright and O’Neill, 2002).

Yet, there is another view of students being associated with customers and products. McCollough and Gremler (1999) argue that service guarantee should be fundamental consideration in any educational institution and this includes both customer and product satisfaction. The implication is that if the external customer (employer) is not satisfied with the quality, the product (student) may be returned to the manufacturer (institution) for further inspection (Naumann and Giel, 1995). As an example, Durham College in Ontario, Canada, offers a mutual-benefit agreement between employers and students, an initiative launched in 1994. The College provides a satisfaction guarantee to employers of
their alumni in positions related to their major academic disciplines. If a graduate of the College is not performing to the level as expected by the employer, the agreement allows this alumnus to be “returned” to the institution for further training with no additional cost incurred by the sender. As a parallel to industry standards, the ultimate goal of higher education is the “production” of students who are equipped with both the intellectual and practical qualities that will contribute to optimal job performance (Srikanthan and Dalrymple, 2002; Worthen and Sanders, 1973). In this context, we develop our first Research Question in support of the RP: **(RQ1) Why is customer focus an important factor of service quality in higher education?**

**How is service quality measured in education?**

Much of the research of the measurement of service quality within educational settings has been influenced by the seminal work of Zeithaml, Parasuraman, and Berry (1990) based on the SERVQUAL model from which a 22-item instrument for measuring customer expectations and perceptions have been developed along with five quality dimensions: tangibles, reliability, responsiveness, assurance, and empathy. This methodology operates by means of identifying “expectations” and “perceptions”, with the aim of closing the gap between the two. These can be demonstrated in the following five dimensions in relation to educational settings.

1. **Not knowing what customers expect.** Institutions should be prepared for the shifting needs of their customers (students) in providing courses and training programmes that are relevant in subject matter and teaching approaches. The learning process is expected to be academically rigorous, yet with a certain degree of flexibility in areas pertaining to course selection and assessment. With the advent of technology, course design and delivery are expected to be progressive wherein the innovative and spontaneous construction of knowledge should be the byproducts (and process) of learning.

2. **Inadequate service quality standards.** It is sometimes a challenge for institutions to exceed customer expectations and demands. For instance, a shortage of teaching staff and the need for optimal enrolments have seen an increase in class sizes, stretching the teacher-student ratio. This has implication on the level of individual attention given to each student inside and outside class. Further, with teachers are expected to assume multiple roles including curriculum writing, stand-up teaching, mentoring, project supervising and administrative responsibilities, the level of service quality may become less standardized and desirable over time.

Taking into consideration these two dimensions, we develop our second research question: **(RQ2) How does course design and delivery contribute to service quality in higher education?**

3. **Service performance inconsistencies.** The challenge for institutions is to ensure that service specifications such as course content, delivery and application meet the expectations of their customers consistently. This is a precarious concern as performance associated with these “specifications” is highly context-driven based on a variety of
factors, sometimes beyond the control of the actors involved. Learning experience and orientation at large cannot entirely be evaluated by grades alone; service performance should go beyond tangible forms. In addition, learning objectives need not necessarily lead to outcomes that are strictly quantifiable. As some would argue, the relevance of any course can only be evaluated years later when knowledge and skills acquired by students are usefully applied in professional contexts.

4. When promises do not match delivery. Discrepancy between promise and delivery is largely the result of inaccurate communication of some institutions from advertisements, road shows and exhibitions. These institutions tend to oversell their services, leading to grand promises that misrepresent their actual potential and academic readiness. For instance, one of the most common strategies is the promotion of facilities and support services, ranging from “hardware” to “software” needs. Some institutions boast of their state-of-the-art technology used in laboratories, computer systems and other learning facilities. On the “software” front, common concerns include the number of student clubs, activities, counseling and medical facilities, and entertainment outlets.

5. Level of tolerance as a result of the first four dimensions. Judgment of high or low service quality largely depends on how the customers perceive the actual service performance in the context of their expectation. The level of tolerance in service standards differs across all areas; for instance, the more important the area, the smaller the boundary of tolerance. Customers’ willingness to modify expectation of service standards can be appropriately managed through the availability of choices. These should diversify the expectation levels of customers in a way that the shortcomings of one service can be offset by the strengths of another. Hence, from the holistic perspective of education, support services and facilities should play an equal, if not an even more important role, in contributing to the overall service quality in higher education (Parasuraman et al., 1988; Srikanthan and Dalrymple, 2002).

In summary, the final two dimensions have led us to develop our third research question: *(RQ3) What support services are required to enhance service quality in higher education?*

A Conceptual Framework
The Engineering School’s service quality framework has been developed based on the five dimensions of the SERVQUAL model (Zeithaml et al., 1990). We used Figure 1 as a prior theory to guide us in this exploratory research.

*Figure 1: A service quality framework*
Customer focus

The School has classified their customers into three distinct yet interrelated groups: employers of its graduates, current students and their parents. Performance of this strategic objective is evaluated by the “employer satisfaction survey” and “student satisfaction survey”. In addition, focus group discussions involving employers and parents constitute another feedback mechanism to ascertain the level of customer orientation.

Quality course design and delivery

Performance in this area is largely determined by the “student satisfaction survey” and “graduate employment survey”. Feedback gathered from the former survey provides a sounding board for the School to fine-tune its curricula and course delivery gradually, while the latter survey provides a double-feedback channel through which more broad-based and industry-relevant perspectives are considered. For instance, it is believed that graduates having been employed should be in a better position to comment constructively on the quality of the course design compared with current students.

Quality support services

Satisfaction in this area is evaluated by the number of compliments and complaints about the School’s support services. Students are encouraged to submit comments, suggestions or complaints via online channels to help the School improve their support service further. Quality expectations include the availability of facilities such as computer and technical laboratories, printing and internet facilities, as well as administrative and technical support from staff.

We now provide some examples of the instruments developed to evaluate customer satisfaction in educational settings. These include the Classroom Environment Scale (CES), My Classroom Inventory (MCI) and Individualized Classroom Environment Questionnaire (ICEQ) developed by Watkins and Hattie (1990). One of the most widely-used instruments in USA is the College Student Experiences Questionnaire (CSEQ) (Pike, 1995) while the Course Perception Questionnaire (CPQ) (Ramsden, 1991) has gained acceptance in Europe and Australia. According to Marsh and Bailey (1993), one of the most popular instruments is the Student Evaluation of Education Quality Questionnaire (SEEQ) introduced in Australia. However, it has been found that these instruments focus primarily on the teaching aspect based on the student’s experience (Cuthbert, 1996; DiDomenico and Bonnici, 1996; Entwistle and Tait, 1990).

The relationship between learning and teaching is not necessarily straightforward as much depends on the approach to which students adopt in their learning process. In this context, a student’s experience involves much more than simply teaching and learning. As a consequence, none of the available instruments would be able to completely account
for service quality in higher education. Adaptation of the SERVQUAL model would be considered an appropriate means for evaluating service quality in educational settings (Coleman, 2003; Cuthbert, 1996; Entwistle and Tait, 1990). The advantage of this model over those from the student learning literature is that it encompasses the whole-person experience rather than the experience of teaching. The SERVQUAL approach is one that integrates both the dimensions of perception and expectation, taking into account that students rating questionnaires tend to be influenced by their recent assessment experiences, thereby affecting their decisions. Asking students to consider their expectations as well as experiences provides an opportunity for reflection based on personal desires and contextual considerations. This way, rating and feedback provided by students would be more objective and less erratic. In order to strengthen the interrelations between expectation and experience, the Engineering School has aligned its service quality strategies to its corporate objectives by focusing on three key variables of Figure 1.

Methodology

We employed an exploratory orientation in our research by means of structured interviewing as the rich qualitative data gathered would be useful in providing insights into the issues being investigated (Lee, 1999). We adopted a purposive sampling frame as our aim was to select respondents who were able to provide a wide, longitudinal range of views pertaining to service quality in higher education (Cohen and Manion, 1994). In order to gather varied views, we limited our sample size to 12 subjects and categorized them into three groups: management staff (M1-M4), section heads (S1-S4) and lecturers (L1-L4). Management staff include deputy directors and course managers while section heads are subject leaders. All respondents had at least three years of teaching experience within the Engineering School and the sample comprised equal numbers of males and females. According to Wellington (2000), the total number of subjects considered for this study is adequate as the 12 acted as key informants to this qualitative research, allowing in-depth issues and views to form the core of theory-elaboration.

We further conducted a pilot study to ensure that the interview questions were clear to an initial group of four respondents. These included a management staff, a section head and two lecturers, representing a cross-section of the actual sample. The pilot interviewing took an average of 45 minutes. Based on the respondents’ comments and suggestions, the questions were fine-tuned to form the finalized interview protocol used in the subsequent stage. The final interviews each lasted about an hour and probes were used to elicit deeper issues involved in the RP and RQs.

The data was analyzed using a manual approach through the technique of thematic categorization (Holliday et al., 2002). Thematic headings were developed based on the research problem and questions, and with close reference to the literature. This helped us to ensure construct validity of the data as the views were gathered in strict accordance to the interview protocol. External validity was achieved through the use of a pilot study to ensure clarity and consistency of the questions asked (Krejcie and Morgan, 1970). The raw data was further coded at different levels to allow underlying themes and patterns to emerge. Word recurrence, repeat phrases, convergence of anecdotes and examples in
addition to general (dis)agreements were closely observed in the treatment of the data. The research questions, in particular, and the probes used were useful in helping us formulate thematic categories to reduce the data further in meaningful ways. Reliability was established by matching the analyzed data to the research problem, questions and probes to determine the amount of variation (Llusar and Zornoza, 2000).

**Discussion and Implications**

*(RQ1) Why is customer focus an important factor of service quality in higher education?*

The perception of tertiary students as customers or products is not necessarily straightforward. Our findings reveal that 50% ($n = 6$) of the respondents regarded students as predominantly customers, while 16.7% ($n = 2$) regarded them as products. Yet, 33.3% ($n = 4$) perceived them as both customers and products depending on the context in which the subjects will be assessed. For instance, a key theme that has arisen from the data provides a fundamental direction to which tertiary students should be judiciously treated, that the view of “customers” would be appropriate if a marketing perspective was adopted where satisfied students would increase the profile and popularity of the institution. In contrast, the view of “products” could be adopted if students were considered as outcomes of the educational system to be prepared for the industry and society. Hence, the dichotomy between “customers” and “products” is largely context-driven and each perspective will have a different influence on the way service quality might be developed in the institution (Dagger and Sweeney, 2006; Perry, 1991; Rinehart, 1993). It is with this observation that we develop our first proposition ($P$) with reference to Athiyaman (1997), Cuthbert (1996), Owlia and Aspinwall (1998), and Wright and O’Neill (2002), as an extension to Zeithaml, Parasuraman and Berry’s (1990) SERVQUAL model.

$$ (P1) \text{Views of students as customers or products are context-driven and the interplay between the two influences the way in which service quality in higher education will be perceived, evaluated and upheld.} $$

The type of perception given to students determines the affective relationship between teachers and learners. Our findings further reveal that those who adopt a customer-orientation tend to demonstrate a human dimension to their interaction with students, while those who adopt a product-orientation tend to be more mechanistic in their approach to human relations. The underlying issue concerning this perception dichotomy, therefore, raises the question of intent on the part of the teachers whether to view their network of association as an organism where satisfaction is derived from the learners’ continued growth and renewal (Argyris, 1982), or a machine where the primary preoccupation is to repair any part that might hinder routine operations (Taylor, 1911). In this context, we draw on Zeithaml, Parasuraman and Berry’s (1990) notion of service quality as being associated with the dimension of empathy in the SERVQUAL model, which suggests caring and individualized attention given to customers. According to Hill (1995) as well as Babakus, Yavas, Karatepe and Avci (2003), empathy in higher education stems from the premise that students are delicate and valuable entities, and should be sensitively dealt with. He suggested that even the simple act of listening to
them would be perceived as a type of service performance credited to the institution. In this context, we develop our second proposition:

(P2) Intent and empathy of teachers cannot be overemphasized as these are attributes that can transform mental models of students and recreate the classroom into an extended learning space where the interaction dynamics will engage the whole person rather than a portion, the mind.

Interpretation of service expectation should be consolidated rather than distributed in order to achieve a baseline for continued evaluation. This assumption is enmeshed in Zeithaml, Parasuraman and Berry’s (1990) theory that an appropriate interpretation begins with the narrowing of the disparity between perception and expectation. We also draw on the propositions of Ford, Joseph and Joseph (1998) Owlia and Aspinwall (1998), and Widrick, Mergen and Grant (2002) that interpretation can sometimes be influenced by individuals’ prior knowledge and experience in higher education, as it is a required process that provides some understanding on why expectations may change from time to time given the increased familiarity with a particular service. To allow the role of interpretation to maneuver within reasonable boundaries, we refer to Hill’s (1995) as well as Srikanthan and Dalrymple’s (2002) suggestion that students’ expectations should be evaluated progressively within an acceptable timeframe, for instance, from enrolment to graduation. In order to narrow the interpretation between perception and expectation, we develop our third proposition:

(P3) Clarification of expectations to meeting students’ needs is fundamental to the understanding of service quality in higher education. Communication of judiciously-defined expectation outcomes is vital to the facilitation of conditions for the achievement of desired service standards.

(RQ2) How does quality course design and delivery contribute to service quality in higher education?

Findings reveal that the comprehensiveness in the evaluative measures of teaching effectiveness as associated with increasing service quality can sometimes lead to adverse effects. While it is appropriate to conduct periodic teaching observations by supervisors, the underlying intent of linking the requirement to performance appraisal has led to an overall experience that is rather mechanistic. Further, the auditing process sometimes extends to the collection of feedback from students regarding teaching effectiveness. The general sentiments reflected in the interviews have led us to conclude that an over-reliance on external measures to bring about the intrinsic value of teaching and learning may not be completely feasible in today’s changing educational contexts where spontaneity and innovativeness count towards creating an essential learning experience for tertiary students (Altbach and Knight, 2007; Harvey and Green, 1993). We are mindful of the management strategy of the Engineering School, that is “to build an educational system that prepares students effectively to meet employers’ expectation”, and further suggest that teaching effectiveness be evaluated based on a systems
perspective which takes into consideration the public and private teaching “spaces” of teachers. Hence, we develop our fourth proposition:

(P4) Systems related to the facilitation of effective course delivery are necessary mediating agents that support teachers’ quest for continued professional improvement and development. However, these should not be established for the purpose of increasing organizational profile nor as criteria used to assess teaching competence in performance appraisals.

At the point of research, the Engineering School, in their quest for continued growth and renewal, had established several initiatives to support the teaching competence of their academic staff. One of these was “promoting good teaching practice” which involved the creation of “teaching and learning effective circles” as part of their total quality service strategic orientation. This initiative brought together teachers as project teams to be involved in reflective thinking and action to bring about a wider dimension of teaching and learning, as supported by the works of Eisingerich and Bell (2008), Holmes (1993), Muller and Funnel (1993), Ramsden (1979, 1993), and Trigwell and Prosser (1991). According to Carlzon (1987), the essence of teaching effectiveness lies at the heart of individual interaction within a specific context, which he calls “the moment of truth” where enlightenment is revealed in the human dynamism of meta-cognition.

Another perspective on the quality of teaching and learning is proposed by Narasimhan (1996) as involving informal ways of evaluating teaching effectiveness. He has developed a “teaching and learning situation inventory”, arguably an extension of SERVQUAL, that can quickly account for the differences in expectations between teachers and their students on what constitutes an ideal session. The “inventory” helps identify the possible gaps between these expectations and assist teachers to decide if modification in terms of perspectives, course content and/or delivery style would be required for the achievement of teaching excellence. Narasimhan’s (1996) discovery is that learners are generally concerned about the applicability of knowledge learnt in class to the external world. In this context, teachers will need to keep current knowledge on industry trends and technological developments to provide a balance between theory and practice in the course content. According to a framework developed by Clewes (2003) as well as Owlia and Aspinwall (1998), such factors as relevance of curriculum to the future jobs of students, primary knowledge skills, use of computer, communication skills, team working and flexible utilization of knowledge collectively contribute to the overall service quality of higher education. It is with this reference that we develop our fifth proposition:

(P5) Students’ learning experience can be greatly enhanced by acquiring knowledge and skills that have lifelong impact. This requires curricula that are designed to incorporate a balance between theoretical and practical perspectives with an applied emphasis on industrial relevance.

Another of the Engineering School’s management strategies is to enhance the value of staff so as to achieve staff and customer satisfaction, taking into account staff development, involvement and well-being. However, our findings reveal that the relationship between staff development, and the quality of course design and delivery is
not firmly established. This observation is in line with the study of DiDomenico and Bonnici (1996), which reveals that the level of competence of university professors does not commensurate with students’ satisfaction of their learning process. Hence, the linking mechanism between teachers’ competence and the quality of learning experience could be further established. We further draw on the work of Coleman (2003) as well as Owlia and Aspinwall (1998) to provide some explanation on the relationship between the two variables. They view competence of teachers as dealing with theoretical and practical knowledge, including the extent to which teachers are kept updated in their subject areas, and their expertise in classroom delivery and communication. We adopt this definition and describe in the following proposition the possible linkage between teachers’ competence and service quality in higher education:

(P6) Competency in both theory and practice of teachers is a key asset to the transformation of learning experience within and outside the classroom for learners. The success of knowledge facilitation within learning communities begins with the fundamental utilization of teachers’ core skills in simplifying complex concepts for the relevance of the current environment.

(RQ3) What support services are required to enhance service quality in higher education?

Findings reveal that the quality of educational service is not limited to the unique experiences that take place within the confines of classrooms. The wider spaces of learning and social interaction involving such facilities as laboratories, libraries, computers, sports and healthcare centers as well as cafeterias are largely contributive of the total service quality of any institution. For instance, a study by Clark and Ramsay (1990) reported that high-achieving university students were found to have made extensive use of support services. According to Zeithaml, Parasuraman and Berry’s (1990) SERVQUAL model, support services have been classified as “tangibles” which include physical facilities, equipment and the professional appearance of staff. Emphasis on support services provides an additional dimension to the total learning experience in higher education (Dagger and Sweeney, 2007; Patterson, 1991; Srikanthan and Dalrymple, 2002). Its importance is evident in the increasing demand for package deals in international educational institutions. A study by Brown (1991) on Australian tertiary institutions attests to the need to consider academic and facility excellence as a means to attract international enrolment. As global education increases in competitiveness, it is crucial that service quality be evaluated from a broad-based perspective. A study by Steadman and Dagwell (1990) reported that students’ overall satisfaction was, to some extent, negatively affected by their low evaluation of general and library facilities despite their high regards for the quality of courses and teachers. It is in this context that we develop our seventh proposition:

(P7) Satisfaction in any learning experience goes beyond the classroom; it requires fulfillment of the diverse aspects of that experience through supportive facilities, systems and processes. Taken together, these will promote an environment that motivates self-directed and team learning continually supported by a variety of learning networks and infrastructures.
Findings further reveal that there are adequate facilities and support services provided by the Engineering School but with low levels of utilization by students. A general sentiment that has emerged from the interviews points to the possibility that the poor utilization could have been due to two factors: the availability of facilities after office hours and the general attitude of support staff. In order to encourage utilization of these resources, one of the key concerns is that support staff need to be service-oriented rather than merely being administratively efficient. This phenomenon, as perceived by Solomon (1993) in her study on TQM in tertiary institutions, is one that should be carefully addressed. Changing employees’ mental models about quality requires clear direction from the management and the strategic influence of leadership. In order to enhance collective mental models, a shared vision on the philosophy of quality as influencing the overall institutional performance is essential. In achieving a shared cognition on how quality is to be interpreted and institutionalized, regular feedback and dialogue with all levels of employees are necessary. In addition, an appropriate deployment of human resources and allocation of responsibilities are crucial to creating the conditions for achieving quality service in support services. In this context, we develop our final proposition:

\[(P8) \text{Quality of an educational service can be achieved by having the right human resources as contributing to the success of multifaceted experiences created to develop learners’ knowledge- and skills-based learning needs and expectations further. A strong mindset to serve rather than to instruct is fundamental to the acceleration of service standards in educational settings.}\]

**Implications for practice**

On customer focus, we suggest that students be viewed either as “customers” or “products” in appropriate contexts. As reinforced by an interviewee:

(M3) “…as customers, we need students for marketing our courses, capability…they are our ambassadors and will influence their peers…[as] products…after three years we must make sure that they have the necessary skills as they will be deployed in the industry.”

There is a need to further enhance the relationship between teachers and students even beyond regular contact time. In order to promote trust and reliability between them, regular dialogue sessions highlighting positive examples of optimal lecturer-student rapport and sharing techniques on improving the relationship would be useful to teachers. In addition, the management of student expectations is of utmost importance to ensuring appropriate service quality in higher education. As these expectations may change with time and space, the management should facilitate a clear understanding between teachers and students on an achievable level of expectation. The following comment attests to this need:

(M1) “…we have to define what ‘expectations’ mean. Their (students’) responsibility to learn is theirs but it becomes ours (lecturers) in providing the right environment for their learning. Do not also confuse meeting [customer] expectations as giving students easy handouts and quizzes.”

On quality course design and delivery, we suggest that course curricula be reviewed periodically to ensure a good mix of theory and practice including such fundamentals as technological know-how and lifelong skills.

with industry partners should be also encouraged as they provide useful feedback on curricula relevance. This was expressed repeatedly during the interviews, as represented by:

(L3) “… I strongly feel [that] going for industry attachment will provide [lecturers] with [a] better feel on what is the practice in the industry.”

In addition, the management should reevaluate their annual performance appraisal system to identify wider attributes pertaining to teaching quality. We propose that good teaching is a lifelong pursuit and should not be confused with appraisal achievement. For instance, teaching efforts could be recognized not merely by teaching evaluation (provided by students) and teaching observation (provided by supervisors); instead, they should be evaluated based on different teaching-related activities. Teacher competence is another issue that should be carefully dealt with. As agreed by all interviewees, theoretical and applied competence will inadvertently deteriorate over time if teachers do not keep themselves abreast of updated research and industry trends. Hence, teacher competence should be reviewed every three to four years with optimal opportunities provided for the upgrading of knowledge and skills. This concern was unequivocally summarized by an interviewee:

(S3) “Every three years there is a course evaluation… Industry dialogue sessions should be conducted and information of these sessions should be shared with staff [lecturers]. Corrective action can be taken, if any… I think different courses demand different levels of competency… most lecturers are competent in their own subject areas…I think the course should have a team vested with the responsibility to ensure content quality. Subject leaders and peers should also help lecturers… [for example through] peer [teaching] sit-ins…”

On quality support services, we suggest that this aspect should relate to a larger group of people including teaching, administrative and technical staff. Quality service, in this regard, also involves the availability of facilities that support the learning process and well-being of students. As such, the point of contention hinges on the effectiveness of resource allocation and utilization. As expressed by an interviewee, these services should be differentiated, not generalized:

(M4) “Support services should be identified by core areas…or critical areas… [so that there is a] clear service level…there may be too many support services… we should really identify the core [ones].”

Response to students’ needs in any specific area should be provided promptly and professionally in order to achieve a broad-based yet in-depth educational experience for today’s students. In this context, strategic deployment and training of staff would be required to ensure that service standards are kept to an optimal and relevant level. The following view exemplifies the need to keep support services focused:

(S4) “…to clearly define the type of services supported by a particular group of the department… instead of spending time to find out the suitable staff that can provide the service… provide work instructions for each department.. services provided by each specific section should be made known.”
Finally, it is essential to promote the right mindset for staff to be student-centered rather than merely task-driven; the former suggests customer orientation while the latter, rules and regulations. For the long-term quality excellence of support services, short-term measures need to be considered. According to an interviewee, one of the issues is that:

(M1) “The current KPI (key performance indicators) do not require any measurement on support services.”

Nonetheless, some of the possible ways to encourage positive mental models and personal mastery would be to enforce a shared vision of excellence mediated through the recognition of good service, regular dialogue and sharing of good practices in addition to personal coaching and counseling (Senge, 1990), as encapsulated in the following quote:

(S1) “We…should try to inculcate the desire to give good service as a culture.”

Limitations and Future Lines of Study

Although the study focused on three key aspects of service quality management in the Engineering School, views generated from the interviews were somewhat limited. This was due to the lack of a more cross-sectional sample which should involve both teaching and non-teaching staff as well as students. Views from external customers (Jaraiedi and Ritz, 1994; Widrick et al., 2002) such as graduates and perhaps their employers could have been sought to provide a more balanced analysis. Further, it would have been ideal if data could be collected on a longitudinal basis over several years to explore and evaluate the different facets of service quality that could have changed with time and expectations (Athiyaman, 1997; Babakus et al., 2003; Hill, 1995). The current study could have also considered triangulated data such as student satisfaction survey results, teaching evaluation reports and other service performance indicators to provide a wider empirical dimension to the issues investigated (Bell, 1993; Wright and O’Neill, 2002). Finally, the study only concentrated on the Engineering School and the results explored might not be representative of the institution as a whole. A cross-comparison of the strategies adopted by the different academic schools would have contributed to a better understanding of service quality in this higher learning institution.

Still, the study has shed some light on the interpretations of service quality in higher education and how different perceptions associated with it can be integrated to provide a practical framework for the continued achievement of service excellence. The study could be complemented by an explanatory dimension where key relationships would be investigated through quantitative means. The use of questionnaire surveys would serve to capture a much wider data set to evaluate both perception and performance in terms of the specific aspects of service quality (Cronin and Taylor, 1992; Lawson, 1992; Widrick et al., 2002). In addition, the framework (Figure 1) developed for this study could be further tested through the development of scale items pertaining to each construct.

One the conceptual front, it was discovered that appropriate systems should be implemented to facilitate a community of teaching practice across all course levels. Future work could explore the relationship between systems development and teaching effectiveness to determine how personal mastery can be integrated with team learning to enhance individual competence (Senge, 1990). Another issue discussed relates to the
mental models of both academic and non-academic staff in providing service quality. Although such individual attributes as attitude and motivation may be difficult to modify over a short period, given the right stimulus through, for instance, an appropriate reward and compensation system, mental models can be changed for the benefit of the institution. Further work could focus on a strategic stimulus-response system to encourage positive mental models, developed through an integrated human resource perspective (Skinner, 1972).

In summary, we concur with Garvin’s (1988) view that service quality is a complex and volatile issue, largely driven by contextual uncertainties. As such, any study that attempts to unravel the complexity of service-quality definitions and assumptions requires a fundamental preparedness to withstand the test of time.

References


TRUST TOWARDS FASHION BRANDS CLOTHING: EFFECT OF CULTURAL AND INDIVIDUAL FACTORS AMONG BRITISH MUSLIMS IN THE UK

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Abstract: Studies have suggested that a number of factors contributed to trust. In UK, ethnic minorities represent 7.9% of the total UK population and are growing at 15 times the rate of the white population. Due to their high population growth, it has becoming increasingly important to understand the factors that influence trust among these ethnic minorities. Thus, this research aims to investigate the effect of cultural factors (acculturation, ethnicity and generation) and individual factors (self image congruence and religiosity) on British Muslims consumers’ trust towards fashion brands clothing in the UK.

Introduction

Despite the recent interest among consumer researchers regarding the impact of trust in relationship marketing success (Morgan and Hunt 1994, Sichtman 2007, Chaudhuri and Holbrook 2001, Delgado-Ballester and Munuera-Aleman 2001, Reast 2005), there is a gap in our understanding about factors contributed to consumer trust on brand. Specifically, little is known about the cultural and individual factors effect on consumer trust towards a brand. Given that the role of ethnicity has been neglected in the literature on relationship marketing issues such as trust (Burton 2000), this research aims to investigate the effect of cultural factors (acculturation, ethnicity and generation) and individual factors (self image congruence and religiosity) on British Muslims consumers’ trust towards fashion brands clothing in the UK.

Trust and Fashion Brands Clothing

Various studies in the literature have proven that trust has significant impact on marketing success such as brand loyalty (e.g. Morgan and Hunt 1994, Chaudhuri and Holbrook 2001), commitment (Delgado-Ballester et al. 2001), brand extension acceptance (Reast 2005), increase in market share and relative price (Chaudhuri and Holbrook 2001), positive effects on purchase intention and word of mouth behaviour (Sichtman 2007).

Clothing is seen as one of the main tools of expressing one’s identity, since it is a very visible part of personal consumption (Horn and Gurel 1981, Piacentini and Mailer 2004). Therefore, the element of trust is relevant in fashion brands clothing choice because of the symbolic meaning attached. According to Elliott and Yannopoulou (2007), in the
case of symbolic brands, consumers have to trust the brand in order to make a purchase choice. This is because product that has symbolic meaning involves higher risk (e.g., Schiffman and and Kanuk 2007, pp. 183) and thus trust between the consumer and brand is needed so that the risk involve in the clothing choice can be eliminated. In other words, trust is needed because wrong choice of clothing may results negative consequences on the part of the consumer.

Ethnic Minority Consumers in the Uk

The Census 2001 indicated that the ethnic minorities represent 7.9% of the total UK population and are growing at 15 times the rate of the white population (UK National Statistics 2001). One of the fastest growing ethnic minority segments is the Muslims. The population is growing fast over the last five decades from 21,000 to 1.6 million and likely to be doubled by 2021 to around 3 million (Lewis 2007, pp. 20). This group has also been identified as untapped market and estimated to have spending power of at least 20.5 billion pounds (Salzman 2007). In terms of age profile, this group has the youngest age profile of all the religious groups in the UK (UK National Statistics 2001). Furthermore, this population is concentrating in large cities such as London, Birmingham and Bradford which makes it relatively easy to reach large numbers of these consumers.

Due to their high population growth, it has becoming increasingly important to understand the consumption pattern of this group. As been suggested by Bocock (1993, pp. 80), ethnicity can affect a range of consumer behaviour such as style of dress, tastes in music and leisure time pursuits, or in food and drink consumption. However, studies related to ethnic minorities have received very little attention in British marketing literature (Nwankwo and Lindridge 1998, Burton 2000) as compared in the United States. Muslims migrating to UK go through acculturation-the process of learning and adopting cultural traits different from the ones with which the person was originally reared (Ownbey and Horridge 1997). Previous research suggested that an immigrant can actively adopt the dominant culture’s values, attitudes and behaviour while others may retain their minority culture’s values, attitudes and behaviour (e.g. Khairullah et al. 1996, Penaloza 1994) The changes experienced among the immigrants might be reflected in their buying behaviour. Therefore, British Muslim consumers should be studied in the context of ethnicity and acculturation; however, up to the present, British Muslim consumers have received considerably less attention from academic professionals and marketing practitioners. The next section presents the conceptual framework guiding this research and some of the research propositions to be tested in this research.

Figure 1, given on next page, presents the conceptual model developed for this research. The model posits that two sets of factors affect consumer trust towards fashion brands clothing via brand liking. These two factors are cultural (acculturation, generation and ethnicity) and individual factor (self image congruence and religiosity). We also propose that brand liking will lead to trust.
Acculturation, Ethnicity, Generation and Brand Liking

Previous studies showed that acculturation, ethnicity and generation are closely linked with various consumer behaviour. For instance, Khairullah et al. (1996) reported that acculturation level influenced the perceptions of Asian Indian on Indian versus American print advertisements. Their study shows that as acculturation increased, subjects preferred American advertisements more and Indian advertisements less. The same findings have been demonstrated in another study by Khairullah (1995) whereby low and moderate acculturated respondents had a greater preference for Indian advertisements while high acculturated Asian Indians had a greater preference for American advertisements. Swaidan et al. (1996) reported that acculturation levels influence consumers’ views of ethics whereby those who are less acculturated are less tolerant of unethical consumer activities than those who are highly acculturated. Podoshen (2006) study shows that the higher the degree of acculturation, the less likely Jewish consumers will be brand loyal. The role of acculturation on media exposure, coupon use and brand loyalty among the Hispanic population has also been investigated by Petroshius et al. (1995). The results indicate that as acculturation increased, the Hispanics are more frequently exposed to English language media, use coupons with greater frequency, and display less loyalty to specific brands.

The relevance of ethnicity and consumer behaviour has also been studied in Kim and Arthur (2005) study. The study investigates how the strength of ethnic identification influences attitudes towards and ownership of ethnic apparel, importance of product and store display attributes, and purchase intention among Asian American consumers in Hawaii. The results showed that those participants who identified themselves strongly with their ethnic group put more emphasis on ethnic features of clothing and window displays than those with a weak ethnic identification.
Evidence also shows that the behaviour of immigrants varies from generation to generation. For instance, study by Jamal (1998) demonstrated that the first generation of British Pakistanis perceive their own food to be traditional, tasty but oily and problematic while the English foods are perceived as foreign, bland but healthy. On the other hand, the young generation of British Pakistanis is increasingly consuming mainstream English foods while also consuming traditional Pakistani food. Sekhon and Szmigin (2005) study found that second and subsequent generations are likely to develop new loyalties and become more assimilated than first generation immigrants. Therefore, based on the existing findings, it is suggested that acculturation, ethnicity and generation affect the consumers’ liking towards fashion brands clothing. Hence, this leads to the following set of propositions:

P1: An individual’s acculturation level will be associated with his or her liking towards fashion brands clothing.

P2: An individual’s ethnicity level will be associated with his or her liking towards fashion brands clothing.

P3: An individual’s generation will be associated with his or her liking towards fashion brands clothing.

**Self Image Congruence, Religiosity and Brand Liking**

Consumer self concept researchers have long theorized that a product-user image interacts with the consumer’s self concept generating a subjective experience referred to as “self image congruence” (Sirgy et al. 1997). The self image congruence theory suggests that consumers are often more likely to prefer products or brands that have images similar to their own self concept (e.g. Jamal 2004, Kleijnen et al. 2005, Ericksen 1996, Heath and Scott 1998, Ross 1971, Jamal and Goode 2001, Sirgy et al. 1997, Dolich 1969). The studies also suggest a purchase is not likely to take place when there is incongruence (Onkvisit and Shaw 1987). Furthermore, where incongruence exists and a purchase does take place, consumers are unlikely to repeat such a purchase (Onkvisit and Shaw 1987). Therefore, if a consumer feels that a particular product or brand has similar image to their own self concept, the consumer is likely to develop ‘liking’ towards the brand. Hence, this leads to the next proposition:

P4: British Muslims consumers with different levels of self image congruence will exhibit different level of liking towards fashion brands clothing.

Muslims are expected to dress modestly according to the clothing requirement been laid down in the Quran and Hadith. McDaniel and Burnett (1990) cited in Siguaw et al. (1997) defined religiousness as a ‘belief in God accompanied by a commitment to follow principles believed to be set forth by God’. Based on the definition, we can say that a Muslim is considered religious if he or she believes in God and follow the principles laid down in Quran and Hadith. It has been argued that religiousness may affect consumers’ shopping options or alternatives (Clark and Dawson 1996). For instance, if a religious
consumer deems a particular practice, such as wearing the ‘sexy’ westernised clothing as contrary tenets held, the consumer may eliminate the practice an alternative. Hence, consumers’ religiosity will determine the consumers’ liking towards fashion brands clothing. Stated formally:

P5: British Muslims consumers’ religiosity will determine the consumers’ liking towards fashion brands clothing.

Brand Liking and Trust

Bennet (1996) cited in Lau and Lee (1999) suggests that to initiate a relationship, one party must be liked by the other. In the context of consumer-brand relationship, a consumer must like the brand first before trust is developed. Previous researches have found several antecedents of trust such as satisfaction, brand familiarity and risk aversion (e.g. Delgado-Ballester and Munuera 2005, Ha and Perks 2005, Matzler et al. 2008). However, it has also been suggested that additional studies that identify other antecedent variables that affect brand trust such as brand reputation and other more personal and emotional factors such as liking could be conducted (Delgado-Ballester et al. 2003). In view of this, if a consumer likes a brand, he or she is more likely to trust that brand. Therefore, this leads to the next proposition:

P6: A consumer’s liking for a brand will directly relate to the consumer’s trust in that brand.

Discussion and Conclusion

This paper is based on a doctoral research (still in progress) and therefore, the research propositions reported here are based on the current findings on literature review. The research aims to investigate the effect of cultural (acculturation, ethnicity and generation) and individual factors (self image congruence and religiosity) on British Muslims consumers’ trust towards fashion brands clothing in the UK. This research attempts to use self administered questionnaire in order to collect the data from the British Muslims in the UK.

As been suggested by Nwankwo and Lindridge (1998), ethnic marketing cannot be successful unless it is strategically driven. Therefore, this study aims to make practical contributions by discussing implications for marketing mix developed by the retailers and manufacturers of fashion brand clothing. In this sense, retailers and manufacturers of fashion brand clothing may develop an effective marketing programme which consists of ‘product’, ‘price’, ‘promotion’ and ‘place’ that blends to target the British Muslims in UK.
References


Nurturing Opportunity Entrepreneurs in Africa: Some Lessons from Ethiopia

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Abstract: This paper examines the distinguishing features of opportunity and necessity entrepreneurs and delineates the factors that characterize each group. Then, based on an exploratory study of a small sample of opportunity entrepreneurs in Ethiopia, it identifies the challenges encountered by them and proposes a set of targeted policies that can help such entrepreneurs overcome the identified barriers, stimulate their entrepreneurial initiatives and accelerate their growth. It concludes by suggesting that in order to be effective, policy interventions should be separately tailored to the unique needs of opportunity and necessity entrepreneurs rather than using a generic “one-size-fits-all” approach. This finding has potentially important implications for policy makers in developing nations.

Keywords: Entrepreneurship, emerging markets, Africa, Ethiopia, opportunity entrepreneurs

1. Introduction

There is ample evidence that entrepreneurship drives economic growth and job creation in any nation (Berger, 1991; Reynolds and White, 1997). Studies have shown strong association between entrepreneurship, poverty reduction and economic growth in developing countries (Thomas et al, 1998; Bridges.org, 2002). In industrialized nations entrepreneurial ventures can contribute to poverty alleviation in inner cities and other economically troubled regions (Schlogl, 2004) while in many emerging markets small and medium-sized enterprises (SMMEs) provide a major share of private sector employment. Convinced of entrepreneurship’s role as a vehicle for economic growth in emerging economies, the United Nations established the Commission on the Private Sector and Development (CPSD) in 2003 for the purpose of energizing the private sector to help grow the economies of developing nations.
While research on entrepreneurship has increased during the last decade, most of the studies have focused on economically developed nations. Entrepreneurial activities vary in different nations (Acs et al., 2004) and there is evidence that the findings from studies conducted in industrialized countries may not be applicable in developing ones (Thomas, 1998). Obviously, there are significant regional and local differences even among developing nations. Therefore, even if many of the barriers that inhibit entrepreneurial success are similar across a continent or a region, each nation needs to design and implement its own strategy to promote entrepreneurship in view of the special conditions that exist there.

While this paper places a particular emphasis on Ethiopian entrepreneurship, it is set in the broader, regional context of African entrepreneurship in general. The following section, based on a review of the relevant literature, identifies the distinguishing features of opportunity and necessity entrepreneurs and delineates some of the challenges encountered by each group. Section 3 presents a discussion of the key determinants of entrepreneurial success in Africa as gleaned from the literature. This is followed by a brief historical overview of entrepreneurship in Ethiopia in Section 4. The methodology used to conduct an exploratory study of a selected group of Ethiopian opportunity entrepreneurs is detailed in Section 5, and the results are presented and discussed in Section 6. Section 7 presents proposed interventions that can help both opportunity and necessity entrepreneurs in Ethiopia overcome the identified barriers and stimulate entrepreneurial initiatives and success. While these proposals are drawn from the results of this study and are directly relevant for Ethiopia, they are framed around the larger African context while recognizing the significant national and regional differences prevailing in the continent. The last section provides conclusions and suggestions for future research.

2. Necessity and Opportunity Entrepreneurs

Kiggundu (2001) classifies African entrepreneurs into two broad categories: (a) micro enterprises or solo entrepreneurs, and (b) small and medium size enterprises. For purposes of this study, however, the entrepreneurship classification used by the Global Entrepreneurship Monitor (GEM) is used which, based on a comprehensive study of entrepreneurship in 29 countries, grouped entrepreneurs into the following two categories: opportunity entrepreneurs and necessity entrepreneurs (Reynolds et al., 2001).

Opportunity entrepreneurs are those who pursue “a business opportunity for personal interest” (Reynolds et al, 2001) and are often motivated to start and grow their business by “pull” factors which include the desire to achieve financial success and independence, family tradition, and the drive to create new products and services (Sriram and Mersha, 2006). On the other hand, necessity entrepreneurs go into their own business for economic survival, forced by “push” factors such as the lack of job opportunities due to insufficient education, low skills and job discrimination (Basu and Altinay, 2002). These are typically one-person operations and comprise the dominant group of entrepreneurs in Africa and other emerging markets (Reynolds et al, 2001). They are normally prevalent in sectors such as retail and personal services and many solo and micro enterprises are owned and managed by women (McDade and
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Spring, 2005). These entrepreneurs are often less educated, typically have very low start-up capital and their organizational and managerial skills are very limited. Record keeping is poor and the level of their business activity is very limited and failure rates are high. Further, not all individuals in this group may take up such entrepreneurial activities as a full time operation; just like opportunity entrepreneurs, some may engage in such endeavours on a part-time basis to supplement the family income. A significant difference though is that necessity entrepreneurs are compelled to engage in business activities to make ends meet while opportunity entrepreneurs take up business activities willingly to pursue a personal interest (Reynolds et al, 2001), create jobs and to accumulate wealth. Opportunity entrepreneurs have the potential to grow their business from solo or micro-enterprise to small or medium size enterprise (SMME) and have better capital and managerial resources. Nevertheless, their failure rate during the first three years is very high (Kiggundu, 2002). Table 1 summarizes the important differences between necessity and opportunity entrepreneurs.

3. Determinants of Entrepreneurial Success

While launching a new business venture is often a challenge in any environment, sustaining and growing the business is more so. Even in industrialized nations where systems are in place to facilitate the launching of new businesses, failure rates remain very high. For example, about 50% of all new business start-ups fail by their third anniversary in Canada (Ward, 2005). African entrepreneurs encounter even greater challenges in launching, sustaining and growing their business ventures including incapacity to transition from informal business practice to formal business operations, inability to fend off external threats, and lack of financial resources (Kiggundu, 2002). Several factors impact the success of entrepreneurs in Africa. These include personality/behavioural factors, the business climate, innovativeness and size, entrepreneurial competency and culture.

3.1 Personal/behavioural factors

Personality traits are important drivers of entrepreneurial initiative and success, although there is an ongoing debate in the literature as to whether entrepreneurs are born with the necessary qualities or whether these can be taught (De Faoite et al., 2003). Thomas and Mueller (2001) identify traits such as internal locus of control, risk taking propensity and energy level as being associated with entrepreneurship and argued that entrepreneurial orientation was higher in some cultures than others and that it decreased as the cultural distance from the US increased. Few studies have examined personality traits in the African context but in a study of South African entrepreneurs, Mitchell (2004) identified the dominant reasons for starting a business. In order of importance, these are: “survival, financial independence and security, to escape a negative situation, and to enable personal growth” (p. 179). Many of these factors may be relevant for entrepreneurs in many other African countries as well. In a comparative study of South African, US and Dutch students, it was found that self-reported entrepreneurial traits -- competing against self-imposed standards, dealing with failure, drive and energy levels and goal setting and perseverance -- were the most developed among the South African students (van Eeden, Louw and Venter, 2005). More recently, based on data from South African firms, Kropp,
Lindsay and Shoham (2008) reported that proactiveness and risk-taking were positively related to the decision to start an entrepreneurial venture.

**Table 1**

**Differences between necessity entrepreneurs and opportunity entrepreneurs**

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>Necessity Entrepreneurs</th>
<th>Opportunity entrepreneurs</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Primary driver</td>
<td>Entrepreneurship is pursued by “push factors” as a last ditch effort for economic survival</td>
<td>Entrepreneurial endeavour is initiated by “pull” factors to attain greater personal satisfaction and wealth accumulation and to create employment opportunities for others</td>
</tr>
<tr>
<td>2. Skill level</td>
<td>Generally unskilled</td>
<td>Skilled</td>
</tr>
<tr>
<td>3. Education level</td>
<td>Generally very low education or no education at all</td>
<td>At least secondary school education; many have attended/ completed college</td>
</tr>
<tr>
<td>4. Ease of navigating the bureaucracy</td>
<td>Difficult since they are not familiar with the bureaucratic red tape and do not know how to navigate the system.</td>
<td>They are generally able to navigate the bureaucratic red tape with ease since they are familiar with the expected process</td>
</tr>
<tr>
<td>5. Geographical location</td>
<td>Both in rural and urban areas</td>
<td>Primarily in urban centres</td>
</tr>
<tr>
<td>6. Employment size</td>
<td>Often solo operators</td>
<td>May hire several employees, often upwards of 10</td>
</tr>
<tr>
<td>7. Financial resource availability</td>
<td>Extremely limited; best source is micro finance (where such facilities are available) or loans from family members.</td>
<td>Often have some financial resources which they may need to augment to be able to start the venture; considered “too wealthy” to qualify for micro finance; although often difficult, they may be able to leverage their limited resources with bank loans.</td>
</tr>
<tr>
<td>8. Community/family support</td>
<td>Available</td>
<td>Available</td>
</tr>
<tr>
<td>9. Growth potential</td>
<td>Limited; start as, and often remain solo entrepreneurs.</td>
<td>High; may start as solo entrepreneurs but have the potential to transform their venture to small or medium-size business</td>
</tr>
<tr>
<td>10. Nature of business</td>
<td>Small retail; handyman or other unskilled services</td>
<td>Import/export; light manufacturing; skilled services; retail services</td>
</tr>
</tbody>
</table>
3.2 Business climate
The environment may create a business climate that fosters entrepreneurship by helping provide the necessary resources and other forms of assistance or one that strangles entrepreneurial efforts by placing intractable barriers. For example, in regard to the floriculture industry in Ethiopia, Belwal and Chala (2008) found that government support and the formation of the Horticulture Producers and Exporters Association were among the major catalysts for its relative success while, on the other hand, infrastructural bottlenecks and shortage of agricultural inputs were among its primary deterrents. Despite some successes in specific sectors however, the prevailing business climate in most African countries is anything but conducive to entrepreneurial pursuits. Adverse government policies and intrusive and corrupt bureaucracies are identified as some of the more significant problems faced by entrepreneurs in Africa (Coyne and Leeson, 2004). Current and would-be African entrepreneurs encounter more severe barriers than their counterparts in other regions, as can be seen from Table 2, where Sub-Saharan Africa is the least efficient of all the regions -- it takes over 230 days and requires over 1,000% of average per capita income in the region to obtain the required licenses and permits to build a warehouse. For Ethiopia, the required time is about 133 days and the associated cost is estimated at 1235% of the nation’s per capita income. In Tanzania it is worse -- 313 days and 3797% of per capita income (http://www.doingbusiness.org).

3.3 Innovativeness and size
African entrepreneurs tend to provide a limited range of services and are not innovative in creating new products or new markets (Kiggundu, 2002). The fact that most entrepreneurial firms are small and operate independently constrains their access to important business networks, limits their innovative capacity in creating new goods and services, and weakens their competitiveness (Ramachandran and Shah, 1999). Many African entrepreneurs use an organization form dubbed the “octopus” whereby the firm invests in different types of businesses with the purpose of distributing risk and uncertainty and to involve different family members (Jorgensen, Hafsi, & Kiggundu, 1986). While this may help minimize exposure to risk and uncertainty, the use of the octopus form of organization scatters the available resources, reduces the firm’s leverage in utilizing its core capabilities for competitive advantage, and inhibits its growth. With access to critical resources highly limited and their potential for innovation and efficiency curtailed, most entrepreneurial firms in Africa lack competitive prowess and eventually go out of business (Kiggundu, 2002). In Kropp, Lindsay and Shoham’s (2008) South African sample, innovativeness was not a factor in the entrepreneurial start-up decision.

3.4 Entrepreneurial competency
This includes the behavioural, managerial and technical capacity to successfully establish and manage a new business (Kiggundu, 2002). Most African entrepreneurs have limited entrepreneurial competency partly due to lack of specialized education and training. For example, an extensive survey by the Ethiopian Development Research Institute of 974 micro and small enterprises revealed that the operators of these enterprises had very limited vocational and technical training before starting a business (Amha and Ageba, 2006). Studies have demonstrated that those entrepreneurs with low education and who also lacked technical skills were less
Table 2

Time and cost in starting a business in different regions

<table>
<thead>
<tr>
<th>Region</th>
<th>Time (in days)</th>
<th>Cost as % of income per capita</th>
</tr>
</thead>
<tbody>
<tr>
<td>East Asia &amp; Pacific</td>
<td>147.4</td>
<td>207.2</td>
</tr>
<tr>
<td>Europe &amp; Central Asia</td>
<td>242.5</td>
<td>564.9</td>
</tr>
<tr>
<td>Latin America &amp; Caribbean</td>
<td>198.7</td>
<td>246.2</td>
</tr>
<tr>
<td>Middle East &amp; North Africa</td>
<td>206.9</td>
<td>499.9</td>
</tr>
<tr>
<td>OECD</td>
<td>149.5</td>
<td>72.0</td>
</tr>
<tr>
<td>South Asia</td>
<td>226.6</td>
<td>375.7</td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
<td>230.2</td>
<td>1,024.5</td>
</tr>
</tbody>
</table>

Source: [http://www.doingbusiness.org/](http://www.doingbusiness.org/)

successful, and that higher education, work experience and exposure to foreign environments positively impacted success (Trulsson, 1997). Even completion of primary education was found to have a positive impact on enterprise management and growth. For example, a study based on World Bank data showed that Asian and European entrepreneurs in Africa who were better educated had competitive advantage over less educated indigenous Africans (Ramachandran and Shah, 1999). While Kropp, Lindsey and Shoham (2008) found that the start-up decision was negatively related to education, this is not necessarily inconsistent with the findings of Ramachandran and Shah (1999) since the factors that impact the start-up of a new venture are often different from those that determine its survival and success.

### 3.5 Culture

There is evidence that the relative success of new business start-ups is influenced by a nation’s cultural traits (Baughn and Neupert, 2003). Entrepreneurship is facilitated by highly individualistic and masculine cultures with low uncertainty avoidance and low power distance (Hayton, George, & Zahra, 2002). Typically, entrepreneurial success is positively correlated with individualism and negatively correlated with uncertainty avoidance. Cultures that grant high social status to entrepreneurs also promote entrepreneurship.

African societies are characterized by high power distance (i.e., hierarchical and authoritarian social structure) and collectivism both of which tend to weaken entrepreneurship (Takyi-Asiedu, 1993). Further, many social norms practiced in Africa are not compatible with entrepreneurial success, and the extensive social network and community involvement enjoyed by African entrepreneurs may be both a blessing and a curse. On the one hand, broad community involvement and social networks may help generate new business to the entrepreneurs as well as sustain them by bringing repeat business. On the other, some studies suggest that such community involvements take too much of the entrepreneurs’ time which causes the business to suffer (Sam, 1998; Takyi-Asiedu, 1993). For example, Ethiopian entrepreneurs close their shops to attend funeral services, religious events and wedding ceremonies. Many necessity entrepreneurs from the Guraghe ethnic group in Ethiopia liquidate their inventory or use up their savings to
go to their villages in September to celebrate a religious holiday called Meskel only to start from scratch upon their return to Addis Ababa or other cities a couple months later. Thus, cultural practices tend to adversely impact entrepreneurial success in Ethiopia, as in many parts of Africa.

4. Entrepreneurship in Ethiopia

As discussed earlier, African entrepreneurs face some unique challenges that hamper their ability to survive and grow, and Ethiopian start-ups are often no different. The political, economic and bureaucratic landscape in which most African entrepreneurs operate is generally similar even though there are unique challenges and opportunities prevailing in each nation which must be taken into account in formulating effective policies to promote entrepreneurship. Takyi-Asiedu (1993) noted that compared with public service jobs, engaging in a business venture has not historically been considered a high status profession in Africa although entrepreneurs may become well respected citizens when they get rich. This has also been true in Ethiopia.

During the past five decades, the ebb and flow of entrepreneurial activity in Ethiopia has varied with the political climate. The waning years of Emperor Haile Selassie’s regime in the 1970s may be considered a watershed in the evolution of entrepreneurship in Ethiopia as several college graduates started working for themselves. While the overwhelming majority still sought employment with public or private organizations during this time, a good number of young educated Ethiopians started considering entrepreneurship as a viable career option. Several graduates of the College of Agriculture started export-oriented agribusiness companies and many landowners began large-scale commercial farming. The government encouraged entrepreneurship although no major resource commitments were made to support entrepreneurial efforts. Significantly, the Centre for Entrepreneurship and Management (CEM) was created at that time with donor assistance to increase managerial and technical capacity of current and nascent entrepreneurs.

Unfortunately, this trend was quickly reversed when a military regime took power and declared socialism as state economic policy in the mid-1970s. During this time, most private enterprises in Ethiopia, including small and medium size firms, were nationalized and private enterprise was discouraged. While necessity entrepreneurs and those who had no other option continued to struggle, the entrepreneurial energy seen in the last few years of Emperor Haile Selassie’s regime waned in part due to fear of potential backlash by leftist ideologues and also due to fear of possible expropriation of their investments. Those entrepreneurs who decided to stay the course or start new business ventures did so under very difficult conditions and some were forced to disguise the expansion of their businesses by registering new ventures in the names of their family members. During the military regime, employers were clearly intimidated by the new power bestowed upon labour unions, and many business owners were victimized by frivolous charges brought against them by their employees with the government’s tacit encouragement. In general, the adverse business climate during the socialist regime effectively dissuaded many from pursuing entrepreneurial ventures.

Today, entrepreneurial fervour has grown, particularly in urban centres. There are indications that for those who have the financial means, starting a business has become a
career of choice. Several factors have contributed to this astounding change in attitude towards entrepreneurship in a relatively short time:

- Salaries failed to keep pace with inflation and it became harder to live on fixed salary by working for a public agency or other government-owned enterprises.
- Due to sluggish economic growth, good jobs have become harder to get.
- Private sector jobs are limited, and many educated Ethiopians tend to perceive that the few jobs that are available in public or state-owned enterprises (particularly good paying positions) are filled not based on merit but rather on political and ethnic affiliations.
- A high degree of uncertainty is associated with jobs in government agencies and state-owned enterprises (SOEs).
- Lowering the retirement age from 65 to 55 years under the military regime (which was later raised to 60 years) forced many experienced and highly qualified managers and administrators to retire and start their own business.

When the military regime was on the verge of its demise in the late 1980s, it began relaxing some of the constraints it had created against private business initiatives and started to encourage investment in selected sectors such as tourism. The Ethiopian People’s Revolutionary Democratic Front (EPRDF) that succeeded the military regime in 1991 reversed the socialist policy that was enforced by the previous regime and initiated a more market-oriented economic policy. Although many large enterprises still remain state-owned, private enterprise in Ethiopia began to sprout again since the early 1990s.

5. The Exploratory Study

An exploratory study was conducted for the purpose of gaining a better insight about the opportunities and challenges faced by entrepreneurs in Ethiopia, with a particular focus on opportunity entrepreneurs. A questionnaire addressing new venture start-up and management issues was developed and pre-tested. After revisions, this questionnaire, prepared in English, was administered in Addis Ababa, Ethiopia, to a group of 20 entrepreneurs selected by the researchers as meeting the criteria of opportunity entrepreneurs in the Ethiopian context. As previously indicated, opportunity entrepreneurs have a greater potential to contribute to a nation’s economic development and job creation and given the study’s aim of examining how entrepreneurship can better contribute to a nation’s economic growth, a convenience sample of opportunity entrepreneurs was used for this exploratory study. Seven research questions were identified as shown below. To enable a better understanding of the relative importance of the issues identified in the study, respondents were asked to rate their responses on a 5-point Likert scale. In order for the participants to clearly understand the questionnaire written in English, one of the researchers was available to provide translations if needed and to clarify any questions in the survey instrument.

5.1 Research Questions

This exploratory study of opportunity entrepreneurs sought to answer the following research questions:

1. What are the primary motivating factors to start their own businesses?
2. What do these opportunity entrepreneurs perceive as important measures of an ideal job?
3. What are the primary challenges and constraints they encountered both during the start-up phase and after their businesses had been launched?
4. What type of support, if any, did they receive when they started their new ventures and from whom?
5. What skill sets are perceived to be critical by this group of Ethiopian entrepreneurs?
6. How did they measure their success?
7. What lessons had they learned from their experiences?

5.2 Participant Profile
The individuals sampled were relatively well-educated with all the participants having completed secondary school, 30% had some college education and 35% had earned a college degree. Most went into business in an area related to their work experience and nearly two-thirds started a business related to their education. The enterprises they created included garment production and distribution, handicrafts, information technology, and import/export operations. As a group, the average length of time they were in business exceeded 10 years, having passed the critical threshold of the formative years during which time many new entrepreneurial ventures fail. On average, they employed 18 workers and 40% of the respondents reported annual employment growth of at least 5%.

6. Results and Discussion

This section presents the responses to the research questions. To better understand the various issues included in the research questions, respondents were asked not only to identify certain dimensions but also to rate each of them using a 5-point Likert scale. Tables 3-8 present the responses to each research question.

6.1 Factors that motivated new business start-up
This exploratory study suggests that multiple factors contributed to the successful launch of new ventures by the participants (Table 3). In descending order, these include the desire for independence, the role model effect (i.e., having family members already in business), the desire to improve earnings, better utilize their skills and talents, and the need to have greater control over their lives. Unlike typical African necessity entrepreneurs, the opportunity entrepreneurs who participated in this study were not pushed to start their business due to lack of employment opportunity or out of fear that they might lose their jobs; rather, it was the search for better opportunities -- including increased earnings, relative independence and the prospect of helping others -- that pulled them to start their own business ventures. In this respect, their motivation for entrepreneurial pursuit is more similar to entrepreneurs in industrialized nations. By World Bank categorization (Bridges.org, 2002), their firms are small or medium size enterprises and have the potential for further growth.
Table 3
Motivating factors that contributed to the successful start of business venture

<table>
<thead>
<tr>
<th>Motivation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Being independent</td>
</tr>
<tr>
<td>Desire to innovate</td>
</tr>
<tr>
<td>Bettering my finances</td>
</tr>
<tr>
<td>Best use of my talents</td>
</tr>
<tr>
<td>Having greater control over my life</td>
</tr>
<tr>
<td>Saw a business opportunity</td>
</tr>
<tr>
<td>Improving my social status</td>
</tr>
<tr>
<td>Enjoy taking risks</td>
</tr>
<tr>
<td>Previous business experience</td>
</tr>
<tr>
<td>Continuing my family tradition</td>
</tr>
<tr>
<td>Family members already in business</td>
</tr>
<tr>
<td>Couldn’t find a job</td>
</tr>
<tr>
<td>Discrimination in my current (old) situation</td>
</tr>
<tr>
<td>My job was (is) underpaid</td>
</tr>
<tr>
<td>Lost my job</td>
</tr>
<tr>
<td>Other</td>
</tr>
</tbody>
</table>

6.2 Perception of an ideal job
Table 4 presents measures of an ideal job as identified by the participants as well as the perceived importance of each measure in descending order (on a 5-point Likert scale where 5 = Strongly Agree, and 1 = Strongly Disagree). The participants perceived the ideal job as one that offered an opportunity for higher earnings while also providing sufficient time for personal and family life. It is interesting to note that, in contrast to the experiences of entrepreneurs in industrialized nations who tend to work hard and long particularly during the formative years of their business, these Ethiopian entrepreneurs anticipated that creating their own business ventures would afford them more time to spend with families and friends. This may be due to the availability of affordable labour to perform routine aspects of the work. The entrepreneurs who participated in this study also believed that new venture creation provided an important avenue for helping others by generating viable employment opportunities. Interestingly, “working in a well defined job situation where the requirements are clear” is rated high by the respondents, inconsistent with the typical view that entrepreneurs are generally comfortable working in less structured environments.
Table 4
Measures of an ideal job

<table>
<thead>
<tr>
<th>Characteristics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Have an opportunity to help other people</td>
</tr>
<tr>
<td>Have sufficient time left for my personal or family life</td>
</tr>
<tr>
<td>Work in a well defined job situation where requirements are clear</td>
</tr>
<tr>
<td>Have an opportunity for high earnings</td>
</tr>
<tr>
<td>Be able to express disagreements with your superior</td>
</tr>
<tr>
<td>Be consulted by my direct superior in his/her decision</td>
</tr>
<tr>
<td>Have an element of variety and adventure</td>
</tr>
</tbody>
</table>

6.3 Problems/challenges during the start-up phase

In contrast to necessity entrepreneurs who often find navigating the bureaucracy a severe challenge, the respondents, all of whom were opportunity entrepreneurs, indicated that they were satisfied with their decision to start their own business and that they were able to get the information they needed with relative ease since they were familiar with the workings of the bureaucracy. The respondents identified lack of adequate financing to be the most significant problem. Other challenges mentioned frequently include insufficient space and lack of training for their employees. Table 5 presents the problems/challenges encountered by entrepreneurs in starting a new business in Ethiopia as identified by the respondents.

Table 5
Problems/challenges experienced while starting a new business

<table>
<thead>
<tr>
<th>Type of Challenge</th>
<th>Number of times mentioned</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lack of finances</td>
<td>13</td>
</tr>
<tr>
<td>Space and location limitations</td>
<td>8</td>
</tr>
<tr>
<td>Lack of training/planning</td>
<td>5</td>
</tr>
<tr>
<td>Lack of qualified and honest employees</td>
<td>4</td>
</tr>
<tr>
<td>Difficulty in entering a new market</td>
<td>3</td>
</tr>
<tr>
<td>No government protection</td>
<td>2</td>
</tr>
<tr>
<td>Others*</td>
<td>12</td>
</tr>
</tbody>
</table>

*This includes a list of 12 problems/challenges mentioned just once. These problems include market saturation due to competition, identifying suppliers of machinery and raw materials, rent cost, lack of information, lack of customers, lack of mentors, etc.

6.4 Nature of help and support received

The respondents indicated that since there were no family members or financial institutions that were able and willing to provide the financial support they needed, they relied on personal sources of funds. About 90% of the respondents reported that there were no government programs or community-based financial resources to provide them with the required funds. The strongest support seems to have come in the form of


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encouragement and moral support from their communities and many had family members who were willing to work for them. Table 6 lists the sources of support as reported by respondents, in descending order.

Table 6
Type of support received during the start-up phase of the business

<table>
<thead>
<tr>
<th>Support</th>
</tr>
</thead>
<tbody>
<tr>
<td>Encouragement and moral support from my community</td>
</tr>
<tr>
<td>Personal financial resources</td>
</tr>
<tr>
<td>Family members willing to work for me</td>
</tr>
<tr>
<td>Debt financing</td>
</tr>
<tr>
<td>Equity financing</td>
</tr>
<tr>
<td>Family members’ resources</td>
</tr>
<tr>
<td>Government programs</td>
</tr>
<tr>
<td>Community-based financial networks</td>
</tr>
</tbody>
</table>

6.5 Skills required for success
The ability to identify the right business, navigate the legal and bureaucratic system, recruit and hire needed personnel, and manage day-to-day operational and marketing functions are critical success factors for any business (Herron, 1994). These participants reported that they believed they had adequate level of skill in such areas as technical knowledge about the business, organizational skills, industry knowledge, information gathering, leadership and networking. They also perceived their skill level to be sufficient with regard to monitoring their financial performance, managing their operations, and marketing, but they indicated that they could do somewhat better when it came to business planning. Table 7 presents the responses of the participants regarding their perceived skill level in several areas. (For rank ordering purposes, the various skill sets were rated from 1 to 5 where 1 indicated “no acquired learning at all”, and 5 indicated a “huge amount of learning”. These results are presented in reverse order to highlight skills that the entrepreneurs are lacking. So, for example, among the skill sets they were asked about, they perceived themselves to have the least skill in business planning and the most in technical knowledge related to their business).

6.6 Measures of success
Acknowledging that different groups or individuals may use different benchmarks to measure success, the respondents were asked how they measured success in their business ventures. Not surprisingly, the most frequently mentioned measure of success was profitability, followed by production growth or sales growth, customer satisfaction, providing employment opportunity to others, and growth in market share. Half the participants reported that their profits grew just 1-5% per year on average during the previous three years, and 32% indicated that that their profits grew between 5-10% per year. Nearly 13% of the respondents reported annual profit growth of more than 10% per year, and 55% reported average annual sales growth of 5% or more. They also indicated that availability of financing, dedicated employees, training, and continuous product/service improvement and innovation were important factors that would
contribute to greater success. Given their specific measures of success, the respondents indicated that they considered themselves moderately successful with a mean score of 3.73 on a 5-point scale, where 1 = very unsuccessful and 5 = very successful.

**Table 7**

<table>
<thead>
<tr>
<th>Perceived Skill Levels</th>
</tr>
</thead>
<tbody>
<tr>
<td>Skill Level*</td>
</tr>
<tr>
<td>Business planning</td>
</tr>
<tr>
<td>Brainstorming</td>
</tr>
<tr>
<td>Business analysis</td>
</tr>
<tr>
<td>Marketing/Selling</td>
</tr>
<tr>
<td>Creativity</td>
</tr>
<tr>
<td>Networking</td>
</tr>
<tr>
<td>Tracking Financial Performance</td>
</tr>
<tr>
<td>Day-to-day operations</td>
</tr>
<tr>
<td>Leadership</td>
</tr>
<tr>
<td>Information-gathering in general</td>
</tr>
<tr>
<td>Industry knowledge in the area in question</td>
</tr>
<tr>
<td>Organizational skills</td>
</tr>
<tr>
<td>Technical knowledge related to your business</td>
</tr>
</tbody>
</table>

* Skill levels are presented from least to from highest

### 6.7 Important lessons learnt from past mistakes

The entrepreneurs were also asked to recall important mistakes they made both during the start-up and sustenance phases of their business from which they learnt. As shown in Table 8 below, lack of planning, poor customer relations management, not conducting market research, and not using professionals top the list of mistakes from which the entrepreneurs learnt valuable lessons. Other mistakes from which lessons were learned include neglecting quality control, trusting others, and selling on credit.

**Table 8**

<table>
<thead>
<tr>
<th>Lessons learnt from past mistakes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lack of planning</td>
</tr>
<tr>
<td>Poor customer relations management</td>
</tr>
<tr>
<td>No prior market research</td>
</tr>
<tr>
<td>Not using professionals to help tackle some of their activities</td>
</tr>
<tr>
<td>Lack of quality control</td>
</tr>
<tr>
<td>Trusting others</td>
</tr>
<tr>
<td>Selling on credit</td>
</tr>
</tbody>
</table>

### 7. Policy interventions to nurture opportunity entrepreneurs

As stated earlier, successful entrepreneurship can promote job creation and contribute to economic growth. Efforts undertaken to promote entrepreneurship, however, must take
into account the specific socio-economic, cultural and political environment prevailing in each county since a “one-size-fits-all” strategy cannot apply across nations. Clearly, the types of entrepreneurs and their needs will vary significantly from one nation to another. For example, in contrast to South Africa where most new business ventures are primarily opportunity-driven (Naude et al., 2008), new business start-ups in Ethiopia are mostly driven by necessity. Further, as this study demonstrated, there are distinct differences in the needs and challenges of necessity and opportunity entrepreneurs even within the same country. It is therefore important that in developing nations like Ethiopia different support mechanisms be utilized (a) to strengthen and grow opportunity entrepreneurs, and (b) to help necessity entrepreneurs transition to small and medium-size enterprises. It is particularly important that appropriate measures are taken to strengthen opportunity entrepreneurs in view of their higher potential to contribute to the nation’s economic growth and development. Based on the findings of this study the following interventions are proposed to energize and nurture opportunity entrepreneurs in Ethiopia:

7.1 Increase availability of financial resources. Acquiring start-up and working capital was the biggest challenge with which the entrepreneurs who participated in this study had to wrestle with thus suggesting that Ethiopian entrepreneurs face similar challenges as those in other African countries. Micro finance initiatives have played a very important role in providing small loans to millions of micro entrepreneurs in Africa and elsewhere in developing countries. It is estimated that at least 80 million clients worldwide have benefited from micro finance loans and that micro lending has helped thousands of people to become budding entrepreneurs (Dolan, 2005). Some studies have shown that for entrepreneurs who lack basic organizational know-how and competencies, providing additional financial resources will not improve their profitability and performance and that increased access to capital and credit facilities would contribute immensely to the success of the relatively better organized and better managed business enterprises (Baughn and Neupert, 2003). In this study, lack of adequate financial resources was the most frequently mentioned constraint encountered by the opportunity entrepreneurs. These entrepreneurs were considered “too wealthy” to qualify for micro finance loans that often target the poor, but they did not possess the credit history or adequate collateral that would enable them to borrow money from commercial banks. As a result, their ability to expand their business was stymied by lack of needed finance. Thus, to energize and strengthen the growth of small and medium size enterprises in Ethiopia and other African countries, governments need to consider creating credit guarantee facilities that could channel direly needed funds to credit-worthy opportunity entrepreneurs through existing financial institutions. Such an arrangement already exists in the agricultural sector and can be adapted to assist burgeoning opportunity entrepreneurs. To alleviate the funding constraints, making bilateral and multi-lateral arrangements with donors should be explored and NGOs may be encouraged to play a more active role in supporting entrepreneurial endeavours in the nation. Providing funding to support aspiring and current opportunity entrepreneurs would certainly require committing a significant amount of resources but it is a worthy investment that will pay handsome dividends in the long-term.
7.2 Improve capacity to support entrepreneurial efforts. The opportunity entrepreneurs who participated in this exploratory study indicated that they needed assistance with training and other capacity enhancing skills so that they could run their businesses more efficiently and effectively. Institutional capacity that can provide technical and managerial support and training services to current and budding entrepreneurs is inadequate in Ethiopia as is the case in many other African nations. To minimize the adverse impact on Ethiopian entrepreneurs of limited technical competency, inadequate access to markets and finance, and other constraints, Amha and Ageba (2006) proposed providing critical business development services (BDS). Such services, among others, may include quality management techniques, productivity improvement programs, process design, product development and market analysis. The collaboration of national and local government agencies, universities, the Ethiopian Management Institute (EMI) and the Chamber of Commerce is critically important to adequately meet the demand for these services and to efficiently utilize the available limited resources. EMI and local universities may offer programs to train aspiring and/or current entrepreneurs to start and grow new ventures (Sriram and Mersha, 2006), and bilateral and multilateral assistance programs may target developing institutional capacity initiatives. Business schools in the US and Europe have well-established programs, both degree granting and short-term workshops, to impart the necessary business skills to entrepreneurs and universities in Ethiopia and other African countries with a strong educational infrastructure can develop similar programs. The creation of incubator programs and the provision of temporary working facilities to promising new enterprises can further energize entrepreneurial ventures. Yet another potential source of valuable resource for strengthening the capacity of local entrepreneurs can be the educated and skilled Ethiopians residing abroad, particularly those who have become successful entrepreneurs and management experts in their adopted countries. Thus, there is critical need for capacity building intervention to strengthen opportunity entrepreneurs in Ethiopia and in other African nations.

7.3 Assist necessity entrepreneurs to transition to small or medium size enterprises. A major factor that contributes to a lack of progression from necessity to small and medium-size enterprise (SME) status is that most micro entrepreneurs take up entrepreneurial activity only to generate enough income to meet a specific short term need. For example, the primary motivation, at least initially, for many young men and women from the Gurageh ethnic group in Ethiopia for engaging in entrepreneurial activities (such as working as peddlers and engaging in a multitude of retail and service activities) is to send money home to support those that they left behind and to meet certain social obligations. In addition, their families expect them to come home at least once a year for major holidays and other important social events. However, attending such events comes at a huge cost: the young entrepreneurs not only squander their hard earned resources to purchase relatively expensive items for themselves and for their relatives and neighbours; to finance these purchases, those who are engaged in some form of retail business may find it necessary to liquidate some or all of their inventories only to start from scratch all over again upon their return to Addis or other cities. Clearly, conforming to cultural norms and traditions has detrimental effect on the potential growth and success of many budding entrepreneurs. While there are some who transition from necessity entrepreneur status and establish successful business ventures, these are very
few compared to the large number of necessity entrepreneurs who can barely stay afloat. Thus, a concerted educational effort aimed at steering some of the necessity entrepreneurs away from wasteful conspicuous consumption practices may help them grow their business and transition to become growth-oriented business ventures.

This study suggests that in terms of motivation and perception of an ideal job, many Ethiopians have the drive and desire to pursue entrepreneurial opportunities and that with the right training, support and encouragement, they can become successful entrepreneurs. The findings also indicated that to be effective, the interventions used to help current and aspiring entrepreneurs to survive and prosper should be tailored separately to the specific needs of necessity and opportunity entrepreneurs. Based on feedback gleaned from this exploratory study, Table 9 summarizes proposed policy interventions that may be applicable to necessity and opportunity entrepreneurs in Ethiopia.

8. Conclusions and directions for future research

The contribution of entrepreneurial endeavour to an economy has long been recognized, but the dilemma in many emerging markets has been the question of how best to nurture, develop and support new business start-ups and how to help existing businesses to expand and grow. In Africa, given the preponderance of necessity entrepreneurs, the focus of many of the interventions aimed at stimulating entrepreneurship has often been with these micro enterprises in mind. The types of interventions provided should target the needs of different groups of entrepreneurs and must consider the specific socio-economic and cultural environment prevailing in each country since a “one-size-fits-all” strategy cannot effectively address the needs of different entrepreneurs in all developing nations. Further, this study indicated that even within the same developing country, necessity and opportunity entrepreneurs have distinctly different needs and challenges.

This study also showed that opportunity entrepreneurs in Ethiopia often find themselves struggling with financial and human resource constraints and have limited managerial skills sets. While some macro-level changes such as capacity building, cutting start-up costs, offering credit and finance and improving the infrastructure will undoubtedly help all private sector businesses, the results of this study suggest that a more refined and focused approach will be needed if certain initiatives are to have their maximum impact. Educated and skilled opportunity entrepreneurs will have needs of a far different order of magnitude than someone that is pushed into starting a subsistence-level business in order to supplement the family income. Whereas assistance programs should target both types, this paper argues that a thorough assessment should be made of the entrepreneur and the business before support is extended in order that the intervention is properly calibrated to fit the need. For example, the nature of the training, provision of finance, and building of managerial capacity are all issues that have to be custom-fitted to the business venture. Therefore, despite strong motivation to start a business, in developing countries like Ethiopia and in Africa in general, it is particularly important to thoroughly assess baseline levels of skills, resources and capabilities before embarking on funded assistance so that these resources and motivations can be effectively channelled. In view of the potentially
significant impact of opportunity entrepreneurs in creating jobs and income, this group of entrepreneurs should be identified early and support brought to bear on these individuals and their businesses so that they can be even more effective in contributing to the nation’s economic growth and prosperity.

Future research should also look into opportunities for women entrepreneurs. While the number of women entrepreneurs is growing around the world and in Africa, their socio-economic contributions have often been underestimated (Woldie and Adersua, 2004). According to Global Entrepreneurship Monitor, one out of 11 women in the world today is an entrepreneur (“Global 360”, 2004). However, anecdotal evidence suggests that a significant proportion of women in developing countries are necessity entrepreneurs and that the participation of women in opportunity businesses is very limited (for example, only 10% of the opportunity entrepreneurs who participated in this study were women). To enhance the participation of women in more value-added entrepreneurial initiatives requires identifying the unique challenges facing women entrepreneurs and developing mechanisms for addressing these challenges. Examining the effectiveness of initiatives launched by the Economic Commission for Africa and the International Labour Organization (UNECA, 2000; ILO, 2003) to mobilize African women entrepreneurs may also be fruitful avenues for future research.

The literature indicates that in many African nations, political instability, the efficiency and transparency of public administration, uncertain property rights, level of taxation and prevalence of corruption not only affect the number of business start-ups but also determine business success. For example, Bonaglia and Goldstein (2006) found that the investment and political climate in Egypt impacted foreign direct investment in the country. The socio-economic environment also has significant impact on entrepreneurial success. As can be seen from Table 2, the cost of getting a business license in sub-Saharan Africa is among the highest in the world. This also works against aspiring entrepreneurs who may not have learnt the ropes or do not have the resources to get the desired results (Takyi-Asiedu, 1993). To further stimulate entrepreneurial endeavours in Ethiopia (and the rest of Africa), therefore, it is crucial that a more business friendly environment is created and easy-to-navigate administrative systems are put in place. Currently business process reengineering (BPR) is being introduced in government agencies in Ethiopia the impact of which is not yet fully documented. Future research may examine the relationship between improved business processes and the rate of entrepreneurial success in the country.

We should emphasize, however, that in order for these findings to be generalized, they need to be replicated using larger samples in Ethiopia and in other countries. For instance, recent research indicated that many new ventures in South Africa were started by opportunity rather than necessity entrepreneurs (Naude et al., 2008). This further reinforces the point that interventions must be targeted and sharply defined to fit not only different types of entrepreneurs in the same country but also adjusted to the specific needs of entrepreneurs in different nations.
Table 9
Proposed interventions for necessity and opportunity entrepreneurs

<table>
<thead>
<tr>
<th>Type of intervention</th>
<th>To assist necessity entrepreneurs</th>
<th>To assist opportunity entrepreneurs</th>
</tr>
</thead>
</table>
| Provide financial resources | ● Micro finance  
● Traditional funding sources such as *ukub* in Ethiopia | ● Small bank loans;  
● Identify other financing sources |
| Streamline bureaucratic hurdles and improve the business climate | ● Establish a one-stop service facility to facilitate new venture start-up process.  
● Provide assistance in navigating the bureaucratic system as necessary such as registration and licensing;  
● Increase transparency  
● Apply established laws and procedures consistently  
● Keep the cost of doing business (licensing fees) reasonably low | ● Establish a one-stop service facility to assist opportunity entrepreneurs in the Diaspora to navigate the bureaucratic system.  
● Assist current local entrepreneurs with their specific needs to further strengthen their business success  
● Increase transparency  
● Apply established laws and procedures consistently  
● Keep the cost of doing business (licensing fees) reasonably low |
| Facilitate managerial capacity to enhance productivity and profitability | ● Encourage/educate necessity entrepreneurs to minimize conspicuous consumption and to accumulate wealth.  
● Isolate cultural practices that dampen entrepreneurial success  
● Educate necessity entrepreneurs on operational effectiveness and wealth accumulation so that they can transition to more established business ventures. | ● Assist opportunity entrepreneurs to improve their operational efficiency and profitability  
● Assist local entrepreneurs to increase their competitiveness. |

*ukub* is an informal credit association in Ethiopia whereby members contribute a fixed amount of funds each week and the amount so collected is advanced to one of the members interest free. The order in which weekly contributions are distributed is determined by lottery. Those who won the lottery but do not need the fund right away may opt to yield in favour of someone else for a fixed fee—usually an agreed upon percentage of the weekly jackpot.
References


Introducing Flow Theory to Explain Interactive Online Shopping Experience in a Travel Context

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Abstract: Online travel commerce has evolved significantly from the initial sales of less complex products like airline tickets, accommodations and car rentals to include more complex products like vacation packages and cruises. However, many online travel portals have fallen behind in terms of creating a compelling online environment for customers. Consumers’ on-line shopping behavior is becoming increasingly complex with the evolution of hedonic and utilitarian shopping practices. These two types of shopping practices have a significant effect on formation of consumers’ attitudes towards a website and eventual purchase intentions. The proposed model delineates consumers’ preference towards a web site for hedonic and utilitarian purchase contexts when flow variables ‘control’, ‘cognitive enjoyment, and ‘focus’ are involved. The results of this study help online travel businesses to identify unique web quality features that satisfy the needs of hedonic as well as utilitarian customers. Moreover, this model shows that a successful travel site could entice utilitarian customers to engage in hedonic features that might result in positive attitude formation and consequent future revisits.

Key words: e-commerce, on-line travel; hedonic; utilitarian; flow theory; consumer attitudes;

Introduction:

The Internet’s global reach, interactivity, and information-rich context have redefined the travel industry. Online travel commerce has evolved significantly from the initial sales of less complex products like airline tickets, accommodations and car rentals to include more complex products like vacation packages and cruises (Beldona, 2005). The online travel sales grew from 33.7 billion in 2001 to 58 billion in 2005. However, Blank (2000) has reported that online businesses have experienced potential loss of $6.1 billion in 2000 when customers abandoned the purchase process after visiting a web site. In the same vein, a report by DoubleClick (2004a) has indicated that the percentage of customers who buy online per Website visit remains low at less than 5%. In addition, many online travel portals have fallen behind in terms of creating a compelling online environment for customers (Tierney, 2000).

According to Bolton (1998), creating satisfying shopping experiences plays a major role in enhancing customer retention and loyalty which may result in more desirable outcomes eventually. Many research studies have established a relationship between web quality
and customer satisfaction (Loicacono, Watson, & Goodhue, 2002; Ziethaml, Parasuraman, & Malhota; 2002). One of the effective methods of achieving a competitive advantage and differentiating strategy is to provide superior service quality. Consequently, many scale measures have been developed to measure customers’ perceptions of service quality. For example, Zeithaml et al. (2002) have developed e-service quality; Yoo and Donthu (2001) have introduced SITEQUAL; and Parasuraman et al. (2005) have developed the E-S-QUAL.

Van Reil, Lemmink, Streukens, and Liljander (2004) examined the dimensions of online travel service quality by expanding the SERVQUAL model. They reported that accessibility, navigation, design, reliability, responsiveness, and customization are the major online service quality dimensions. Moreover, Law and Wong (2003) concluded that the following three dimensions could motivate customers to make online travel purchases: secure payment methods; different price ranges for products and services; and user-friendly systems. In the travel area, Jeong and Lambert (2001) developed E-QUAL to test website quality dimensions in a travel context. The E-QUAL scale is composed of seven dimensions: content and purpose, navigation, responsiveness, personalization and customization, accessibility, design and presentation, and background. Table 1 shows a comprehensive review of the different measures of online service quality measures.

Recently, there has been a growing focus of research on two categories of online consumer behavior; experiential-oriented (hedonic) shopping behaviors; and utilitarian-oriented shopping behaviors. Attributes of the hedonic shopping include social interaction, entertainment, fun, and intrinsic motivation. On the contrary, utilitarian shopping aspects include convenience, goal attainment, information availability, extrinsic motivation, efficiency, and expressions of accomplishment. Research supports that both shopping orientations (experiential and utilitarian) could potentially affect consumer responses toward online shopping (Hoffman & Novak, 1996; Childers, Carr, Peck, & Carson, 2001; Fiorre & Jin, 2003). Ultimately, one can state that the degree to which online travel portals fulfill consumers’ experiential-oriented and/or utilitarian-oriented needs through innovative interactive quality designs could affect the amount of shopping dollars consumers spend in each online environment.

Over the past decade, there has been a growing consumer research suggesting the use of the “flow construct” as a tool for creating compelling online environments (Hoffman & Novak 1996). Novak, Hoffman, and Yung (2000) reported that a compelling online consumer experience is positively correlated with fun, recreational and experiential uses of the web. Interestingly, later Novak, Hoffman, and Duhacheck. (2003) found more evidence of benefits of ‘flow’ more for utilitarian-oriented rather than experiential-oriented activities. The flow construct has been proposed as an important concept for understanding online consumer behavior, and as a way of defining the nature of compelling online experiences (Novak et al., 2003 ; Mathwick & Rigdon, 2004). However, there is a disagreement over the applicability of the flow construct in online shopping context. For example, authors like Zeithaml, Parasuraman, & Malhorta (2002) claimed that ‘flow’ is irrelevant in online contexts.
Some studies have examined the experiential shopping orientation and the utilitarian shopping orientation in light of the controversy in using flow construct (Novak et al., 2003; Sicilia, Ruiz, & Munuera, 2005) for online shopping incidences. In case of online shopping contexts, some web interactive features are thought to stimulate more utilitarian-oriented consumers i.e. the assessment of product information feature (Fiorre et al., 2005), while others are more associated with experiential-oriented i.e. a view of best selling products feature (LaRose, 2001). However, the theoretical and empirical links among shopping orientations, utilization of online interactive features, and site attitude are yet to be established. The present study proposes a model of online shopping experience, integrating and understanding of the flow state construct; a state where consumers’ self-control is diminished and their sense of time becomes distorted. Additionally, given a growing recognition that shopping involves hedonic as well as utilitarian outcomes, this study examines whether interactive web features could positively stimulate a flow experience and thereafter positive site attitudes regardless of the consumer’s shopping orientation (utilitarian or experiential). In other words, the purpose of this study is to examine whether high interactive web features play a pivotal role in enhancing positive site attitudes through the invigoration of a flow state regardless of consumers’ shopping orientation.

**Shopping Orientations**

Shopping orientation is defined as a shopper’s attitude toward shopping activity that may vary with the situation. This definition is based on Holbrook’s (1986) definition of a shopping value as a key outcome or expected benefit pursued by shoppers. The web can be used as a medium for engaging in many diverse types of behaviors: merely exploring, searching for specific information, entertaining oneself, or shopping (Parsasuraman & Zinkhan, 2002). Such web usage behaviors are likely to be motivated by the benefits from using the site, experiential as well as utilitarian (Childers et al, 2001). Several studies have revealed that the benefits consumers seek from using the web are categorized into (1) experiential (hedonic) shopping orientations obtained when the Web is used for the enjoyment of the online experience itself, and (2) utilitarian shopping orientations resulting from achieving specific goal (Fischer & Arnold, 1990). The online hedonic-orientations are based on fun and amusement via interacting with the Web, whereas utilitarian shopping orientations are goal-oriented (Holbrook, & Hirschman, 1982; Babin, Daren, & Griffin, 1994).The degrees to which online travel portals fulfill the utilitarian and hedonic consumer needs will affect the perception of website quality. Research on Web quality design (Menon & Kahn, 2002; Eroglu, Machleit, & Lenita, 2003) indicated that hedonic and utilitarian orientations affect the value driven by consumers.

Although utilitarian and experiential orientations are distinct dimensions, they are not necessarily mutually exclusive. For example, if a customer finds the utilitarian product that he/she is looking to buy at a low price at the first travel Web site he/she navigates, both utilitarian and experiential outcomes could be found in this shopping experience. That is, utilitarian value is present because of the efficiency and easiness of the product acquisition, while hedonic value comes from the excitement caused by the bargain sale.
Alternatively, consumers may visit a travel web site with a specific purchase goal in mind (i.e. airline ticket purchase), but be attracted by an online shopping recommendation “car rentals bargain sale” (unplanned purchase). This suggests that online shopping possessed multiple shopping orientations, combining the pursuit of utilitarian and experiential outcomes (Brown, Pope, & Voges, 2003).

**Utilitarian Shopping Orientations:**

The Internet has been described as a perfect online channel for utilitarian oriented shoppers (Donthu & Gilliland, 1996). A Website is seen offering utilitarian benefits when offering the following quality dimensions: saving time/effort, reducing risk, and increasing likelihood of finding a superior alternative (Klein, 1998). Utilitarian consumer behavior has been described as goal-oriented, deliberate, and based on rational view of consumer behavior (Batra & Ahtola, 1991; Engel, Blackwell, & Miniard, 1995). Moreover, shoppers may find a utilitarian value when navigation needs are accomplished successfully rather than the experience itself (Babin et al., 1994). Utilitarian users also highly value time allocations and regard time as a resource to be managed carefully (Cotte & Ratenshwar, 2003). According to Huang (2005), the utilitarian customers’ buy online because of the benefits derived from such a purchase in terms of convenience and money savings. For utilitarian users, web designers need to be aware of availability of information and intuitive design interfaces that facilitate easy use of the site for information search (Wolfinbarger & Gilly, 2001).

**Experiential Shopping Orientations:**

Experiential shopping orientation refers to the fun, amusement, and sensory stimulation that customers experience in return for expending resources such as time and money (Holbrook & Hirschman, 1982). Some studies have examined the hedonic aspect of a Website quality as: fun, playfulness, pleasure, enjoyment, increased arousal, heightened involvement, perceived freedom, fantasy fulfillment, and escapism (Koufaris, Kambil, & LaBarbera, 2002; Huang, 2005). According to social cognitive theory, these interactive features systematically undermine the three sub-functions of self-regulation (LaRose, 2001): self-monitoring, judgmental process, and self-reactive influence. Website quality features that undermine self-regulation are called “experiential shopping features”. For example, the excitement generated by e-mail alerts of new products may overwhelm self-monitoring of one’s spending behavior.

**Interactive Online Quality Features:**

Interactivity is a two-way communication between consumers and the machine-interface in order to change and customize a web site’s look, feel, content (Hoffman & Novak, 1996, Palmer, 2002; Zhu & Kraemer, 2002) according to customers’ own preferences. The interactivity in a broader meaning emphasizes concepts such as the direction of communication, user control, and time (McMillan & Hwang, 2002), and active control, two-way communication (Liu & Shrum, 2002). In this study, there are two levels of interactivity (low interactive utilitarian shopping features) and (high interactive experiential shopping features). Low interactivity level is interactivity that utilizes textual descriptions of product information, price comparison features, and reviews written by
other shoppers. Additionally, a search engine is one such feature (Zhang, 2002), since shoppers could find the products they intend to buy easily, without browsing, using the search engine.

On the other hand, high interactivity experiential features are associated with increased customers’ satisfaction (Devaraj, Fan, & Kohli, 2002; Palmer, 2002; Teo, Oh, Liu, & Wei, 2003). The high interactivity quality features include, media vividness “the degree of media richness in a site, such as text, images, sound video, and 3-D simulations” (Fiore, 2005), customization, is the service attributes that recognize the preferences of individual customers, and allow them to tailor their choice of products and services to create individual user experiences (McKinney et al. 2002), personalization, is giving customers individualized attention, understanding the specific needs of customers, and providing service related to convenience that creates a personal and friendly user interface (Madu & Madu, 2002, Yang & Jun, 2002; Zhu & Kraemer, 2002), list of best selling products (i.e. hotels, cruises, vacation packages), lowest price guarantees, list of good deal items, and list of new items “vacation packages”.

Flow Theory

Flow is a useful construct for describing human-computer interactions (Csikszentmihalyi, 1990; Ghani & Deshpande, 1991; Trevino & Webster, 1992; Webster et al., 1993). The flow theory was developed by Csikszentmihalyi in 1975. Csikszentmihalyi (1975, p. 4) defined flow as “the state in which people are so involved in an activity that nothing else seems to matter”. Additionally, Csikszentmihalyi operationally defined flow as “the holistic sensation that people feel when they act with total involvement” (p. 36). When people are in flow, they shift into a common mode of experience when they become absorbed in their activity. This mode is characterized by a narrowing of the focus of awareness, so that irrelevant perceptions and thoughts are filtered out, by loss of self consciousness, by responsiveness to clear goals and unambiguous feedback, and by a sense of control over the environment (Csikszentmihalyi, 1977).

As users shop online with a clear goal, they are using their Internet skills to complete a particular task at hand, either for entertainment or product search and purchase. Consumers while navigating the Internet may experience three main elements of flow: control, attention focus, and cognitive enjoyment (Webster et al. 1993). Users are controlling the interaction with the site through system response, feedback, or choices among alternative in the site. As they are concentrating on their Web surfing and immersed in their online shopping, users filter out irrelevant disturbing stimulus from the environment, achieving attention focus. The website provides curious new options for interaction, and the users may be carrying out this site navigation for its own sake and enjoyment (Webster et al. 1993). These conditions of control, attention focus, and cognitive enjoyment create a flow state, as the Internet allows for a flow experience (Chen, Wigard, & Nilan, 1999; Novak et al. 2000, 2003). In the same vein, Novak et al (2000) empirically measured and modeled a set of key constructs related to flow, including interactivity, involvement, focused attention, skill, control, arousal, challenge, telepresence, time distortion, and exploratory behavior.
While consumers are shopping online, they formulate an attitude towards the site. While they are in a state of flow, they are most likely to learn about the content of a site, and consequently this learning results in attitudinal changes, such as positive site attitudes. Consumers may ultimately decide as a consequence of their online shopping to intend to purchase an item or a product in the future. These consequences are important to online travel businesses, as they may impact their profit margins and bottom line.

Building upon the work of Csikszentmihalyi, flow has been studied in the online context and has been recommended as a possible metric of the online consumer experience (Webster et al., 1993; Ghani and Deshpande, 1991; Hoffman & Novak, 1996). Perhaps, as some have suggested (Hoffman & Novak, 1996; Novak, Hoffman, & Duhacheck, 2003) consumers who utilize interactive Website features enter a seamless sequence of responses, a “flow” state in which their sense of time and reality becomes distorted and their self-control is diminished. Consequently, the convenience of online shopping could facilitate the flow state, as well rational consideration of minimizing search and transaction costs.

Hoffman and Novak (1996) are two of the few pioneers who apply the optimal experience theory to people’s online experience. They proposed a conceptual flow model in a computer-mediated environment. Later on, Novak et al. (2000) tested the model with data collected online. Their study concluded that higher levels of challenge and skill contribute to higher level of people’s experience. More recently, Hoffman et al. (2003) found that online flow experience is more likely to occur in task-oriented activities than during recreational activities. On the other hand, Nantel, Senecal, and Gharbi (2002) found that flow contributes to more hedonic online shopping experiences than utilitarian shopping. Additionally, King (2003) who applied the concept of flow to general Website design believes that people in flow tend to be more playful and exploratory, and presumably are willing to buy more products and services.

Model of Interactive Online Shopping Experience in Travel Context:

As shown in figure 1, utilitarian and experiential orientations are hypothesized to be first order independent variables. Since utilitarian orientation consumers focus on the purchase of products as the primary goal of shopping activity, a strong positive relationship between utilitarian shopping orientation and site attitude is expected (Anderson, 1971; Babin et al., 1994; Donthu & Gilliland, 1996).

H1: Utilitarian shopping orientation is positively related with site attitude.

An indirect effect on site attitude of online shopping through utilitarian interactive features (low interactivity) is also expected. A utilitarian orientation leads consumers to Web features that save their search costs in order to pursue their utilitarian outcomes. Such low interactivity features may include search engines, price information, price comparison functions, and product reviews from other shoppers. Thus, the following hypotheses are proposed:
H2: Utilitarian oriented shopping is positively related with the usage of utilitarian web features (low interactivity).

H3: Usage of utilitarian shopping features is positively related to site attitude.

H4: Experiential shopping orientation is positively related with the usage of experiential shopping features (high interactivity)

On the other hand, Klein (2003) and Chen et al. (1999) reported that consumers perceive more flow with high interactivity features as opposed to low interactivity features. This supports the fact that information integration gives the consumer a high level of freedom and control (Wolfinbarger & Gilly, 2001). As such, we predict the following hypotheses:

H5: experiential Website features is positively related to:
   a- The control dimension of flow.
   b- The attention focus dimension of flow.
   c- The cognitive enjoyment dimension of flow

Site attitude is the user’s positive or negative predisposition towards a Website. Site attitude is positively related to attitude toward the brand and the purchase intention (Bruner & Kumar, 2000), shopping likelihood and site loyalty (Donthu, 2001), and satisfaction with the online shopping (Szymanski & Hise, 2000; Yang, Peterson, & Huang, 2001). Some researchers reported a positive relationship between the state of flow and customers’ attitude toward making purchases on the web (Baronas & Louis, 1988; Trevino & Weber, 1992). On the other hand, Baronas and Louis (1988) found that control, a dimension of flow, to have a positive influence on users’ attitudes toward the site. According to Childers et al. (2001), enjoyment is a positive predictor of attitude toward the online site. Also, Agrawal and Karahanna (2001) indicated that cognitive absorption, a construct based on flow dimensions such as control, curiosity, attention, and enjoyment, is an antecedent predictor of site attitudes.

H6: (control dimension, attention focus component, cognitive enjoyment) of flow increases the likelihood of users site attitude

Online consumers are both utilitarian and experiential oriented. In addition, consumers who start shopping with utilitarian orientations might subsequently pursue hedonic outcomes (Beaty & Ferrell, 1998), particularly after being exposed to Website features that encourage experiential shopping activity (LaRose, 2001). For example, lists of best selling items and lists of new items might be able to reduce the search time and effort of shoppers.

H7: There is a positive relationship between utilitarian shopping orientation and the usage of experiential shopping features (high interactive).

Research Methodology:

Sampling and Data Collection:
The subjects of the study are undergraduate students at a large Midwestern university and participation in the study is voluntary. The sample size is approximately 230. A cover letter explaining the purpose of the research and the URL of the Web survey site will be provided. To achieve reliability, previously validated and reliable scales are used in the present study (please refer to table 2). In addition, a pilot study is conducted to assess the reliability of the scales. To do so, a content analysis will be conducted to list the maximum number of hedonic and utilitarian features for each of the five prominent travel sites (as reported by J.D Powers consumer reports, 2005). These sites will be selected based on a ranking published by J.D. Power Consumer report (2005). The J.D. power report (2005) ranked the top five websites based on customers’ satisfaction in terms of web quality dimensions. According to the report, Orbitz was ranked first; Expedia, Hotwire & Travelocity were ranked second; Hotels.com was ranked third; and Priceline.com was ranked last. To achieve reliability, a pilot study (n=50) will test whether the extracted features are hedonic or utilitarian. After that, participants will rank each of the features in terms of perceived value.

A Website that is a replication of expedia.com, a major online travel site, will be designed under the name of “BestTravel.com”. Not only “BestTravel.com” is a replication of expedia.com, but it also combined the most important hedonic (high interactive) and utilitarian (low interactive) features recommended in the pilot study. For example, if a hedonic/utilitarian feature was ranked #5 in importance and was not available within expedia.com, this feature will be added to “BestTravel.com”.

The experiment will take place in a computer lab. This allows for tighter control and reduced distractions and interruptions. In the lab, subjects will be directed to URL link to “BestTravel.com” and will be given a shopping task to complete. After they finish the practice task; participants will be directed to the URL link to answer the survey questions.

**Data Analysis:**
As suggested by Hair et al., (1998), the analysis will be conducted using a two phase approach. First, a confirmatory factor analysis will be used to measure the adequacy of the measurement model. Unidimensionality of the constructs, reliability using construct reliability and item reliability will be tested. Having ensured that the scale is unidimensional and reliable, the next step will be to check construct validity using convergent and discriminant validity. Then the measurement model will be evaluated and finalized. In the second phase the structural model will be evaluated. The overall model fit in both measurement and structural models was evaluated using conventional fit indices including Chi-Square/df ratio, CFI, NFI, PNFI, RFI, IFI and RMSEA (Jöreskog & Sörbom, 1993; Hair et al., 1998, Schumacker & Lomax, 2004). The data will be analyzed using the statistical software SPSS 15 and Lisrel 8.

**Implications for Theory**
This study contributes to the online consumer behavior literature by utilizing flow theory and investigating the mediating effects of web interactivity features (hedonic and utilitarian) and flow experiences on website attitude. At the same time, given a growing
recognition that shopping involves hedonic as well as utilitarian outcomes, this study examines whether interactive web features will positively stage a flow experience and thereafter positive site attitudes regardless of the consumer’s shopping orientation (utilitarian or experiential). Thus, the results of the paper will confirm the validity of the use of flow in an online travel context. Additionally, one of the major contributions of this study is to expand the number of hedonic and utilitarian quality features beyond the nine-item measure provided in literature (LaRose, 2001; Zhang, 2002). The content analysis of the five prominent travel sites will yield a comprehensive list of hedonic and utilitarian features.

Implications for Practice
Online travel services should not assume that one combination of web site features can effectively serve all customers. The results of this study would allow online travel businesses to identify specific web quality features that satisfy the needs of hedonic as well as utilitarian customers. Moreover, a successful travel site would entice utilitarian customers to engage in hedonic features that might result in positive attitudes and future revisits. Additionally, web site designers and managers need to consider integrating features that make shopping experiences more enjoyable by creating contexts that facilitates the flow state. In turn, this flow state will potentially increase purchase intentions, traffic, and repeat visits on the site, resulting in positive site attitudes and more or longer visits. In sum, the findings should inform web site designers to create high quality travel sites that facilitate the flow state by providing interactive features and by understanding online shopping behaviors that users’ exhibit.

Limitations and Future Research:
A college student sample is used for the present study, and college students do not represent all Internet consumers. This may impact the external validity and the possibility of generalizing the results to the population. Additionally, there is possibility that there might be a high inter-correlation between the hedonic and the utilitarian features, as indicated in the methodology section; this inter-correlation could be resolved by the pilot study that is aimed to distinguishing between both features. Finally, experiments that are normally conducted in laboratory settings lack the real world realm (Benbasat, 1989). However, laboratory experiments provide for tighter control and greater objectivity and increase internal validity.

This research only addressed site attitude as a consequence of the online shopping. Future studies would also want to consider other variables, such as exploratory behavior and the learning experience associated with surfing the web. In addition to the positive outcomes of flow, future research must consider the negative outcomes of flow. Examples of such negative consequences: too much flow may distract the consumer from purchase-related activities; also flow has been linked to over-involvement which leads to mental and physical fatigue. Finally, the model of this study could also be expanded to other consequences of attitude formation such as intention to purchase, repeat visit, and word-of-mouth.
References


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Figure 1: A proposed SEM summarizing the casual relationships among consumer shopping orientations, web site features, and site attitude. LI refers to low interactivity features, whereas HU refers to high interactivity.

Table 1: Summary of Previous Studies on Service Quality Measures

<table>
<thead>
<tr>
<th>Study</th>
<th>Key dimensions of online service quality</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aladwani and Palvia (2002)</td>
<td>Content quality; appearance; trust</td>
</tr>
<tr>
<td>Barnes and Vidgen (2001)</td>
<td>Content quality, usability (ease of use, navigation); reliability; personalization</td>
</tr>
<tr>
<td>Cox and Dale (2001)</td>
<td>Accessibility; communication; credibility; understanding; appearance; availability</td>
</tr>
<tr>
<td>Jeong and Lambert (2001)</td>
<td>Ease of use; usefulness, information content; security; responsiveness; personalization</td>
</tr>
<tr>
<td>Kaynama and Black (2000)</td>
<td>Security; responsiveness; personalization; information content</td>
</tr>
<tr>
<td>Loicacono et al. (2002)</td>
<td>Information-fit-to-disk; interactivity; trust; response time; ease of understanding; online completeness; emotional appeal; consistent image; intuitive operations; visual appeal</td>
</tr>
<tr>
<td>Madu and Madu (2002)</td>
<td>Ease of use; security, responsiveness; personalization; customization</td>
</tr>
<tr>
<td>Ranganathan and Ganapathy (2002)</td>
<td>Quality of information; security</td>
</tr>
<tr>
<td>Szymanski and Hise (2000)</td>
<td>Convenience; site design; financial security</td>
</tr>
<tr>
<td>Van Reil et al. (2004)</td>
<td>Accessibility; navigation; design; responsiveness; personalization</td>
</tr>
<tr>
<td>Yoo and Donthu (2001)</td>
<td>Ease of use; aesthetic design; processing speed; security</td>
</tr>
<tr>
<td>Zeithaml et al. (2005)</td>
<td>Efficiency; fulfillment; system availability; privacy; responsiveness; contact; personalization; information content</td>
</tr>
</tbody>
</table>
Table 2: Measure of the Six Constructs:

**Utilitarian Shopping Orientation:**
Likert scale (from 1 strongly disagree to 7 strongly agree) (Babin et al. 1994)

1- I accomplish just what I want to while shopping online
2- I cannot buy what I really need.
3- While shopping online, I find just the item(s) I am looking for.

**Experiential Shopping Orientation:**
Likert scale (from 1 strongly disagree to 7 strongly agree) (Babin et al. 1994)

1- I continue to shop online, not because I have to, but because I want to.
2- Online shopping truly feels like an escape.
3- I enjoy shopping online for its sake, not just for the items I may have purchased.
4- I have a good time because I am able to forget my problems.

**Utilitarian Shopping Features:**
Likert scale (from 1 strongly disagree to 7 strongly agree) (LaRose, 2001; Zhang, 2002)

1- Search engine for findings products I want.
2- Product price information.
3- Price comparison with other web sites.
4- Reviews written by other shoppers.

**Hedonic Shopping Features:**
Likert scale (from 1 strongly disagree to 7 strongly agree) (LaRose, 2001; Zhang, 2002)

1- Email alerts of special offers.
2- List of new items.
3- List of best selling items.

**Flow Experience Scales**
Likert scale (from 1 strongly disagree to 7 strongly agree) (Webster et al. 1993)

**Control**

1- when using the web site, I felt in control
2- I felt that I had no control over my interaction with the site
3- The site allowed me to computer interaction

**Attention Focus:**

1- When using the site, I thought about other things.
2- When using the site, I was aware of distractions.
3- When using the site, I was totally absorbed in what I was doing.

**Cognitive enjoyment:**

1- Using the site excited my curiosity.
2- Using the site aroused my imagination.
3- The site was fun for me to use.

**Site Attitude**

7-point Likert scale (from 1 strongly disagree to 7 strongly agree) (Teo et al. 2003),

1- This site is interesting.
2- This site is enjoyable.
3- I like this site
CAN JAPANESE MANAGEMENT STYLES BE APPLIED TO AFRICA

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ABSTRACT

Most of the remarkable managerial know-how of the Japanese is gifted by their culture and society. Culture affects the way problems are perceived and solved. Societal learning also establishes horizons of perception. Managerial efficiency in any business organisation is the fundamental key to success. A good number of managers all over the world are showing a great deal of interests in Japanese ways of managing business because of the great success of the Japanese corporations throughout the world. The fact that the Japanese manage their enterprises efficiently and effectively without using the excessive scientific and advanced management tools has shaken a good number of countries, notably the United States of America. This paper discusses the fundamental management styles of Japan with a view to establishing its applicability to Africa.

Introduction

The success of managers in Asian countries like Japan, Singapore, South Korea, and Taiwan over the years has been rapid. Recently a great deal of interest existed among managers around the world to find out the Japanese way of managing business, because of the tremendous success of the Japanese corporations throughout the world. The fact that the Japanese manage their enterprises very well without the excessive use of scientific and advanced management instruments has shaken the confidence of the Americans in their approach. The latter appear to be more inclined to import the Japanese art of management, while their self-acclaimed monopoly in scientific management was already eroded by the worldwide presence of professional managers.

Western management principles have been borrowed wholesale in African countries, and African managers practice them, irrespective of whether or not the culture permits. On the other hand, Japan also started its economic development in the thirties; it was rebuilt from a devastated state. The Japanese have been extremely effective in borrowing from the West, in the areas the West excelled. But, in the process, they did not become Americanised or Europeanised. Instead, they took the best the West had to offer which
could be transplanted in the East and use it. This is because, throughout history, various management styles have succeeded one another in attracting the attention of the world’s management scholars to investigate and recommend for practice by fellow managers.

In addition, the Japanese have developed their own skills of management, which stem directly from their cultural and social values and beliefs. This blending has led Japan to emerge as a great economic power. Empirical statistics testify to Japanese superiority over any other nation and to the decline of America’s industrial standing. This trend has made Japan a subject of research throughout the world since 1960 and vigorous investigations and analyses still continue to bring forth the factors responsible for the spectacular success of the nation.

The Meaning of Managerial Efficiency

Managers of today face a variety of interesting and challenging situations. The average executive in Africa works at least 45 hours a week and faces increased complexities posed by globalisation, domestic competition, government regulation and shareholder pressure. The task is further complicated by rapid change, inadvertent disruption as well as minor and major crises such as the current economic, financial and political crises in Africa. In this context, managerial efficiency—the use of the limited resources judiciously and in a cost-effective manner—should be given priority by managers in African organisations. The second emphasis should be on managerial effectiveness in terms of making the right decisions and successfully implementing them. This is because managerial efficiency and effectiveness compliment one another.

The ability to develop and use appropriate strategies that will use the best available means for the attainment of desired ends is an important aspect of effective management. Managers cannot live in isolation from the realities of life, nor conduct their operations without reference to the existing economic and technological situation. Hence one of the most significant aspects of effective management is the ability to plan for the future by using the best available resources for the attainment of desired objectives. In this context, management is the ability to develop and implement appropriate strategies in given circumstances. It may be a process of efficient functioning based on correct choices and actions. However, in the contemporary world which is increasingly dependent on large organisations, the most crucial situations are those which require organisational management. This implies decision and action in a context characterised by organised group or collective activity and the goals toward which the group effort is directed.

These objectives are pursued by managers in Japanese corporations who make decisions pertaining to the desired objectives and concerning relationships among resources: the people, money and machines, materials and methods which can be effectively deployed to attain those goals.
Now the economic and technological realities of the emerging Africa nations such as Nigeria and South Africa, for instance, are important given the circumstances under which industries have to operate and produce results. Any industry where the managers live in isolation from the realities of life and conduct their operations without reference to the economic and technological situation is, simply existing on a desert island. Thus the choice and use of the right management techniques are a matter of considerable importance, not only for the African nations and its people, but also in the long run for the survival, growth and prosperity of the industry itself.

**Background to Japan**

Japan is the world’s most successful manufacturing and trading economy, accounting for some 10 percent of world output and generating large balance of payments surpluses. Japan is a mountainous country with relatively few natural resources and variable climate. It suffers earthquakes and extremes of weather. Its culture has been influenced by Taoist, Confucian, Asian and Western ideas. It also tends towards Mercantilism. The Japanese regard people and their competence as the country’s key resource. The Japanese are homogeneous race, both linguistically and culturally.

In the areas of the national culture, the Japanese have a relatively High Power Distance; and High Uncertainty Avoidance. They are relatively highly Collectivist, although communitarianism is limited to membership and reference groups (the Japanese do not see themselves as ‘members of the public). Japan is the most masculine of all countries studied by Hofstede (1991). Japan is a monochronic and very high in context because it displays strong national and pragmatic characteristics, operating within traditionally holistic mental concepts that derive historically from Taoism, Budhism and Shintoism.

A feature of the Japanese is their particularism: an intense interest in detail and miniature (space is at premium in Japan). The Japanese adopt flexible attitudes to change; believing that society is evolutionary and subject to kaizen or continuing improvement, particularly as experience is accumulated, refined and handed on over time. They also subscribe to a synchronous view of time rather than the sequential approach of the West. The passage of time is associated with cycles, which in turn affects individuals, generations, entities and processes, and society generally. The present underpins the future, and lays its foundations. This synchronous view is best illustrated by long-term view taken towards technology. Development now will as progenitors yield generations of products in the future. At the same time, the development of technologies may be synchronised over time to achieve fusion: firstly, in the hybrid technologies for which Japan is famous; and, secondly, to produce newly synthesised technologies (such as those based on the properties of the laser (Hampden-Turner and Trompenaars, 1994) through the process of yugo-ka
The Japanese Business Culture and Management Approach

Business culture tends to be closed. The individual subordinates his interest to the wider purposes of membership and reference groups, which in turn, are expected to provide systems of mutual support, as in the times of economic recession. Groupings are tight-knit. It may be difficult to penetrate them without a sponsor who is already a member. There is an expectation that business relations will develop over a long time scale. Business trust and time are correlated; the Japanese want to know that the people with whom they are to do business are totally trustworthy and will be around for a long time. This business culture may appear very confusing to foreigners, and the Japanese may not say what they think for fear of offending or losing face. Hiding one’s feelings is considered a virtue in Japan.

The socio-cultural traits of the Japanese people have imbued in them a perception, a belief of behaviour at the workplace which is congenial for high productivity, fast industrialisation and innovation. In contrast to Western “individualism”, the “groupism” of the Japanese makes them more cooperative, contributive and supportive of others in the group and hence the organisation (Chang, 1982).

This has effectively been used by industry, on the shop floor and other parts of the organisation for all-round improvement and quality. Group-based techniques, such as “Quality Control”, “Quality Circles”, “Zero-defect”, Suggestion scheme”, etc, which was formulated first in the West, yielded much better results in Japan only because of their group cohesion, group ego and “familism”.

Two distinct sectors are visible in Japanese industry. A modern sector comprises large firms engaged in capital intensive production process and facilities. The productivity as well as the wages are high. The best talents are recruited on life time employment commitment and the pay is mostly given on age and seniority basis. The other sector is a traditional one comprising small firms often playing a supportive role. The features of this sector are low productivity, low wages, longer working hours and low profitability. The large firms sometimes help their trusted long-term employees to set up their own small firms either to reward their entrepreneurship or to cut down their own labour force which cannot be done during recession because of life-time employment commitment.

The Japanese government has complementary relationship with business and does not compete with private enterprise. The government facilitates industrial development by involving itself in the form of subsidies, supply of materials, adoption of technology, preferential licensing and low burden of taxation. Currently, the Japanese industrial policy is making a shift from heavy dependence on exports to reliance on domestic demand.

Recruitment to an organisation in Japan usually takes place at the entry level. Graduates from the best universities, such as Tokyo university (Tasie, 1997), for example, go to the best firms. All managerial appointments are made through promotion from within. This
familism makes job-hopping a degrading act; the work unit is based on human relations rather than on professional abilities. Work is organised around the group rather than around the skills of an individual who is assigned specific tasks. The lack of complete task description even to a group, encourages them to think expansively.

Japanese corporations train their employees and provide them with skills for their effective functioning and thereby building loyalty among them. Indoctrination courses are given to employees to nurture total commitment to the organisation. Individual guidance programmes are as important as group training programmes. The recruits receive instructions not only for his or her identified job but for all the jobs at the same level including the human resource function. The Japanese company unions combine rank and file employees as well as lower level supervisory and managerial personnel. Unions are basically autonomous and self-sufficient and the office and other administrative facilities are commonly provided by the company.

In Japanese society, the self is seen as part of a group. Expressing one’s individuality and independence are symptoms of immaturity and selfishness. Harmony or “Wa” becomes a primary concern among the Japanese to maintain efficiency and morale of the group. Consensus or Nemawashi should have been achieved before a decision is made.

Japan has been closed to the rest of the world for a long time. During this period, a sense of conformity and belonging was fostered among the people. As a result, the Japanese have established a very effective non-verbal communication system. Expressions such as Ishiu Denshin (tacit understanding) and Naa Naa Ni Yaru (doing business without a formal contract) are common features of Japanese society.

Characteristics such as loyalty to one’s boss, respecting a senior person, a boss’s obligation to his subordinate, and hard work are linked to the virtues of Confucianism. One can easily see the relationship between these virtues and the Nenko System with practices such as lifetime employment, seniority system, father-leadership, company family, and employee loyalty.

Groupism is the root of Japanese Management and the Nenko System is its flower. Since the system severely inhibits inter-firm mobility, intensive training and development becomes feasible. A large investment in employee who remains with a firm for over 30 years is very worthwhile. But the question of whether or not these management practices when transferred to other parts of the Asian countries will make a difference remain unanswered.

**Experts’ Observations**

A few unique points as identified by researchers in the area of the Japanese management styles are worthy of mention here. A group of experts (Pascale, et al, 1981) concluded that “the Japanese accepts ambiguity, uncertainty and imperfection as much more of a given organisational life”. This quality tremendously enhances their skills in dealing with people. They also find that “the Japanese see themselves as far more
interdependent. Thus, they are prepared to make far greater investments in people and in skills necessary to be effective in dealing with others”.

**Table 1.1 Characteristics of Top Management**

<table>
<thead>
<tr>
<th>Organic Type: Japan</th>
<th>System Type: The USA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Facilitator</td>
<td>Decision-maker</td>
</tr>
<tr>
<td>Social leader</td>
<td>Professional</td>
</tr>
<tr>
<td>Group strength</td>
<td>Individual initiative and creativity</td>
</tr>
<tr>
<td>Emphasis on human relations</td>
<td>Emphasis on functional relationship</td>
</tr>
<tr>
<td>Management by consensus</td>
<td>Management by objectives</td>
</tr>
<tr>
<td>Leader adapts to changes</td>
<td>System adapts to changes</td>
</tr>
</tbody>
</table>


Another expert group (Lee, et. al, 1987) concluded that Japanese management was based on a philosophy and organisational culture that emphasise:

- Hardwork for common goals;
- Consultative decision-making;
- A two-way communication system;
- Long-term planning;
- Sharing of overall objectives of the organisation by the employees at all levels;
- Establishing harmony and loyalty between workers and management, and
- Showing a high degree of concern for people and their values

An expert (Chang, 1982) also maintains that team spirit or group consciousness is very strong in Japan and that Japanese managers do not behave like individuals but as members of groups or subgroups. He concludes that “one of the paths to success in the organisation is to melt themselves into the group aura by becoming loyal company men”. The above Table is a comparison of the characteristics of the top management between Japan and the USA (Flynn et .al, 1982). A similar comparison between Japanese and North American companies on the value system has also been done by Crocker et.al, as presented below.
Table 1. Value System

<table>
<thead>
<tr>
<th>Factor</th>
<th>Japan</th>
<th>North America</th>
</tr>
</thead>
<tbody>
<tr>
<td>Key strategy</td>
<td>Paternalism</td>
<td>Entrepreneurship</td>
</tr>
<tr>
<td>People</td>
<td>Homogeneous</td>
<td>Heterogeneous</td>
</tr>
<tr>
<td>Basic concern</td>
<td>People</td>
<td>Tasks</td>
</tr>
<tr>
<td>Social system</td>
<td>Close and rigid</td>
<td>Open and fluid</td>
</tr>
<tr>
<td>Family</td>
<td>Extended</td>
<td>Nuclear</td>
</tr>
<tr>
<td>Education</td>
<td>Specialised</td>
<td>Liberal</td>
</tr>
<tr>
<td>Employee feeling about firm</td>
<td>Oneness with firm</td>
<td>A place to earn money</td>
</tr>
</tbody>
</table>


On the foundation of the aforementioned traits of Japanese, a few more tangible things are also noticed which are widely talked about in this context. They are:

Just-in-Time system

**Quality Circles**

*Ringi* system of Decision Making

*Kaizen* concept of continuous improvement, etc

But these tools in the absence of the requisite group cohesion, organisational loyalty and flexibility in attitudes, may at best serve only a window dressing purpose. A superficial arrangement will by no way change the spirit of a management. Giving credit to these systems for economic progress of Japan will only misguide us.

**African Approach**

The forthcoming changes in the business environment of African countries like South Africa, Ghana, Nigeria, Zimbabwe, and many others are evident. The emerging social politico-legal standards have increased the expectations from business. Business today is required to respond to the needs of its employees, the customers and the society itself in which it operates.

Besides, African countries, particularly those wanting to industrialise face the problem of major adjustments in their economic system so that they could recover from serious entrepreneurial crises and avoid possible collapse. The continuous economic reforms starting from many circles brought Africa to the era of liberalisation and globalisation. These alone have put an unprecedented pressure for managerial efficiency in business.
units for the upgrading of quality and cost effectiveness. The ultimate aim of management will be to provide the customers with value for money as desired and deserved by them in order to ensure its own survival in the wake of global competition in the world market.

The crucial factors in this challenging job will be the quality assurance, cost effectiveness, consumer satisfaction and ethical standards for good image building. In order to achieve these end results, African businesses need the quality in its managerial performance itself, management of change, creating a favourable work and African culture, team spirit and organisational loyalty as well as other relevant conditions.

Meeting this great challenge successfully is the key to survival. Do countries like Nigeria, Ghana, Zimbabwe and Kenya have enough potential to do all this or are they handicapped by some of their in-built weaknesses that are the real issues before us for serious consideration?

Africa in general do not have a dearth of capable people. Manpower resource is quite large and comprises people with vision, creativity, modern outlook and professional training. The social and religious values are also deep-rooted in the population of Africa, thereby making it capable of becoming a cohesive group with loyalty and respect for elders. This pluralistic orientation of life has rewarded these countries suitably in the West where people are mostly individualistic.

But, apart from these, do we also have a work culture that is conducive to high performance and can we bring up a well motivated team of individuals who believe in results and are prepared to take up challenges in the accomplishment of their tasks? Any structure or strategy will fail to show results without such a workforce in business. Instead of having team spirit and innovation in the work culture, there are conflicts and unhealthy politics in organisations. Management tools are used by us as armours to defend ourselves and as weapons to offend others. A constructive system turns into a futile confrontation with mutual grips and hard feelings but no solution of the problem. Any organisation ridden with a bitter political manoeuvring generates opportunism, exploitation, favouritism, yes-manship, pulling others down, persecution and many more.

Most firms run by the people of this region, complain of having more crises day by day. Consequently, reactive and passive nature managers tend to concentrate on them. They live too much in the present and neglecting the future. When this becomes a way of life, things are attended to only when they become urgent and alarming. Crises put some of the conscientious managers under tremendous stress and tension, but for others they lose significance, causing a decline in their commitment to the organisation.

The problem in the managerial system of Nigeria, Ghana, Zimbabwe, Kenya, to mention but few, is so deep rooted and widespread that short-cuts or quikies would probably not work. Although these countries are not completely homogeneous in terms of religion, they do share certain characteristics in terms of culture. Reforms should be started from
the foundations per se. An internal introspection for a few basics for continuous refinement and improvement is the need of the time.

Efficiently created corporate work culture that may generate among workers a spirit of continuing introspection, innovation and experimentation is the need of the hour. Managerial values should focus more on implementation rather than on designs, and achievement should be given more importance than effort. Freedom for entrepreneurial actions should prevail all over the organisation. Actions and resulting achievements may become a matter of pride for the African people in general.

To have a kind of culture in the organisation, managers have to be more pragmatic, open, innovative, entrepreneurial and risk-taking. The people have to be more tolerant and patient to listen to hired foreign professionals, see others doing, welcome positive as well as negative results of others’ actions but at no cost of creativity, innovation, experimentation and entrepreneurship being halted.

Another major element of professionalism which fails to get its proper due in management practice is the MBO (management by objective). The internal balance and harmony in the set of objectives is usually lacking, causing confusion and diversion in effort. Making it a driving force for the entire organisation requires developing in each and every member a consumer orientation. Employers and employees both have to dedicate their efforts to the consumer satisfaction. This may become a very effective means of causing congruence in individual and organisational objectives.

Can the Japanese Management Styles be applicable to Africa?

We have witnessed both the Japanese and American philosophies towards human factor as homogeneous and heterogeneous respectively – which have been claimed to contribute towards improved productivity, excellence, creating difference, creating a niche, increasing competitiveness; all of these are targeted at producing the competitive edge over competitors either to survive or to be ahead of them. Other Asian model considers respect for individuals as the most important ingredient in its own right for successful, high quality and excellent management that is the human factor in the form of customer, local inhabitants and/or personnel who actually perform all the tasks in the whole organisation. Indeed, if the human factor is absent, there can be most excellent organisation in terms of buildings, structures, charts, rules, regulations, systems, support and facilities. Yet nothing will actually move, much less function in a coherent, well organised manner. To paraphrase Yong, “training will neither make a fish fly nor a bird swim; but training will certainly help a fish to swim faster and a bird fly higher” (Yong,1996). Alhabshi’s argument support the above statement when he said, “You can bring the horse to water but you cannot force it to drink” (Alhabshi, 1994). On the other hand, in the absence of the rest, the human element can still move something, as in the case of establishments which are about to be organised or started.
In the beginning, the Japanese success was termed as ideal and hence separate from the rest of Asia due to their commitment to quality and productivity ascribable to outstanding investments in Research and Development. But, lately, many scholars turned down the idea and attributed their success instead to values, work ethics, work culture, and corporate values. Tersely, they are described as successful based on the appropriate blending of technological education and knowledge advancement in the close and rigid Japanese cultural mould.

The contributions of contemporary management in Japan and Western countries including the USA are so numerous; many of the conclusions were derived from empirical studies that were carried out within a certain cultural framework. These conclusions are not universally practicable and are more applicable to the societies in which the experiments were carried out. The differences in the social set-up induce variations in the managerial skills, strategies, systems and structures. Moreover, some of the Western managerial concepts are based on a certain premise of thought that is alien to the state of mind of some business managers in other Asian countries. The strategies, structures, and systems that are strictly contradictory to the revealed knowledge are, however, few and they are equally controversial among the Western scholarship. Hence the strategies adopted by the Japanese will provide more additions to the field of existing knowledge of management theories and practice.

It must be appreciated that the Japanese style of business and management is deeply rooted in traditional Japanese society and culture, and is considerably influenced by their values and attitudes. Some key contextual factors which have paved the way for the success of Japanese style management are authoritarian society, a communal outlook, factions and cliques, copying and perfecting technology, future orientation and business-government relationships, decision-making by consensus, active role of middle and top management, lifetime employment, seniority-based wage system, training by rotation and enterprise unions.

Many observers of Japanese management practices have taken the view that these practices are desirable to be applied in other countries and cultures. Consequently, little attention has been paid to the costs which the system inflicts on society, and workers in particular. These costs can be substantial in terms of loss of individual freedom, a rigid social structure and sacrifice of other values which individuals and groups may cherish. Another little known fact, is that the benevolence of the Japanese management system is not bestowed on a majority of workers, but is limited to a small minority (Iwata, 1982). Approximately 35 per cent of the total workforce enjoys the privileges of lifetime employment in Japan. Women are almost never granted this privilege, and therefore occupy the lowest paid jobs in industry (Yakabe, 1974).

Despite the above limitations of Japanese-style management, William Ouchi (1978) has argued that the theoretical basis of the Japanese management system is the existence of industrial clans which have developed by a slow organic process within the Japanese society. Drawing on the work of the classic French sociologist, Emile Durkheim, Ouchi suggests that industrial organisations in the big business sector of the Japanese economy
can be described as clans in the sense that they provide employees with a feeling of social cohesion and stability and a sense of belonging, meaning and direction in life. It is these characteristics which have been lost in western society which is suffering, in Durkheim’s terms, from a problem of normlessness, with the decline of the family and other traditional social institutions and values. In the case of Japan, the values underlying the industrial clans have developed, according to Ouchi, as a result of cultural imperatives.

**Conclusions and Recommendations**

From the foregoing discussion, the author recommends the following basic elements in management model of African countries, as these are *sine qua non* for contemporary world of African managers facing the present day problems.

**Table 1.3 Elements in the Management Approach of African Countries: Nigeria, Kenya, Ghana, and Zimbabwe**

<table>
<thead>
<tr>
<th>1. Respect for individuals as an organisational philosophy</th>
</tr>
</thead>
<tbody>
<tr>
<td>Its dimensions will be:</td>
</tr>
<tr>
<td>(a) Low concern for the employees</td>
</tr>
<tr>
<td>(b) Low concern for customers</td>
</tr>
<tr>
<td>(c) Low concern for the local inhabitants</td>
</tr>
<tr>
<td>(d) Low concern for society and ethics</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>2. Organisational culture as an infrastructure for efficiency.</th>
</tr>
</thead>
<tbody>
<tr>
<td>This includes, in particular:</td>
</tr>
<tr>
<td>(a) Super-ordinate goals - that gives direction to the effort</td>
</tr>
<tr>
<td>(b) Zeal - that supplies energy and fervour</td>
</tr>
<tr>
<td>(c) Action Bias - that discourages entrepreneurship and implementation</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>3. Leadership - Creating impact of people running the business</th>
</tr>
</thead>
<tbody>
<tr>
<td>4. Professional arrangements in the form of tools of scientific management, viz.</td>
</tr>
<tr>
<td>(a) Strategy - to plan the course of action and resource allocation</td>
</tr>
<tr>
<td>(b) Structure – to divide and distribute the task of personnel</td>
</tr>
<tr>
<td>(c) Skills – to create distinct capabilities in key personnel</td>
</tr>
<tr>
<td>(d) Systems – to proceduralise reports and routinise processes.</td>
</tr>
</tbody>
</table>

Source: *Author’s observations through residential experience, traveling and working in Africa.*

It may be noted that the basic philosophy of management in respect of concern for human beings does not figure in the previous models, but it has specially been placed in African model in order to cleanup the internal as well as external environment of the organisations and build an atmosphere of mutual trust, team spirit and group consciousness in the firm-the human interface.

The managerial tools with their roots in the culture and subcultures of African nations have been included for their importance and priority to its system. The leadership that
has to play a vital role in implanting a healthy culture within organisational premises has then been positioned. No discipline and order can be maintained without providing an acceptable and exemplary leadership. But an effective leadership is expected to emerge easily in a fairly healthy work culture. The present state of organisational climate in industrialising African countries is hardly capable of supplying us with great and committed leaders in sufficient numbers.

Incorporation of the elements of professionalism which refer to African managerial styles completes our list. Anybody who can manage well the strategy, structure, skills and systems in a given social set-up may be qualified enough to be called a professional manager. Anachronistic management methods such as those demonstrated above should be redefined to incorporate the more modern and scientific ones. The implementation of this step, it is anticipated, could possibly improve efficiency and update managerial decision-making process.

The emergence of Japan as a global economic power dramatically illustrates the nature of global economic change due to some of its management styles. Best known for the prowess it developed during the 1970s and 1980s in steel, electronics, and automobile production, (Post et.al, 1996), by the year 2008 and beyond, no continent including African business leaders could afford to ignore Japan as a leading competitor in major sectors of the global economy. If other African countries, such as Nigeria, South Africa, Kenya, Ghana and Zimbabwe are to improve efficiency and quality in their organisations, they must, to a significant extent, follow a success story of the Japanese management styles. The issue of cultural impediments to organisational change like unemotionality, conservatism, depersonalisation of problems, subordination, isolationism, and antipathy (Blunt, 1988) must be carefully and constructively addressed. South Korea and Taiwan are two newly industrialised countries, which have shown rapid growth in productivity and per capita income since the 1950s. Most of their business culture, organisation, working practices, and relations as well as management styles are, to some extent, similar to that of the Japanese. Singapore, one of the fast growing economy in South East Asia has shown a great interest in the Japanese way of managing, particularly in the area of human resources.

If African countries are to improve their management styles efficiently and effectively, they must apply, but with caution, the Japanese styles of management. However, to do this, African countries, particularly Nigeria and others, must put in place certain fundamental infrastructural facilities such as constant supply of electricity, water, good roads and dependable health institutions.

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Influence of Organizational Commitment and Islamic Work Ethics on Attitudes towards Organizational Change

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Abstract: Organizations in the Kingdom of Saudi Arabia, privates and publics alike, are continually witnessing programmes of change. Considering the fact that successful change effort depends, in part to the employees’ behavior, this study was prompted to examine two of the possible factors, organizational commitment and Islamic work ethics, which can influence attitudes towards organizational change of Saudi employees. A sample of 220 employees from different organizations in the Eastern Province of Saudi Arabia is used. The results of correlation analysis found that both organizational commitment and Islamic work ethics have positive influence on the Saudi employees’ attitudes towards organizational change.

The implications of these findings, among others, were discussed. The limitations of the study were highlighted and areas where further researches might be needed were also suggested.

Keywords: Organizational commitment, Islamic work ethics, attitudes towards organizational change, and Saudi employees.

1.0 Introduction

To cope with increased competitive pressure, globalization and demand for efficiency, (Ugboro, 2006), among others, many organizations have to continually embark on programmes of organizational change. Organizational change is one of the most important features of this era (Yousef, 2000a).

As Peter Drucker mentioned, change is the norm in the period of upheavals, such as the one we are living in now. Organizations must run fast to keep up with changes taking place all around them. They must modify themselves not just from time to time, but every time.

Hence, today’s organizations must poise themselves to change, not only to prosper but merely to survive in the world of increased competition. To the organizations in the kingdom of Saudi Arabia in particular, the need for change is more urgent now ever than before, especially with the Kingdom having obtained membership in the World Trade Organization (WTO) which unveils the hitherto protection from competition enjoyed by many local companies.

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contributed greatly in the first draft of this study. Dr. Youssef was instrumental in the analysis part of this project.

The success of such organizational change programmes, however, depends, in part, on the behaviors of the people in the organizations and their work attitudes (Ugboro, 2006). Human beings, hence, are the most important determinants of the success or failure of the organizational change process (Yousef, 2000a).

Thus, to ripe the benefits of the change efforts, organizations need to uncover and manage those factors that influence individuals’ attitudes toward change. One factor which is believed to affect individuals’ attitudes toward change is their commitment to their organization. This is for that fact that those committed to their organizations are more likely to embrace change, especially if they perceived such change beneficial to their organizations (Yousef, 2000a). Similarly, work ethic, Islamic work ethic in the case of Saudi organizations, is another factor that might influence individuals’ attitudes towards organizational change.

However, the role of both organizational commitment and work ethics (Islamic work ethic) on influencing attitudes toward organizational change has received inadequate attention in the literature. Furthermore, our literature search revealed that, to date, no such study was undertaken in Saudi Arabia. Hence, the purpose of this study is to examine the interaction between individual’s commitment to their organizations, individuals’ Islamic work ethics and their attitudes toward change for Saudi employees.

1.1 Objectives of the Study

This study seeks to examine the importance of two factors in the attitude towards change. These factors are organizational commitment and Islamic work ethic. Thus, the overall study research question is: Do organizational commitment and Islamic work ethic influence the attitudes towards organizational change in Saudi market?

Specifically, the study aims at:
1. Examining the influence of organizational commitment on attitudes towards organizational change
2. Examining the influence of Islamic work ethic on the attitudes towards organizational change

1.2 Significance of the Study

Attitudes towards change and its relation with employees’ commitment and Islamic work ethics have not received adequate attention in the Saudi market. Thus, this study will be of considerable importance, owing to the dearth of such empirical studies in Saudi Arabia.

In addition, Saudi society (Saudi organizations) is faced with a lot of challenges to modernize it self. Therefore, it is expected that this study will help the mangers in the
Saudi market to understand some factors which affect Saudi employees’ attitudes towards organizational change

Moreover, the study result will provide the change leaders valuable information for successful planning and implementing organizational change through creating a work environment in which employees accept rather than resist change. Therefore, the study is of considerable value to practitioners and scholars alike.

2.0 Literature Review and Conceptual Framework

2.1 Organizational Change

Owing to the fluid nature of the business environment today, organizations are confronting continuous and unparalleled changes ever than before (Madsen, et. al., 2005). They are constantly embarking on several programmes of change (Vakola and Nikolaou, 2005). These changes are commonly driven by technology (Hsich & Tsai, 2005; Parsons, et.al., 1991) like computerization and e-commerce that have created a quantum leap in data communication, work processes and the new way of doing business (Abdul Rashid et. al., 2004). Another driven force is the challenge of the impending move toward globalization and liberalization of markets, among others (Abdul Rashid et. al., 2004).

Organizational change can be referred to as a process of altering people's actions, reactions, and interactions to move the organization’s existing state to some future desired state (McNabb and Sepic, 1995). In particular, organizational change encompasses broad categories of changes that include structural changes such as the merger of organizations and organizational subunits, the establishment of a new organizational subunit, or the delayering, downscoping, and downsizing of an organization (Lines, 2005); system changes, such as the implementation of balanced score card systems or a new reward system; and process changes, such as the introduction of new work processes (Eby, et. al., 2000), changes in formal job descriptions, or mechanization of processes performed by humans.

A report by the American Management Association maintained that about 84 percent of American companies were in the process of at least one major change initiative and 46 percent confirmed that they had multiple change programmes in progress (Peak, 1996). Moreover, organizational change initiatives have been considerably increasing the world over as organizations have struggled through economic downturns, employee shortages, technological advancements, downsizing, mergers, and general instability; and for others, ongoing change has been essential because of rapid growth, new business ventures, exciting opportunities, innovative inventions, and novel leadership and management approaches (Madsen, et. al., 2005).

Change is hence a real challenge that many organizations have to confront (Abdul Rashid et. al., 2004) and whatever the reason for the change, embracing constant and continuous change is now a matter of necessity rather than choice for business success (Rowden, 2001).
It is worth noting, however, that several change efforts failed over the years and nearly 40 percent of such failure rates (Cartwright and Cooper, 1992) are attributed to the employee resistance to change (Chawla and Kelloway, 2004). Among the possible reasons why employees resist changes is that while some employees perceive change may bring satisfaction, joy and advantages, for others the same change may bring pain, stress and inconveniences (Abdul Rashid et. al., 2004).

Failed change efforts have drastic effect on organizations. Some of the adverse effects included higher turnover rates, lower efficiency, and decreased organizational commitment (Goldstein, 1989; Kotter and Schlesinger, 1979). It is often suggested that it may be easier, at times, and less costly to start a completely new organization than it is to change the culture of an existing one (Madsen, et. al, 2006).

Therefore, managing change effectively is a critical challenge facing organizations today (Madsen, et. al., 2006) and history proves that organizations that continually and consistently rise to meet that challenge are those that are most successful (Madsen, et. al., 2006). Thus, it becomes imperative for an organization to promote the readiness for change of its employees (Madsen, et. al., 2006) or rather its employees' attitude to change.

The importance of employees’ attitude to organizational change, as expressed by a willingness to exert effort on behalf of the change (Armenakis et al., 1993) can not be overemphasized if an organization is to realize the expected benefits from the change initiative.

Attitude towards an organizational change is regarded as a person’s overall psychological evaluation of the change with some degree of favor or disfavor (Petty and Wegener, 1998; Eagly and Chaiken, 1998). Attitudes toward change in general consist of a person’s cognitions about change, affective reactions to change, and behavioral tendency toward change (Piderit, 2000) and each of the type of attitude toward change may induce a person to support or not changes occurring in an organizational setting (Dunham, 1984).

Favorable or positive attitudes toward change are expected to produce behaviors that are focused, persistent, and effortful in an organizational attempt to support and facilitate the implementation of the change (Lines, 2005). Such pro-change behaviors may include extra role efforts to solve unforeseen problems and other organizational citizenship behaviors (Organ, 1990).

Hence, the necessary initial condition for successful planned change, as research has posited, is the employees’ positive attitudes toward a change (Miller, et. al, 1994). Thus, there is a need to understand those factors that can impact, favorably, attitude toward organizational change. Literature search indicates few studies have investigated the relationship between attitudes toward organizational change and organizational outcome, among which included organizational commitment and work ethic (Abdul Rashid et. al., 2004)
2.2 Organizational Commitment and Attitude towards Organizational Change

Commitment has been a focus of research attentions (Wright & Bonnett, 2002). However, no consensus in the literature exists over its meaning (Morris et al., 1993). One view about organizational commitment is that it is a relative strength of an individual’s identification with and involvement in a particular organization (Mowday et. al., 1982). Organizational commitment can equally be seen as a psychological state that characterizes an employee’s relationship with the organization and reduces the likelihood that he/she will leave the organization (Allen and Meyer, 2000).

Literature has shown that organizational commitment is not only an attitude, but also a behavior (Nijhof, 1998). Attitudinal approach to commitment focuses on the process by which individuals think about their relationship with an object. It centers on the extent to which their goals are harmonious with those of an organization (Mowday et al., 1982). In the behavioral approach on the other hand, individuals are viewed as becoming committed to a particular course of action (Ugboro, 2006).

In some studies, commitment is considered as a unidimensional concept (LaÈmsaÈ and Takala, 2000). However, literature research by Allen and Meyer (1991) and substantiated by Dunham, et. al. (1994), among other findings, identified three types of organizational commitment, which comprised of affective, continuance and normative commitment. But, a study in a Middle Eastern work environment, Jordan, found that only the affective and continuance were prevalent in the Jordanian work environment (Suliman, et. al. 2000).

Affective commitment is an employee’s emotional attachment to, identification with, and involvement in the organization and its goals (O’Reily & Chatman, 1986). While continuance commitment is regarded to as the willingness to remain in an organization because of personal investment in the form of nontransferable investments such as close working relationships with coworkers, retirement investments and career investments, acquired job skills which are unique to a particular organization, years of employment in a particular organization, involvement in the community in which the employer is located, and other benefits that could make it too costly for one to leave and seek employment elsewhere; normative commitment on the other hand is induced by a feeling of obligation to remain with an organization, owing to generalized value of loyalty and duty (Wiener, 1982).

Common to all the three types of commitments is the view that commitment is a psychological state that characterizes the employee’s relationship with the organization, and has implication for the decision to continue or discontinue membership in the organization (Ugboro, 2006).

It should be noted, moreover, that the extend of employees’ commitment to their organizations may vary with respect to their personal characteristics and the most frequently studied demographics in relation to commitment are age and level of education (Morris et al., 1993). The level of commitment is assumed to follow a U shape pattern.
with age (Clark et al., 1996). It is maintained that younger employees are more committed than older ones, because they are highly motivated to start a career and able to cope with change, whereas older employees are less committed because they are often disappointed (Morris et al., 1993). On the other hand, older employees, who have worked many years for the organization, do have a strong attachment to the organization (Morris et al., 1993).

With respect to education, Gallie and White (1993) found that higher educated employees have a higher task commitment. However, other studies found a negative correlation, though small in magnitude, between level of education and commitment (Mowday et al., 1982).

Different levels of commitment were reported by different studies. A study in a sister Gulf country, UAE, found that employees were neither commitment nor uncommitted to their respective organizations (Yousef, 2000a). The study’s finding of low overall mean of organizational commitment is consistent with the findings of other studies carried out in other Arab Gulf states (Al-Meer, 1989; Ben-Baker et al., 1994; Bhuian et al., 1996). Such a low pattern of organizational commitment has been attributed to the fact that expatriate workers work for relatively high salaries and benefits, and therefore they tend not to hesitate to leave their organization for better jobs elsewhere (Bhuian et al., 1996).

Similarly, a finding of a separate study in the western setting indicated that a negative correlation exist between employees’ competence and affective commitment, indicating that highly competent survivors have a high propensity to leave an organization subsequent to restructuring and downsizing (Ugboro, 2006).

A number of studies, though widely in the western settings, have investigated the impact of organizational commitment on attitudes toward organizational change (Hui and Lee, 2000; Judge, et. al., 1999; Yousef, 2000a.). Organizational commitment is regarded as the second most important determinant, after union membership, of attitudes toward organizational change (Iverson, 1996).

A common wisdom is that a person committed to an organization is more likely to accept its goals and values; willing to exert effort on its behalf (Mowday, et. al. 1979); and therefore more likely to accept its changes provided such changes are perceived as beneficial to the organization and has no potential to alter the basic values and goals of the organization (Yousef, 2000a).

Empirically, mixed findings were reported on the effect of organizational commitment on organizational change. A number of studies indicated significant positive relationships between organizational commitment and organizational change (Madsen, et. al., 2005). A study in Netherlands that targeted over 4,000 human resource managers found greater willingness to change as one of the effects of commitment (Nijhof, et. al. 1998). Additionally, another study found that a significant effect exist on teachers’ commitment to change in Hong Kong (Yu, et. al., 2002). A study by Lau and Woodman (1995) also
discovered that organizational commitment had significant, direct effects on change schema.

However, a study by (Yousef, 2000a) found a weak relationship between organizational commitment and attitudes toward organizational change. Conversely, with respect to the specific dimensions of both organizational commitment and organization change, the study indicated that only affective commitment has positive influence on affective and behavioral attitudes to change, but not on cognitive attitude to change. A related study by the same author conducted in the same setting substantiated the finding that it is only certain, but not all dimensions of organizational commitment influence certain dimensions of attitudes toward organizational change (Yousef, D. 2000b) and continuance commitment was found to negatively influence cognitive attitudes toward change, (Yousef, 2000b).

As for the mediating role of commitment to organizational change, Vakola and Nikolaou (2005) found that organizational commitment plays no role in moderating the relationship between occupational stress and attitudes to change. However, continuance commitment was empirically supported to mediate the influences of the Islamic work ethics on the behavioral tendency dimension of attitudes toward change (Yousef, 2000a).

Essentially, it could be proposed that those who are more committed to their organizations are more likely to embrace change than those who are less committed to their organizations. Hence, the following hypothesis was formulated for testing:

H1: The organizational commitment influences the attitudes toward organizational change positively.

2.3 Islamic Work Ethic and Attitude towards Organizational Change

A belief about work ethic is believed to differ across time and societies (Ali and Al-Kazemi, 2007). However, most of the studies on attitudes toward work ethics were in the Western countries.

The concept has started been examined in non-western civilizations in recent years. In line with this, Furnham (1991) and Furnham and Muhuldeen (1984) studied work ethic and found evidence that not only do elements of the Protestant work ethic (PWE) exist in nonwestern countries, but also that subjects from these nations score high on PWE.

However, PWE measures were criticized for their inadequate validity (Furnham, 1990), when used in a settings other than original setting from where it was originated. Hence, for the fact that these measures were developed, tested and extensively used in the West and little is known about their reliability and validity in the Arabian Gulf region (Ikhlas, 1997) in particular, effort has been made to come with a peculiar measurement that could accurately measures the subjects perception of work ethic in this region and other
countries that subscribe to the same values. One of such instruments is Islamic Work Ethic (IWE) measures.

Islamic work ethic stands not for life denial but for life fulfillment and holds both business motives and economic development (Ali, 1992; Congleton, 1991; Furnham, 1991) in the highest regard. It is built upon the pillars of effort, competition, transparency, and morally responsible conduct and these pillars are meant to inspire confidence in the market and reinforce social contract, ethical understanding, and motivates market actors to focus on meeting their primary business responsibilities (Ali, 2005).

A number of studies examined and found that work ethics, defined as the Protestant ethics, have significant relationships with organizational outcomes (Putti et al., 1989; Oliver 1990; Saks et. al. 1996).

Though both the Islamic work ethic (IWE) and the Protestant work ethic (PWE) place considerable emphasis on hard work, commitment and dedication to work, work creativity, avoidance of unethical methods of wealth accumulation, cooperation and competitiveness at the workplace (Yousef., 2000a) but their relationships with organizational outcomes might be different owing to the differences among them (Yousef, 2000a)

Specifically, the concept of the PWE was advanced by Weber (1958) who proposed a causal relationship between the Protestant ethic and the development of capitalism in the western society. One the other hand, the concept of the Islamic Work Ethic (IWE) has its origin in the Quran and the sayings and practice of Prophet Mohammed (Yousef, 2000a). It perceived hard work as a virtue; creative work as a source of happiness and accomplishment, and those who work hard are more likely to get ahead in life among others (Yousef, 2000a).

Owing to the fact that Islam is one of the most influential factors that shapes Muslims’ value systems (Ali, 1986), Islamic work ethic deserves a serious inquiry (Nasr, 1984), especially in Saudi Arabia which is popularly seen as the cradle of Islam.

Most of the literatures on the Islamic work ethics had been descriptive and general in nature until Ali (1988) developed a qualitative measurement for it. The scale which has 17 items is uni-dimensional as PWE and was found to be reliable (Ali, 1992; Yousef, 2000a, 2001). The validity and reliability of IWE scale were originally tested using 117 managers in Saudi Arabia.

One of the few studies on IWE, empirically, conducted in UEA found that though overall mean on Islamic work ethic is high for three cultural groups, but Arab expatriates and UAE nationals scored higher on the Islamic work ethic scale than Asian expatriates (Yousef, 2000c). This finding was corroborated by Ali (1992) and...
Ali and Azim (1994) who also found that Arab managers scored high on the Islamic work ethic. However, in another Gulf country, Kuwait, expatriates were found to have higher attitude on IWE than Kuwaiti managers and men scored relatively higher than women on IWE (Ali, and Al-Kazemi, 2007).

Relationship of IWE with organizational outcome enjoyed little attention in the literature. One of the few studies in the area found a moderate relationship between the Islamic work ethic and attitudes toward organizational change (Yousef, 2000a). The study found that IWE directly and positively influences various dimensions of attitudes toward organizational change.

Hence, it can be hypothesized that:

H2: The Islamic work ethics influence the attitudes toward organizational change positively.

Based on the study objectives which were substantiated by the reviewed literature, the hypotheses of the study were developed. These hypotheses are translated into a theoretical model presumes that attitude toward organizational changes is positively influenced by Islamic work ethics and organizational commitment.

3.0 Methodology

3.1 Data Collection and sample

Researchers are confronted with several challenges when undertaking surveys in Saudi Arabia, more prominently in designing sampling procedures as well as in undertaking primary data-collection (Sohail, 2005).

A field survey was proposed for this study and questionnaires were directed at employees occupying different organizational levels using a convenient sampling. To ensure representativeness, the survey instruments were distributed to employees of organizations of different sizes, activities and ownership in the Eastern Province of Saudi Arabia. Though the study covers only one of the major provinces in the country, but the cosmopolitan nature of the region may be representative of all other regions in the kingdom.
A total of 600 surveys were hand-delivered using drop-off and pick-up methods. Only 226 questionnaires were returned, representing 37.67% response rate which is considered favorable compares to response rates for other recent studies in the Kingdom (Sohail, 2005). Of the returned questionnaires, only 220 questionnaires were usable.

3.2 Measures

All the constructs of the study were measured from items adapted from previous studies to improve construct validity and comparability.

All the 24 items adapted from Meyer and Allen’s (1991) instrument was considered in measuring organizational commitment. The decision to this instrument instead of Mowday et al. (1979) scale is because the latter has been recently criticized for lack of homogeneity (Benkhoff, 1997b). From the result of the factor analysis, scores on the nine items (see table 2) were averaged to yield a measure of organizational commitment for the study.

Islamic work ethic was measured using a short version of Ali’s (1988) instrument, which has been previously tested using a sample of 117 managers in Saudi Arabia. The 17 items of the scale were initially considered and based on the result of factor analysis as shown in table two, ten items were eventually used in measuring the construct.

Attitude toward organizational change was measured using Dunham et al.’s (1989) 18-item instrument and only 6 items were eventually considered appropriate in this study based on the outcome of factor analysis. Each of the three scales were measured on a seven-point Likert scale ranging from 1 (strongly disagree) to 7 (strongly agree).

3.3 Statistical Analysis

In this section, the issues of reliability and validity are discussed. The reliability of the study constructs is first discussed followed by the content validity and then construct validity.

Reliability

Coefficient alpha analysis was used to determine the extend to which items making up each measure were homogenous and loaded on the same scale (Allen and Yen, 1979). Cronbach alpha has been suggested to be the preferable measure of index reliability. The scales used in this study were checked for their internal consistency. While there was no theoretically acceptable value for the reliability measure, Nunnally (1978) had suggested alphas of 0.70 as an acceptable value for scale development.

Validity

Generally speaking, validity refers to the degree to which a construct measures the variable under investigation.

A. Content Validity
This validity determined the adequacy of the sample characteristics to describe the measure (Nunnally, 1978). The questionnaire used in this study built upon existing research where it was found to be valid. The study questionnaire also benefited from the scrutiny, and suggestion of the research supervisor.

**B. Construct Validity**

One widely used technique to assess the construct validity of an instrument is factor analysis (Kerlinger, 1973). Various items that represent each dimension were analyzed to see if they are properly assigned to the appropriated scale (Carmines and Zeller, 1980). Since the items in each scale had been analyzed above for content validity, the factor analysis provided a test of construct validity.

**4.0 Data Analysis and Result**

This part of the study reports the profile of the respondents and presents the tests to evaluate the validity and reliability of the scales used for the data collected. The remainder of the section then presents the testing for the two hypotheses.

**4.1 Profile of the Respondents**

The demographic profile of the respondents is presented in Table I. It can be inferred from this table that over half of the respondents (58.5 percent) were aged 26-35 years. The smallest groups of respondents were those aged less than 26 (10.6 percent) and those aged over 45 (10.1 percent). About 36.9 percent have less than six years work experience. While almost equal number (34.6 percent) has over 10 years experience, only 28.6 percent have 6-10 year work experience. In terms of education, most of the respondents (68.4 percent) have university degree. While only 2% hold top management position, 47.9 percent occupy no managerial position.

With respect to the subjects’ work organizations, about three fourth of the respondents (75.1 percent) work in large organizations with over 1000 employees and 84.3 percent work in organizations which have been in business for over 10 years. Fifty-one percent of the respondents work in service organizations and 43.7 percent and 37.2 percent work in private sector and public sector respectively.

**4.2 Reliability and Validity of Variables**

Several major steps were carried out to enhance the reliability and validity of the variables. Factor analysis was first made for this purpose. Reliability was then utilized to check the internal consistency of the scales involved in the study.

**4.3 Construct Validity**

Factor analysis with varimax rotation was utilized to analyze the questionnaire variables of interest. The factor analysis detected relevant factors for (1) organizational commitment (2) Islamic work ethics, and (3) attitudes towards organizational change. Two criteria were used to identify factor scales. First, all scale items that loaded less than 0.50 were removed. Second, the construct would be represented by the factor that has the highest eigenvalue. Significant results of the factor analysis were depicted in table 2.
Table 1: Respondent’s Profile

<table>
<thead>
<tr>
<th>Variable</th>
<th>Valid responses</th>
<th>Percent</th>
<th>Cumulative Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Age</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>25 years or less</td>
<td>23</td>
<td>10.6%</td>
<td>10.6%</td>
</tr>
<tr>
<td>26-35 years</td>
<td>127</td>
<td>58.5%</td>
<td>69.1%</td>
</tr>
<tr>
<td>36-45 years</td>
<td>45</td>
<td>20.7%</td>
<td>89.9%</td>
</tr>
<tr>
<td>Over 45</td>
<td>22</td>
<td>10.1%</td>
<td>100.0%</td>
</tr>
<tr>
<td><strong>Experience</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5 Years or less</td>
<td>80</td>
<td>36.9%</td>
<td>36.9%</td>
</tr>
<tr>
<td>6-10 Years</td>
<td>62</td>
<td>28.6%</td>
<td>65.4%</td>
</tr>
<tr>
<td>Over 10 years</td>
<td>75</td>
<td>34.6%</td>
<td>100.0%</td>
</tr>
<tr>
<td><strong>Educational level</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less than University</td>
<td>33</td>
<td>15.6%</td>
<td>15.6%</td>
</tr>
<tr>
<td>University degree</td>
<td>145</td>
<td>68.4%</td>
<td>84.0%</td>
</tr>
<tr>
<td>Postgraduate degree</td>
<td>34</td>
<td>16.0%</td>
<td>100.0%</td>
</tr>
<tr>
<td><strong>Organizational size (employees)</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less than 100</td>
<td>9</td>
<td>4.1%</td>
<td>4.1%</td>
</tr>
<tr>
<td>100 - 500</td>
<td>21</td>
<td>9.7%</td>
<td>13.8%</td>
</tr>
<tr>
<td>501 – 1,000</td>
<td>24</td>
<td>11.1%</td>
<td>24.9%</td>
</tr>
<tr>
<td>More than 1,000</td>
<td>163</td>
<td>75.1%</td>
<td>100.0%</td>
</tr>
<tr>
<td><strong>Occupational level</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Top management</td>
<td>5</td>
<td>2.3%</td>
<td>2.3%</td>
</tr>
<tr>
<td>Middle management</td>
<td>46</td>
<td>21.2%</td>
<td>23.5%</td>
</tr>
<tr>
<td>Supervisory employee</td>
<td>62</td>
<td>28.6%</td>
<td>52.1%</td>
</tr>
<tr>
<td>Other</td>
<td>104</td>
<td>47.9%</td>
<td>100.0%</td>
</tr>
<tr>
<td><strong>Organizational ownership</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Private</td>
<td>94</td>
<td>43.7%</td>
<td>43.7%</td>
</tr>
<tr>
<td>Government</td>
<td>80</td>
<td>37.2%</td>
<td>80.9%</td>
</tr>
<tr>
<td>Joint</td>
<td>41</td>
<td>19.1%</td>
<td>100.0%</td>
</tr>
<tr>
<td><strong>Organizational activities</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Manufacturing</td>
<td>56</td>
<td>26.0%</td>
<td>26.0%</td>
</tr>
<tr>
<td>Service</td>
<td>110</td>
<td>51.2%</td>
<td>77.2%</td>
</tr>
<tr>
<td>Both</td>
<td>49</td>
<td>22.8%</td>
<td>100.0%</td>
</tr>
<tr>
<td><strong>Organizational age</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5 Years or less</td>
<td>17</td>
<td>7.9%</td>
<td>7.9%</td>
</tr>
<tr>
<td>6-10 Years</td>
<td>17</td>
<td>7.9%</td>
<td>15.7%</td>
</tr>
<tr>
<td>Over 10 years</td>
<td>182</td>
<td>84.3%</td>
<td>100.0%</td>
</tr>
</tbody>
</table>
A single factor emerged for the organizational commitment, Islamic work ethics and attitudes toward organizational change. Factor analysis was the first test used in this study to determine reliability and validity of the study constructs. The reliability subgroup in SPSS was also used for each of the study constructs to determine the Cronbach’s alpha for each scale.

The reliability scores for the various constructs showed reasonably high internal consistency. The nine items which define organizational commitment scored 0.906 on the reliability scale. While the Islamic work ethics had 0.857, attitudes towards organizational change measured 0.848 on the reliability scale.

The constructs used in this study were checked for their internal consistency by using reliability procedures. The procedures computed the Cronbach alpha values. These values, along with the relevant items that defined each construct, were shown in table 2. The table demonstrated that all the scales had high internal consistency. Nunnally (1978) suggested that minimum Cronbach alpha level of 0.70 is satisfactory. Since all the alphas scores in table 2 are above this minimum requirement, reliability minimum levels have clearly been satisfied.

4.4 Hypotheses Tests
Correlation analysis was the statistical tool used to test each of the two study hypotheses. A positive correlation was found between both organizational commitment and Islamic work ethics with organizational change, at 1% level of significance.

These results in table 3 indicate that there is a positive relationship between organizational commitment and attitudes towards organizational change and between Islamic work ethics (IWE) and attitudes towards organizational changes. Hence, both hypotheses were supported.

From the correlation coefficients, it can be seen that though both the two independent variables are positively correlated with the depended variable, but the extend of correlation is higher (0.465) between Islamic work ethics and the attitudes towards organizational change. Thus, it may be deduced that Islamic work ethic has more influence on the attitudes towards organizational change compared to the organizational commitment.
### Table II: Significant Factor Analysis and Reliability Analysis Results

<table>
<thead>
<tr>
<th>Construct name</th>
<th>Item</th>
<th>Factor*</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Organizational Commitment</strong></td>
<td>I would be very happy to spend the rest of my career with this organization</td>
<td>0.758</td>
</tr>
<tr>
<td></td>
<td>I enjoy discussing my organization with people outside it</td>
<td>0.613</td>
</tr>
<tr>
<td></td>
<td>One of the major reasons I continue to work for this organization is that I believe that loyalty is important and therefore feel a sense of moral obligation to remain</td>
<td>0.509</td>
</tr>
<tr>
<td></td>
<td>I really feel as if this organization's problems are my own</td>
<td>0.717</td>
</tr>
<tr>
<td></td>
<td>I think that I could not easily become as attached to another organization as I am to this one</td>
<td>0.718</td>
</tr>
<tr>
<td></td>
<td>I feel like 'part of the family' at my organization</td>
<td>0.786</td>
</tr>
<tr>
<td></td>
<td>I feel 'emotionally attached' to this organization</td>
<td>0.823</td>
</tr>
<tr>
<td></td>
<td>This organization has a great deal of personal meaning for me</td>
<td>0.845</td>
</tr>
<tr>
<td></td>
<td>I feel a strong sense of belonging to my organization</td>
<td>0.886</td>
</tr>
<tr>
<td><strong>Variance explained (%)</strong></td>
<td></td>
<td><strong>30.33</strong></td>
</tr>
<tr>
<td><strong>Cronbach’s alpha</strong></td>
<td></td>
<td><strong>0.906</strong></td>
</tr>
<tr>
<td><strong>Islamic Work Ethics</strong></td>
<td>Human relations in organizations should be emphasized and encouraged</td>
<td>0.665</td>
</tr>
<tr>
<td></td>
<td>Creative work is a source of happiness and accomplishment</td>
<td>0.710</td>
</tr>
<tr>
<td></td>
<td>Any man who works is more likely to get ahead in life</td>
<td>0.709</td>
</tr>
<tr>
<td></td>
<td>Work gives one the chance to be independent</td>
<td>0.737</td>
</tr>
<tr>
<td></td>
<td>One should constantly work hard to meet responsibilities</td>
<td>0.565</td>
</tr>
<tr>
<td></td>
<td>Good work benefits both oneself and others</td>
<td>0.631</td>
</tr>
<tr>
<td></td>
<td>Justice and generosity in the workplace are necessary conditions for society's welfare</td>
<td>0.631</td>
</tr>
<tr>
<td></td>
<td>One should carry work out to the best of one's ability</td>
<td>0.656</td>
</tr>
<tr>
<td></td>
<td>Work is not an end in itself but a means to foster personal growth and social relations</td>
<td>0.615</td>
</tr>
<tr>
<td></td>
<td>Life has no meaning without work</td>
<td>0.691</td>
</tr>
<tr>
<td><strong>Variance explained (%)</strong></td>
<td></td>
<td><strong>39.55</strong></td>
</tr>
<tr>
<td><strong>Cronbach’s alpha</strong></td>
<td></td>
<td><strong>0.857</strong></td>
</tr>
<tr>
<td><strong>Attitudes towards Organizational Change</strong></td>
<td>I usually benefit from change</td>
<td>0.738</td>
</tr>
<tr>
<td></td>
<td>I look forward to changes at work</td>
<td>0.714</td>
</tr>
<tr>
<td></td>
<td>Changes tend to stimulate me</td>
<td>0.784</td>
</tr>
<tr>
<td></td>
<td>Change often helps me perform better</td>
<td>0.785</td>
</tr>
<tr>
<td></td>
<td>Change usually benefits the organization</td>
<td>0.703</td>
</tr>
<tr>
<td></td>
<td>I intend to do whatever possible to support change</td>
<td>0.728</td>
</tr>
<tr>
<td><strong>Variance explained (%)</strong></td>
<td></td>
<td><strong>36.93</strong></td>
</tr>
<tr>
<td><strong>Cronbach’s alpha</strong></td>
<td></td>
<td><strong>0.848</strong></td>
</tr>
</tbody>
</table>

Rotated factor scores
Table 3: Pearson Correlation

<table>
<thead>
<tr>
<th>Attitude towards organizational change</th>
<th>Organizational commitment</th>
<th>Islamic work ethics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sig. (2-tailed)</td>
<td>.412(***)</td>
<td>.465(***)</td>
</tr>
<tr>
<td>N</td>
<td>218</td>
<td>218</td>
</tr>
<tr>
<td>Mean</td>
<td>*5.07</td>
<td>*4.53</td>
</tr>
<tr>
<td>SD</td>
<td>1.00</td>
<td>1.25</td>
</tr>
</tbody>
</table>

**Correlation is significant at the 0.01 level (2-tailed).

* Measured on a seven point Likert scale ranging from 1= strongly disagree to 7=strongly agree

The result of descriptive statistics means and standard deviations reported in the same table 3 indicate the levels of the three constructs as reported by the respondents. The results show that the overall mean of organizational commitment is slightly above the scale mid-point, 4. This can be interpreted as meaning that employees in the investigated organizations are neither committed nor uncommitted to their organizations. However, they are more inclined toward being committed. The overall mean of the Islamic work ethic (IWE) and attitudes towards organizational change are reasonably high, which indicate that employees in the investigated organizations strongly support the Islamic work ethic and support change in their organizations.

5.0 Discussion and conclusions

This section of the research discusses the results presented in the previous section. Overall conclusions and limitations of the study are presented as well as the implications for academicians and executives. Suggestions for further research are also discussed.

Tests using correlation analysis shows a positive relationship between organizational commitment, Islamic work ethics and attitudes towards organizational change. The result is indeed in consistent with the study hypotheses, based on what literature suggests.

The finding that Islamic work ethics influence attitude towards organizational change supports the bulk of other studies (Ali, 1992, 1996). It is also in consistence with the similar study by (Yousef, 2000a) undertaken in a sister Gulf state, UAE. This finding implies that those who support the Islamic work ethic would be more likely to embrace change in their organizations.
In the same vein, the finding that organizational commitment directly influences attitudes toward organizational change is not in contradiction with the findings of previous studies (Yousef, 2000a; Cordery et al., 1993; Iverson, 1996). The finding implies that those who are committed to their organizations are more likely to support its change programmes.

The results that the overall mean of organizational commitment are low are consistent with the findings of other studies carried out in other Arab Gulf states (Yousef, 2000a; Al-Meer, 1989; Ben-Baker et al., 1994; Bhuian et al., 1996), though the previous studies attributed such low organizational commitment to the fact that expatriate workers work for relatively high salaries and benefits and therefore they tend not to hesitate to leave their organization for better jobs elsewhere (Bhuian et al., 1996). But, this study examines the organizational commitment of only local employees.

Like other similar studies (Yousef, 2000a; Ali's 1996), the finding that aggregate mean of attitudes toward organizational change is reasonably high supports the argument that only the Arab managers, but also Arab non-managers who constitutes the bulk of the study subjects look favorably on change and are receptive to changes that improve organizational effectiveness and enhance employees’ welfare.

The finding of this study is also in support of the previous studies research (Yousef, 2000a; Ali, 1989, 1992; Ali and Azim, 1994) that employees in the Arab organizations strongly support the Islamic work ethic.

However, against previous studies (Yousef, 2000a) that targeted investigated both the local Arab employees and their expatriate counterparts, this study found based on the factor analysis that some of the items used in the previous studies are not homogeneous in measuring the study constructs in the Saudi work environment.

5.1 Conclusion

This study attempted to examine the significance of human factors, organizational commitment and Islamic work ethics in influencing attitudes towards organizational change. All of the two proposed hypotheses were statistically supported, indicating that organizational commitment and Islamic work ethics influence attitudes towards organizational of Saudi employees.

The study is also concerned with validating some western management theories, organizational commitment and attitudes toward organizational change in non-western setting and recently developed measure, Islamic work ethic, in Saudi environment. The two western theories were validated, though some items were not homogeneous in Saudi work setting. Moreover, Islamic work ethic which was earlier validated by Ali (1992) in Saudi was further validated by this study. However, only ten of the seventeen items were found to be homogeneous in measuring IWE in this study. This slight variation may be due to the passage of time between the two studies and more presence of foreign operations in the Kingdom now, which might have an impact on the Saudi employees’ work ethics and values.
5.2 Limitations of the study

This study, like all studies, is constrained by a number of limitations. Knowledge of these limitations provides a proper basis for suggesting areas for further studies. First, the study generalizes results for the entire Kingdom although the sample has been confined to the eastern province region, thus ignoring possible regional differences in each context. Second, the sample size, although comparable with many studies may be sufficient, is considered small and an obvious limitation. Further studies with larger, more representative samples are likely to enrich the existing literature. Lastly, the study is of snapshot type, which might not fully capture the dynamic nature of the attitudes toward organizational change.

These limitations, while important, do not represent a threat to the fundamental validity of the study findings. These findings have important implications which are discussed in the next section.

5.3 Research Implications

Both academics and executives are likely to find the results of this study useful and meaningful. The following discussion provides the implications of his research for both researchers and executives.

Implications for executives

The findings of this study have implications for executives. First, the findings that the organizational commitment and Islamic work ethic directly and positively influence attitudes toward organizational change would be useful for change leaders in Saudi organizations or in a similar work setting.

Attitudes toward organizational change efforts could be improved through improving both support of the Islamic work ethic and organizational commitment. For organizations that are to raise the commitment of their employees, they might consider better selection and training of HR managers and setting up a commitment policy, among other majors.

Similarly, Change leaders may take steps to enhance employees’ support of the Islamic work ethic (or work ethic in general), and subsequently improve employees’ acceptance of change. Some of the efforts to be undertaken by the change managers in promoting employees’ support of Islamic work ethics include emphasizing and encouraging human relations, among others. In addition, Islamic work ethic (or work ethic in general) could an additional important individual difference to consider, among others, during recruitment and selection for organizations that are looking for ways to hire employees who have positive attitudes toward change.
Implications for Further Studies

The findings of this study, coupled with its limitations will encourage further research that could shed more light on the factors that could influence organizational change. First, further studies should consider respondents from all the major provinces in the Kingdom, possibly including female respondents, to ensure more generality of the findings. Further studies could also replicate the study using larger sample size. To account for the cross sectional nature of the study limitation, further study could be replicated that should collect data using longitudinal survey method so as to accommodate possible changes of the respondents’ perceptions of the study constructs. Furthermore, the influence of other factors on employees’ attitudes toward organizational change is also worth studying. Replication of this study in another sister Gulf countries to confirm or refute the findings of the present study would also be of interest.

References


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A Global Case Study: Mobily of UAE Penetrating Saudi Arabia

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Dhahran, Saudi Arabia

Abstract: Mobily was founded in 2004 by the UAE-based, Emirates Telecommunications Corporation (Etisalat), with the purpose of ownership, operation and management of GSM and 3G mobile telephone networks, and providing mobile internet services. Etisalat won the second GSM license as well as a 3G license in Saudi Arabia in August 2004 for US $3.45 bn, thus ending Saudi Telecom Company's monopoly in the wireless business segment. Mobily launched its services in May 2005, and ended the year with 2.3 million subscribers, capturing a market share of 16%. By the end of 2006, the company's subscriber's base rose to 6 million subscribers, thus increasing its market share to 31%. The management of mobily is focused in its drive to increase its presence with post paid subscribers and offer value added services like mobile broadband internet services, video streaming, et al. An aggressive marketing spree has solidified the brand image of mobily in the expat population, Saudi youth and women citizens. Mobily has positioned itself as an integrated telecom operator with focus on Mobile and data services. The case went through SWOT analysis and discussed the marketing strategy of mobily.

Introduction

Saudi Arabia private sector has grown steadily in the last few years a trend in likely to continue. This is expected according to the overall strength of the Saudi economy which is expected to earn revenue from gas which will be added to the strength gained from the global oil marked which the Kingdom represent one of the largest shares in it. The GDP grew approximately 6% in 2003 and the oil sector expanded by 14.3%. With the efforts of the government to diversify the economy with a particular emphasis on the private sector it is expected that this sector will show a lot of changes in the next five years.

Rate of growth of the population is 3% in 2003. The total population was 23 million, about 60% of them under the age of 25. If the population grows at the same rate accompanied by greater degree of mobility, the need of mobile services will grow as well.

Population Growth:

<table>
<thead>
<tr>
<th>Year</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>23.4</td>
<td>24.1</td>
<td>24.8</td>
<td>25.5</td>
<td>26.2</td>
<td>27</td>
</tr>
</tbody>
</table>
About 75% of these numbers are Saudis and 25% are non Saudis. We expect the number of Non-Saudis to decrease in percentage so the rate will be during the coming years as follows

<table>
<thead>
<tr>
<th>Year</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>100%</td>
<td>24</td>
<td>24.8</td>
<td>25.6</td>
<td>26.7</td>
<td>27</td>
</tr>
<tr>
<td>78%</td>
<td>18.7</td>
<td>19.3</td>
<td>20</td>
<td>21.0</td>
<td>21.6</td>
</tr>
<tr>
<td>Saudi</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-Saudi</td>
<td>5.3</td>
<td>5.5</td>
<td>5.6</td>
<td>5.2</td>
<td>5.4</td>
</tr>
</tbody>
</table>

It is expected that due to Saudization of jobs the rate of Non-Saudis would be 20% for the years 2008 and 2009. This growth from 24 million in 2005 to 27 million in 2009 means an increase in the market. A potential of 60% means that an increase of 1.8 million is expected in 2009 of ages less than 25 years who represent an important target as customers of the mobile and internet services.

**Source:** Attached Telecommunication white paper and Samba review

**Telecommunications Sector in Saudi Arabia**

Saudi Arabia is the largest telecommunications market in the Middle East with approximately 3.4 million fixed lines and 7.5 million mobile subscribers by the end of 2003. STC is currently the exclusive provider of telecommunication services in Saudi Arabia and offers fixed and mobile telecommunications services, wireless communications, paging, satellite technologies and Internet Services.

Saudi Arabia has the largest and fastest growing market for telecommunications products and services in the Middle East. Total expenditures within the Kingdom’s telecom sector are expected to approach $4.7 billion in 2005 and $60 billion by 2020. The expansion of telephone services and their subsequent privatization have been important objectives in Saudi Arabia’s five-year development plans, with particular emphasis placed on the telecommunications sector during the Seventh Development Plan (2000-2005). The Plan calls for increasing line density rates to 25 lines per 100 people by the end of 2005, from 10 lines per 100 people in 1996. With a modern regulatory framework now firmly in place, Saudi Arabia is poised to heavily invest in a state-of-the-art IT infrastructure that will meet the demands of its tech savvy population. Throughout Saudi Arabia’s rapid IT expansion, American companies such as Microsoft, Cisco Systems, Lucent, IBM, Hewlet Packard, Oracle and Motorola have played an integral role. The potential for U.S. firms to take part in the expansion of this sector is heightened with the enactment of the new telecommunications bill, and the rolling out of new mobile, fixed-line, data and satellite operators through 2006 and beyond.

Mobile phones have dramatically altered the telecommunications market in Saudi Arabia. In an effort to keep pace with further advances in telecommunications, Saudi Arabia has vigorously pursued a modern mobile network over the past decade. Beginning in 1994 when the Kingdom launched the Global System for Mobiles (GSM), known locally as
“Al-Jawal,” Ericsson, Nokia and Lucent have worked closely within the Kingdom to transform its mobile infrastructure. By 2004, mobile telephone subscribers had risen from 16,000 in 1995 to 9.2 million. According to a recent report from the Riyadh-based Economics Studies House, the Kingdom’s mobile penetration rate is expected to increase from the current rate of 40 percent to 60 percent by 2014, with over 20 million subscribers.

The Kingdom has dedicated its efforts over the past two years to meeting increased demand in the under penetrated mobile market by rolling out new cellular GSM licenses. In August 2004, the Saudi Cabinet awarded the second GSM mobile telephone license to a consortium led by Etisalat of the UAE with a third GSM license award expected in 2006. Etisalat submitted a bid of SR12.21 billion ($3.25 billion) for the license, the highest bid among the six competing consortia whose bids were previously released to the public in July 2004. The Cabinet also approved a $201 million license for Etisalat to establish and operate the third generation G3 mobile phone network and to provide all related services at local, national and international levels. At the same time, the Cabinet approved granting the STC a license to provide third generation G3 mobile phone services if it submits an application to CITC within one year.

As part of the award, Etisalat was obligated to sell 20 percent of its stock to the public in an initial public offering (IPO). The IPO of Etihad Etisalat, which began on October 16, 2004, was the largest IPO in Saudi history, attracting 51 billion riyals ($13.6 billion). Initially, twenty million shares were offered at 50 riyals ($13.3) each, totaling SR1 billion ($266 million). However, more than 4 million applications were received, resulting in a 51-fold oversubscription. Etisalat is required to sell off an additional 20 percent, which will be offered in another IPO in the third year of the license.

Etisalat, whose brand name is Mobily, officially launched its services at the end of May. The launch followed an almost two month testing period of the 850 towers installed throughout the Kingdom by Ericsson, Motorola, Alcatel and Huawei. Mobily will provide service to 30 cities, including national roaming, voicemail, news and data downloads, SMS, MMS, missed call notification, WAP and Internet browsing. Many of

Source: Communications and Information Technology Commission
the services that Mobily is initially providing would not be possible without STC assistance. This technical assistance, which was delineated in the second GSM license, will last for three years.

Due to Mobily’s limited ground network, STC will provide it with among other things, transmission links between Etisalat locations, particularly in rural villages. As Mobily continues to construct its nationwide mobile network, there will be several contracts available for international telecom companies. In March 2005 for example, Motorola announced an agreement to provide Mobily with a GSM Base-Station System (BSS) mobile network. The BSS system will include Motorola’s Enhanced Data for GSM 4 Evolution (EDGE) and Push-To-Talk over Cellular (PoC). Under the contract, Motorola will provide a Radio Access Network (RAN) for GSM and EDGE, including Horizon II base stations, on a turnkey basis. The network will cover parts of the western, southern and northern regions of the Kingdom. It will also provide traditional voice services and will be able to offer Mobily subscribers walkie-talkie style communication using Motorola’s PoC solution. Motorola was also awarded a contract by Saudi Arabia’s Public Telecommunications Company (PTC) to build and operate a nationwide integrated Digital Enhanced Network iDEN system. PTC, a consortium of four major Saudi companies authorized by STC to build and operate a nationwide iDEN system, anticipates launching the new wireless service in 2005.

The Company believes that the telecommunications sector in Saudi Arabia has evolved considerably since April 1998 when STC was formed and look over the telecommunication operations from the Ministry of Post, Telegraph and Telephones for the provision of telecommunication services. In June 2001, the Telecommunications Act regulating the sector was promulgated creating CITC in accordance with the CITC Ordinance (as hereinafter defined). In September 2002, the Government sold 30% of STC’s share capital through an initial public offering in January 2003.

*Source: Attached Telecommunication white paper and Samba review*

Since 1998, the sector has witnessed significant growth, mainly due to an increase in the number of mobile subscribers and internet users. Between 1998 and 2003, the number of mobile subscribers and internet users grew at an average rate of 69% per annum and 130% per annum (CAGR), respectively. During the same period, fixed line subscribers increased by approximately 1.2 million to reach 3.4 million while mobile subscribers expanded by 6.7 million over the same period. The Company believes that the pace of growth in fixed line subscribers has slowed down on account of the increased use of mobile services and a fixed to mobile substitution trend. The number of mobile subscribers surpassed fixed line subscribers during 2002 and the growth in fixed lines was limited to 2% per annum in 2003, down from 21% per annum in 1999.

<table>
<thead>
<tr>
<th>Mobile subscribers</th>
<th>1998</th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed line (‘000)</td>
<td>119.0</td>
<td>52.7</td>
<td>64.4</td>
<td>83.8</td>
<td>98.0</td>
<td>48.9</td>
</tr>
<tr>
<td>Growth (%)</td>
<td>2.230</td>
<td>2.706</td>
<td>2.965</td>
<td>3.233</td>
<td>3.318</td>
<td>3.398</td>
</tr>
<tr>
<td>Internet Users (‘000)</td>
<td>----</td>
<td>190</td>
<td>350</td>
<td>671</td>
<td>1,620</td>
<td>2,323</td>
</tr>
<tr>
<td>Growth (%)</td>
<td>1.0</td>
<td>21.3</td>
<td>9.6</td>
<td>9.0</td>
<td>2.6</td>
<td>2.4</td>
</tr>
</tbody>
</table>
The introduction of prepaid services in 2002 and the reduction in tariffs have marked a rapid growth phase in the mobile subscriber base in the Kingdom. The number of mobile users expanded by approximately 2.5 million users in 2003 to 7.5 million resulting in mobile penetration increasing from approximately 23% in 2002 to approximately 33% in 2003. Prepaid subscriptions accounted for most of this growth and, by the end of 2003, the number of prepaid subscribers stood at approximately 4.1 million representing 55% of the total mobile subscriber base, up from 43% in 2002.

<table>
<thead>
<tr>
<th></th>
<th>2002</th>
<th>2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prepaid Subscriptions</td>
<td>2,153</td>
<td>4,151</td>
</tr>
<tr>
<td>Growth (%)</td>
<td>---</td>
<td>92.8</td>
</tr>
<tr>
<td>Postpaid Subscribers</td>
<td>2,855</td>
<td>3,397</td>
</tr>
<tr>
<td>Growth (%)</td>
<td>---</td>
<td>19.0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>5,008</td>
<td>7,547</td>
</tr>
</tbody>
</table>

Source: Attached Telecommunication white paper and Samba review

The Saudi Arabia economy is considered one of the biggest economies compared with the other countries in the Middle East and North Africa. The following table shows this fact.

Saudi Arabia is the richest economy amongst the MENA countries with a GDP per capita of US$9,275 compared to an average of around US$1,892 for the large MENA countries. The Saudi mobile market is also more developed than these countries with a penetration of approximately 33% compared to an average penetration of approximately 17% and an ARPU of US$62 compared to an average ARPU US$19 for MENA countries.

<table>
<thead>
<tr>
<th>Country</th>
<th>GDP/Capita</th>
<th>Population</th>
<th>Penetration</th>
<th>ARPU (US$)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Algeria</td>
<td>$1,939</td>
<td>32</td>
<td>4.6%</td>
<td>30.0</td>
</tr>
<tr>
<td>Egypt</td>
<td>$963</td>
<td>70</td>
<td>8.3%</td>
<td>16.0</td>
</tr>
<tr>
<td>Iran</td>
<td>$1,587</td>
<td>66</td>
<td>3.8%</td>
<td>14.0</td>
</tr>
<tr>
<td>Morocco</td>
<td>$1,498</td>
<td>30</td>
<td>24.3%</td>
<td>11.0</td>
</tr>
<tr>
<td>Tunisia</td>
<td>2,506</td>
<td>10</td>
<td>18.6%</td>
<td>27.0</td>
</tr>
<tr>
<td>Turkey</td>
<td>$2,856</td>
<td>67</td>
<td>41.8%</td>
<td>15.0</td>
</tr>
<tr>
<td>Saudi Arabia</td>
<td>$9,275</td>
<td>23</td>
<td>32.7%</td>
<td>62.0</td>
</tr>
</tbody>
</table>

Source: Attached Telecommunication white paper and Samba review
ETIHAD ETISALAT COMPANY OVERVIEW

Mobily is the official brand name of Etihad Etisalat, the new mobile service provider in the Kingdom of Saudi Arabia. Established in accordance with a 2004 royal decree, the ownership of the company is two-fold: A Saudi ownership, comprising public investors holding 20% of the company’s shareholding, while private investors own a 45% stake. The balance of 35% is owned by the Etisalat of UAE.

Mobily Company Values

"We at Mobily believe that our customers come first. We are driven to provide them with state-of-the-art services as simple as possible and in a friendly way. This determination for excellence and customer-orientation is reflected in our company values"

The launch of Mobily is consistent with Etihad Etisalat’s vision and mission which are based on genuine values such as working with an adventurous and ingenious spirit, openness and friendliness, contemporary, Collaborative, driven, simple and dependable.”

“We all have values. They come from the Quran, our parents, the people around us and from deep inside ourselves. They are what we stand for; they make us who we are and govern how we live our lives. Our corporate values are simple”.

Simple & dependable

“We’re simple and dependable – always making sure that no matter how complex the technology, our services are easy to use.”

Open & friendly

“We’re open and friendly – courtesy costs nothing, and we insist on honesty and transparency in all our dealings”

SWOT Analysis

EEC Strength

1. The main strength came from the mother company (Etisalat UAE Company) Values”

“We work together as one team to satisfy customer requirements in telecommunication services and technology in a friendly and efficient manner”

The company presented an additional 20 per cent of its shares for general subscription, giving an opportunity to Saudi citizens to invest. The share subscription
attracted unprecedented interest from Saudi investors and the IPO was oversubscribed more than 51 times.

EEC is not a completely new company. It started dealing with communication and in particular mobile services in the Middle East. This was on 1982. In 1994 it started GSM services. In 1996 the number of customers in mobile services increased to 130,000 while as from 1996 and till now the number increased to become more than 3,000,000.

EEC won the contract after severe competition with other companies specialized in mobile services. Our bid amounted to SR 12,200,000,000 to be paid in advance while the other companies applied for the service with less offers as follows:

11.70 Billions by MTN of South Africa
9.80 Billions Oraikom Telecom from Egypt
9.40 Billions by MTC from Kuwait
8.00 Billions by Samawat from Italy
6.00 Billions by Telecom from Spain

It is expected that number of companies working in Saudi Arabia will be three or more in the near future.

2. Strong Founding Shareholders:

The Founding Shareholders of EEC bring with them experience in diverse business sectors. Etisalat is a leading operator in the Middle East and has a proven track record for profitable GSM and 3G operations in the UAE. Etisalat will bring and apply the strategies and strengths developed in the UAE to the Saudi markets. EEC believes that, Etisalat as the Operator will provide EEC with operational and technical expertise, and managerial resources to roll-out its network. It is further believed that Etisalat will also leverage its relationships with equipment vendors, content developers and international operators to provide high quality products and differentiated customer service. EEC can further draw on the Saudi Arabian Founding Shareholders market insight, business expertise, distribution, logistical and potential site requisition support.

3. Strong Technical Operator:

Etisalat is one of the leading telecommunication service providers in the Middle East Region with over 20 years experience is establishing, building and managing telecommunications operations especially mobile telephone sector in its home market and regional markets. Etisalat commenced commercial GSM service in the UAE in September 1985. Currently, the Etisalat UAE network includes more than 4,100 GSM Base Stations, serving 3.4 million customers. UAE mobile penetration is 85% making this network and market base the largest single mobile operation in the Middle East outside the Kingdom. The Company believes that Etisalat’s technical competencies are further demonstrated in establishing and operating Thuraya, an established GMPCS service provider with nearly 185,000 subscribers and Etisalat’s active involvement in other GSM mobile operations in Tanzania (Zanzibar).
EEC believes that it will benefit from Etisalat’s well-established relationships with leading GSM network infrastructure providers. Etisalat is experienced in accessing international carriers and services. The UAE is the primary hub location for international connectivity, which is accessed via Etisalat infrastructure for the region. Both Fiber Optic Link Around the Globe and Fiber Optic Gulf have access points in the UAE.

4. Innovation:

Telecommunications is now an integral part of the social, economic and political tissue of the world. Networks of the future will be digital and intelligent. They will offer high transmission capacity and flexible bandwidth. They will be easily accessed and connected. Services provided will be personal and tailored to individual needs. They will allow us to interact in ways previously not possible - available at any time and any place. In addition to providing entertainment and business services, networks of the future will provide education, healthcare and other public services.

Major advances in communications technology have substantially widened the range of services carried by the network. Satellites, microwave radio, optical cable links, digital switching and transmission, offer a potential for the improvement of quality and for the extension of access to the most remote areas. The world is now a fully integrated information network.

The pace of technological change is increasing. The magnitude of demands the future will make on our creativity and capacity to adapt is great. Customers will demand more than just state-of-the-art technology. They will want convenience and increased control over their lives that easy and affordable information access can provide. Businesses will look for total telecommunications solutions that will not only enable them to remain productive and compete globally but will also give them a competitive edge and a return on their investment.

Etisalat is well-placed to meet these challenges head on. We will continue to be there - contributing in guiding, assisting and developing cost-effective technologically advanced services that will meet the varied needs of our local and international customers and pave the way for the region's new dynamism in the telecommunications industry well into the 21st Century.

Etisalat was the first operator in the Middle East region to introduce 3G PMCS providing customers with advanced and high speed data services. It currently has over 7,000 3G customers in the UAE and has recently launched video telephony in MENA region and has the largest number of 3G base stations and 3G users in the region. It has established several business units to provide services to other business in the Middle East. For instance, e-Company provides expertise in IT and e-commerce applications, while UAE Lab offers technical support and advisory services regarding acceptance testing and site commissioning.

Following are samples of the latest products Etisalat UAE is launching:
MAYSOUR Prepaid Telephone Service is ideal for Residential/Business Telephone Lines as it gives you the convenience of receiving incoming calls for a full year, while making outgoing calls on a prepaid basis to match your budget needs.

**Prepaid Calling Card**

The Etisalat Prepaid Calling Card is a disposable calling card, available in fixed denomination of Dhs. 30 and Dhs. 60. Cost of calls made is deducted each time the card is used, until the full amount of the card is utilized.

**Smart Payphone Card**

Smart Cards are disposable Prepaid Calling Cards which have an electronic chip. They are available in a Dhs.30 denomination and can be used to make local and international calls from any payphone in the UAE. Smart Cards cannot be used outside the country.

**WASEL - Prepaid GSM Service**

WASEL – Etisalat’s Prepaid GSM Service aims to bring mobile communications within reach of everyone. The service enables subscribers to receive incoming calls on their mobile phones during the one year validity period.

5. **Customer Care:**

Etisalat believes that it provides high levels of customer care directly to its customers in the UAE. Etisalat employs the latest IT systems to ensure that customer care personnel can better respond to the need of its customers. Etisalat believes that customer care has been a major factor in its success in achieving high levels of customer satisfaction and penetration rates exceeding 80% in the UAE. According to a market survey conducted by Etisalat in UAE, over 95% of the respondents expressed satisfaction with Etisalat’s services.

6. **Strong Brand Identity of Etisalat:**

The Etisalat name enjoys a strong brand image in the UAE. Etisalat believes that it has built the brand based on an understanding of customer requirements and transforming that understanding into developing innovative products and services. EEC will utilize the expertise gained by Etisalat in branding and marketing in the Saudi market. Although EEC is a new comer to the market of communication in Saudi

**EEC – weakness**

Despite the strengths available, there are also threats. And the main threat is building something from scratch and operates at the same time. Such threats are around people so EEC realized that since beginning and move forward with the following plans.

1. **Human Resources Management**
Manpower of any company represents important factors for its success or failure. It is important in both administrative and operational levels. The use of scientific methods for recruitment and training is increasingly dominating the industry recently. Job analysis specification and job description are the starting points towards the success of employing to achieve the firm’s targets.

We need manpower estimates to fulfill two main requirements:

1. A detailed manning table to calculate the cost of manpower as part of the service cost.
2. The determination of the training requirement.

**Manpower Planning:**
This will generally start at the department level. It is important to define labor and staff requirements by function and categories. The categories may include:

1. Managerial Staff
2. Supervisors
3. Administration Staff
4. Sales and Marketing Staff
5. Engineers
7. Skilled Labors
8. Semi – Skilled Labors
9. Unskilled Labors

In planning personnel requirements for a company we should consider the following:

1. General assessment of manpower supply in the area.
2. In the view of the skill and technological requirement of the company we should appraise occupational skills available at national level.
3. Legal aspects and labor legislation which cover the industrial relations.
4. Wage levels and fringe benefits and their expected rate of growth.
5. Annual working days.
6. Supervision staff will be considered with caution. Qualifications will be assessed and experience examined. If there is a need for training programs, this will be stated for each case.

**Training:**
Training is a continuous action usually conducted by progressive companies with the aim of increasing efficiency of personal.

**Skills Requirements of the Staff:**
The company staff includes Director General, Managers of different departments, and supervisors of unit till the stage of ordinary clerks. Skills required will range from university and higher institutes and ends with secondary school qualification. Experience
required will depend on the requirement of jobs, but there will be minimum period that should be met.

The staff recruited will be of a high caliber and well trained for higher managerial positions. At the same time it will bear qualification and experience requirement for any particular job.

There is a commitment of EEC as a Saudi entity to employ a high proportion of Saudi nationals. At the same time EEC needs trained employees who have the initiatives and ability to do a job which is sophisticated and may be changing by employment of new technology.

During the first year sufficient numbers of skilled and experienced Technical Managers, Engineers, Technicians and Commercial Specialists will be transferred from Etisalat in its headquarter in UAE. These employees in different status will assist in training Saudi national on the job. Besides a training center will be built to commence training after the end of the first year. The target will be Saudi nationals comprising both Universities and Technical institutes. This is in addition to unskilled laborers who would be Saudi nationals.

Also during the first year and second year the company will get use contractors on the Saudi markets as recruiting agents with a decentralized organizations the company will cover the four regions of the company with staff to perform duties related to company operations in different regions. At the same time the top organization will work from its headquarter in Riyadh.

The ECC have a management agreement with Etisalat and it will be committed to this agreement. According to the agreement the company is headed by aboard of directors consisting of 10 persons, six of them should be Saudi nations.

The executive management and senior positions will be according to the agreement the responsibility of Etisalat.

Other Senior positions of the company will include senior staff which includes:

- Financial Controller
- Mobile Network Development Manager
- Care Network
- Technology and Service development
- International Operations
- Marketing and Strategies
- Product and Services
- Sales Manager
- Human Resources Managers
- Contracts and Administration

The number of staff filling other positions are forecasted to be starting by 500 in the first year and grow according to increase in operations to be 4000.
The growth of employees numbers will be as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>500</td>
<td>1250</td>
<td>2000</td>
<td>3000</td>
<td>4000</td>
</tr>
</tbody>
</table>

Salaries and benefits expected to management and staff are

<table>
<thead>
<tr>
<th>Year</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Millions</td>
<td>150</td>
<td>400</td>
<td>700</td>
<td>1000</td>
<td>1500</td>
</tr>
</tbody>
</table>

The company increased staff as from the third year is due to the introducing services of 3G and the staff needed for new extensions when the company penetrates the market with a higher percentage. Cost of staff will also increase due to the system of merit increase and incentive systems which will be introduced at the beginning of the third year. This is also due to competition expected from a new comer in the market of telecommunication in Saudi Arabia. Each Company will search for retaining its staff which is well trained and experienced within the company.

Management and personnel area will also need more spending in the area of training, which is a continuous effort. During the fourth year training is expected to expand especially in the area of expected new technologies of telecommunication. Cost of training is expected to represent a high increase at the start of the third year. Within the next 5 years costs of training and employee development are forecasted to be:

<table>
<thead>
<tr>
<th>Year</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Million</td>
<td>10</td>
<td>20</td>
<td>40</td>
<td>50</td>
<td>50</td>
</tr>
</tbody>
</table>

The cost of human resources during the next 5 years could be summarized as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Employers (No)</td>
<td>500</td>
<td>1250</td>
<td>2000</td>
<td>3000</td>
<td>4000</td>
</tr>
<tr>
<td>Salaries &amp; benefits Sr. 000</td>
<td>150,000</td>
<td>400,000</td>
<td>700,000</td>
<td>1,000,000</td>
<td>1,500,000</td>
</tr>
<tr>
<td>Cost of Training SR. 000</td>
<td>10,000</td>
<td>20,000</td>
<td>40,000</td>
<td>50,000</td>
<td>50,000</td>
</tr>
<tr>
<td>Total</td>
<td>160,000</td>
<td>420,000</td>
<td>740,000</td>
<td>1,050,000</td>
<td>1,550,000</td>
</tr>
</tbody>
</table>

Source: Interview with EEC officials and informal (Business Plan)

**EEC – Opportunity**

Despite the weakness mentioned EEC has good opportunities to succeed.
Telecommunication market in Saudi Arabia offers a strong business potential. This market characterized by:

1. High population growth rate (3% annually)
2. A relatively low mobile penetration compared with other gulf countries.
3. Only one competitor till 2006.

The intention of offering of 3G services by EEC will increase revenue opportunities. This is in addition to the trends that have emerged in the mobile telecommunication market. The industry is rapidly converging to create a new opportunity in which many types of electronic media will act as personalized interface between providers of mobile products and services and customers. On the other side migration to 2.5G and 3G mean that GSM technology allows operators to provide notice telephony and low speed data transmission products such as short message services (SMS) but it can not support high capacity data transmission services. 3G products and services based on latest technology provide advanced data transmission products that offer full interactive capabilities.

**EEC Threats:**

Despite the ample opportunities available, there are also threats.

**Threats considered as follows:**

1. **Industrial risk**
   
   a. **Government Regulations of the Telecommunication Industry:**

   The business of EEC is subject to Saudi Arabian government regulations. The telecommunications sector regulations have undergone substantial reform in the last three years. These changes have created a new ministry and a new regulator, the Ministry of Communication and Information Technology (the “Ministry”) and CITC, respectively. The Ministry and CITC are the main Saudi government bodies responsible for regulating the telecommunications sector and are responsible for the telecommunications industry policies and regulations, licensing, tariffs, competition, telecommunications resource allocation, service standards, technical standards, interconnection and settlement arrangements and universal service obligations (USO).

   The Telecommunication Regulations (as hereinafter defined) applicable to EEC’s activities and the Licenses are generally new, subject to change, and have been subject to limited governmental interpretation. Precedents for and experience with telecommunication regulation in Saudi Arabia are generally limited. The regulatory framework within which EEC operates may constrain its ability to implement business strategies and limit its flexibility to respond to market conditions and to meet its business objectives and plans as currently envisaged.

   CITC has only recently been established and there can be no assurance as to any new decisions it will issue or whether it will change the interpretation of existing rules applicable to EEC. There can also be no assurance that the law or legal system will not change further or not be interpreted in a manner that could materially and adversely affect EEC’s operations. Under the Telecommunications Act and the Telecommunications By
laws (the “telecommunications Bylaws”), the board of CITC (the “CITC Board”) may amend, suspend, revokes or not renew the Licenses, for violation of basic licensing conditions, bankruptcy, dissolution or liquidation of EEC, failure to pay licensing or other fees or where the Company carries out of activities that are prejudicial to the public interest. Furthermore, under the Telecommunications Act, the Violation Committee of CITC may impose penalties for any violation, including one of frequency outside those that are approved. Finally, any decision of CITC can be appealed to the Minister of Communication and Information Technology and then to the Board of Grievances.

**b. Competition:**

Saudi Telecommunications Company (STC) is currently the sole provider of telecommunications services in Saudi Arabia and as such enjoys a dominant market position. With the award of the Licenses to EEC, the Saudi market will be a duopoly until September 2006, when a third mobile license is expected to be awarded. EEC will therefore face competition from STC and the new providers of telecommunications services, Internet and managed data services.

Competition in the Industry may affect EEC’s market share, ability to acquire new subscribers, marketing costs and tariff structures and other factors, which may materially impact the Company’s business and financial condition, prospects and results of operations.

**c. New technology:**

New emerging technology is subject to rapid and significant changes. Advances in telecommunication and information may adversely affect the whole system.

**d. 3G Adoption**

This is sophisticated service which faces the problem of being adopted in a market where not available before.

**e. Lack of operating History in Saudi Arabia:**

EEC has not worked in Saudi Arabia before.

2. **Financial risk**

The development, ownership and operation of a mobile telephone network require substantial capital investment and operating and marketing expenditure. EEC estimates that it will need to spend significant amounts for the roll out of its network and development of its operations. In line with similar telecommunications startup projects, EEC expects to incur losses initially as it rolls out its network, expands its operations and introduces new products and services. This may require EEC to carry losses going forward.

EEC will also need to obtain financing to repay/refinance the Islamic Financing Facility. In addition, the Company will need to meet the debt servicing requirements of both the...
Islamic financing Facility as well as the long-term debt facility. EEC’s ability to make payments on its debt will depend on EEC’s ability to generate cash in the future. This is subject to economic, financial, competitive and other factors some of which may be beyond EEC’s control.

As a result of any shortfall of internal cash flows and if, for any reason, adequate debt or equity financing is not available as needed, or is available only on terms unfavorable to EEC, the business and financial conditions prospects and results of operations of EEC could be materially adversely affected.

3. **Future risk:**

The development of EEC’s business depends on the future level of demand for mobile telecommunications in Saudi Arabia. These factors include general economic conditions, the development of the GSM and 3G markets, the number of subscribers and their usage trends, the emergence of new technologies competition and future improvements in the quality and availability of fixed line and mobile telephone services in Saudi Arabia. Other factors that may affect the business are costs of attracting new customers, the competitiveness of EEC’s tariffs and the price of handsets.

Given the multitude of factors, many of which are outside EEC’s control, it is difficult to predict with any degree of certainty the future growth of the mobile telecommunications sector in Saudi Arabia. Any developments in the Saudi telecommunications sector that negatively impact EEC or its business could materially affect the Company’s business and financial condition, prospects and results of operations.

Risks related to financial threat and development of Saudi mobile telecommunication market are not controllable and it is very important to depend on strategies that lessen their adverse effect on the profitability of the business.

**Mobily marketing strategy through penetration and pricing:**

**Penetration Strategy**

The company will penetrate the market gradually. There are a number of reason why penetrating the market gradually, namely:

1. For the company it is feasible to start rendering services gradually to compete with previous services provider even if the demand is fairly enough.

2. You have to convince consumers first with your services as being competitive in terms of quality, process and after sales services if needed. So you have to evaluate responses.

3. At this stage your market research will start a big job in discovering the results of your penetration of the markets, the response of competitors, and the attractiveness of your services to end users who could have been discovered and worked with through time.

4. More services or change will be made based on the result and time would have been enough to make any kind of feedback before more services are put on the market.
By gradual penetration of the market ECC share is expected to grow as follows during the 5 Years.

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population (Million)</td>
<td>24.1</td>
<td>24.8</td>
<td>25.5</td>
<td>26.2</td>
<td>27</td>
</tr>
<tr>
<td>Growth %</td>
<td>3</td>
<td>3</td>
<td>3</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>Telecommunication Targeted Market %</td>
<td>60</td>
<td>60</td>
<td>60</td>
<td>60</td>
<td>60</td>
</tr>
</tbody>
</table>
| Telecommunica
tion Targeted Market (Million) | 14.46  | 14.88  | 15.30  | 15.72  | 16.2   |
| Penetration    | 9,075,000 | 9,982,500 | 10,980,750 | 12,078,075 | 13,285,882 |
| EEC Market Share % | 12     | 25     | 30     | 35     | 38     |
| EEC Subscribes | 1,089,000 | 2,495,625 | 3,294,225 | 4,227,526 | 5,048,635 |
| Prepaid Voice (60%) | 653,400 | 1,497,375 | 1,976,535 | 2,536,395 | 3,029,131 |
| Postpaid Voice (40%) | 435,600 | 9,98,250 | 1,317,690 | 1,690,930 | 2,019,454 |

*Source: Interview with EEC officials and informal (Business Plan)*

ECC strategy in addition to gradual penetration of the market will be focused on

1. An extensive coverage of a large geographical area with a high quality network
2. Offering a suite of services that will cater to the needs of the targeted market segment which will include international dialing and general package radio service (GPRS)
3. Provide the entire customer base with a variety of value added services delivered in a simple user friendly and personalized manner accessible through a range of access modes.
4. Provide a superior customer service which could achieve a high level of customer satisfaction.
5. Develop and broaden distribution channels to increase customer numbers. At the same time develop an integrated management information system to support distribution activities.

6. Develop and maintain a simple and transparent tariff structure which enables exercising of leadership in setting of prices and building of market share. Prices according to regulations could be lowered up to the point when any company could cover up to 40%. In our plan the highest coverage will be in 2009 when the share become 38%.

7. Exploiting revenue potential in data services. The company will gradually develop new data application for mobile phones, personal digital assistants and laptop.

8. Deploying of a rich suite of value added services by offering:
   a. Portal which will enable subscribers to configure, manage and modify their subscription services.
   b. Message services such as SMS and instant messaging

9. Establishing roaming services through its affiliate Emirates Data clearing house the main roaming clearing house in the region.

10. During the fourth year of this plan we will deploy a nationwide cellular 3G wideband code division multiple access (WCDMA) network in the kingdom. This network will feature high speed date and voice convectively. This will enable the company to offer voice and data products, applications and services for a wide range of mobile equipment and corporate and consumer markets. These services will benefit from the high speed data capabilities of the proposed 3G network and high speed Internet access and data down load from multiple terminal types.

It is expected that EEC will compete the STC the only service provider in the past. EEC knows that in such kind of industry each company has to establish its strategy as a counter strategy to its competitor. STC is not far away and parts of his strategies are well known in the past. But STC in the past was a natural monopolist. STC was seeking to maximize his profits at the position when his marginal revenue is equal to marginal cost. STC desire was limited by government regulations on prices and the quality of services required. But still STC is a strong competitor in providing the same service and as long as the limit of prices is known or expected STC can earn more if his costs are low. Now circumstances are changed. ECC is in the state of regulated monopoly. Still we have to think of one competitor for at least two years. ECC will expect more competitors after the third quarter of 2006. So competition will be severe.

**ECC plan is based on:**
- Competing by good quality and service
- Competing by reasonable prices
During the years 2005 and 2006 the company could acquire this good quality and service by applying standards gained by Etisalat of UAE. This long experience in good communication products is enough. However after the second year the company will have its own quality standard marketing research findings established in the first year will provide the company with the information about the Saudi market. Services will be rendered in a better manner month after month. Good quality and service will become the rule and not the exception during the third year.

**Pricing strategy**

Competition by reasonable prices is one of the keys of success. Whenever costs of providing the service is low unit prices will be low. The company plan to make costs less will depend on its ability to establish a system of buying material and equipment using the most recent advanced techniques of procurement, stock control and storekeeping. This action will start from the year 2005. Employment of highly educated and experience people in the profession of operations and purchasing will ensure both buying the right requirements in the right quantities with right price and at the right time. Cost reduction in purchasing added to decreased costs of operation will lead to a lower cost that will assist in setting reasonable prices to compete.

**Service Rates Projection:**

Rates for the five years are expected to be as follows:-

<table>
<thead>
<tr>
<th></th>
<th>Year 2005</th>
<th>Year 2006</th>
<th>Year 2007</th>
<th>Year 2008</th>
<th>Year 2009</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Prepaid (SR)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subscriptions</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>On-net off net</td>
<td>0.70</td>
<td>0.70</td>
<td>0.65</td>
<td>0.65</td>
<td>0.65</td>
</tr>
<tr>
<td>National (minute)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>International (minute)</td>
<td>2.40</td>
<td>2.30</td>
<td>2.20</td>
<td>2.00</td>
<td>2.00</td>
</tr>
<tr>
<td><strong>Post Paid (SR)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subscriptions</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>On-net off net</td>
<td>0.30</td>
<td>0.30</td>
<td>0.30</td>
<td>0.28</td>
<td>0.26</td>
</tr>
<tr>
<td>National (minute)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>International (minute)</td>
<td>2.50</td>
<td>2.50</td>
<td>2.30</td>
<td>2.30</td>
<td>2.20</td>
</tr>
</tbody>
</table>

*Source: Interview with EEC officials and informal (Business Plan)*

**Mobily Challenges**

There are several challenges that are facing EEC the most important four are the following:
• Saudi Arabia geographically are so big and to deliver the services for all region need a lot of construction for towers and such capital investment might hinder the business plan.

• There competitor in Saudi Market is established company supported by government for last 30 years so actually they compete with the fixed line in addition to al Jawal (STC)

• The possibility of new competitors entrance during 2006 and 2007 is so high and there might be price ware impacting EEC business plan.

• The Saudi mobile number is not transferable to mobily network so a lot of potential customers reluctant to switch to mobily to avoid contacts info lost

**Section B:**
**Teaching Note**

_Ethad Etisalat Company (Mobily) Penetrating Saudi Arabia_

_Synopsis_

_The case focuses on the efforts of Mobily as it strives to expand its business in the Kingdom of Saudi Arabia. Mobily is an unusual company in that it acts essentially as a subsidiary of UAE-based EEC, although it is 100 percent independent. Mobily officially launched its services May 2004. Mobily provided services to 30 cities, including national roaming, voice mail, news and data downloads, sms, mms, missed calls notification, wap and internet browsing._

_Objectives_

_The mobily case is best used to discuss generic strategies in foreign market. Ideally, it should be used after discussions of Global strategies. It provides an excellent vehicle for differentiating between core competencies and geographic competencies. As such, it highlights the opportunities for companies like EEC of UAE to globalize without necessarily owning assets._

_Teaching approach_

_I recommend using mobily case in a single 75 minute business policy class. An appropriate classroom schedule is:_

*50 minutes – classroom discussion of the case*

*25 minutes – wrap up & short lecture*

_Question # 1 what contributed to the success of mobily?*
A number of factors contributed to mobily's success. The most important factors are:

# Location decisions
# getting product right
# Local service and infrastructure
# Hard work

Question #2 what is your evaluation of the relationship between Mobily and STC? What are the risks in this relationship?

This is a critical discussion that is worth spending some quality time on in the class. The students through information in the class and own experience can highlight the advantages and disadvantages of such relationship and draw a future perspective on what will happen if or when a "needs" imbalance develops? In this case, there is a much higher likelihood that Mobily will over time grow more independently of STC.
Deducing Ibn Taymiyah's Opinion Regarding Contemporary Bank Finance

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Abstract: The contemporary scholars have adopted the resolution of the Islamic Law Research Council which was arrived at during their 1965 convention. The Council's decision was to adopt the opinion of Ibn Taymiyah that the affective cause for prohibiting interest in gold and silver is that it "serves as an absolute monetary entity in the market." On that basis, the resolution declared, the prohibition of interest applies to paper currency. The question that needs to be asked is to what extent contemporary Islamic economics conforms to these necessary consequences of adopting Ibn Taymiyah's opinion? The present paper will explore this matter and answer the central question:

Is the depreciation of purchasing power something intrinsic to the nature of paper currency or something external to it? And if it is part of its nature, what are the implications?

Introduction

The Qur’ân declares interest to be unlawful, but it speaks about interest in general terms without going into detail. The particulars are to be found in the traditions of the Prophet Muhammad – the Sunnah – where the Prophet says: "Gold for gold, silver for silver, wheat for wheat, barley for barley, dates for dates, salt for salt – when these are traded, it must be like for like, hand-to-hand. If any of these items are traded for other than their own kind, then do so in any way that you see fit, as long as it is hand-to-hand." [Sahîh Muslim]

Scholars looking at this prophetic tradition have differed as to which forms of wealth are subject to the prohibition of interest. There are essentially four opinions on the matter. According to three of those opinions, today's paper currency is not subject to the prohibition against interest.

The first school of thought is that of the Zâhirî (literalist) scholars who limit the prohibition to the six types of wealth expressly mentioned by the text. No other forms of wealth are prohibited. This conforms with their literalist methodology that rejects the use of analogy to extend the legal rulings of a text beyond what is explicitly stated.

The second school of thought regarding this matter is that of the four canonical schools of Islamic Law. Their approach is to look at the face value of the text to determine the extent of its ruling, without factoring in any consideration of intent. These scholars take the six forms of wealth mentioned in the text and then extend its ruling, by way of analogy, to any other forms of wealth that bear a superficial resemblance to those six.
They do not explore the reason why interest is prohibited for those six forms of wealth. Sheikh Ibn Sa`dî and Sheikh Hasan Ayyûb are among the contemporary scholars who concur with this view.

The third school of thought is that of certain scholars of hadîth (prophetic traditions). Their approach is to extend a text's ruling to other things by way of analogy only when a clear and precise effective cause for that ruling can be discerned. In the event that a strong effective cause cannot be discerned and where there is considerable scholarly disagreement regarding what that cause might be – as is the case with the effective cause for prohibiting interest in those six types of wealth – then the exercise of analogous reasoning is prohibited and the ruling is restricted to what is expressly mentioned in the text itself. This is the approach of al-San`ânî among the hadîth scholars as well as that of the Hanbalî jurist Ibn `Aqîl.

Finally, there is the school of thought espoused by Ibn Taymiyah and then by his student Ibn Qayyim al-Jawziyyah, which in turn has been adopted by the vast majority of contemporary scholars. (This fourth approach can also be discerned as an alternative viewpoint for some of the scholars of the four canonical legal schools.) Their approach is to look at the intent of text in applying the ruling to the six forms of wealth instead of looking at the superficial characteristics of those six forms. They then extend the ruling by way of analogy to other forms of wealth on the strength of the intent that they have discerned.

Contemporary scholars have adopted the resolution of the Islamic Law Research Council which was arrived at during their 1965 convention. The Council's decision was to adopt the opinion of Ibn Taymiyah that the effective cause for prohibiting interest in gold and silver is that it "serves as an absolute monetary entity in the market." On that basis, the resolution declared, the prohibition of interest applies to paper currency.

What this means is that the school of thought upon which contemporary Islamic economics is based is that of Ibn Taymiyah. This, in turn, has two consequences.

The first is that the methodological basis for deriving the ruling is one of looking at the intent behind it, since this is the essence and logic of Ibn Tamiyah's approach to law.

The second is that the effective cause for prohibiting interest in the trade of gold and silver – which is that it serves as an absolute monetary entity – must remain true for paper currency according to the conditions Ibn Taymiyah set to determine the presence of that effective cause.

The question that needs to be asked is to what extent contemporary Islamic economics conforms to these necessary consequences of adopting Ibn Taymiyah's opinion? The present paper will explore this matter and answer the central question:
Is the depreciation of purchasing power something intrinsic to the nature of paper currency or something external to it? And if it is part of its nature, what are the implications?

The abolition of the gold standard in 1973 led to paper currency losing the ability to be a store of value. Declining purchasing power became an intrinsic characteristic of money rather than something occasionally experienced by it. This violates a condition with respect to something serving as an absolute monetary entity, a condition set forth by Ibn Taymiyah and the scholars and economists who follow his approach. The condition is that the commodity serving as a monetary entity must be of a relatively stable value so that it can serve as a store of value.

Ibn Taymiyah writes:

Minted gold and silver serve as the price for all that which can be bought and sold. A price is the standard of value by which the value of wealth is assessed. Therefore, that which serves as a price must itself be clearly and precisely defined in value, subject to neither increase nor decrease.

Alan Greenspan, former Chairman of the United States Federal Reserve, writes:

In the absence of the gold standard, there is no way to protect savings from confiscation through inflation. There is no safe store of value.

This paper discusses, essentially, the conditions set forth by Ibn Taymiyah for a commodity to serve as an absolute monetary entity, this being the basis upon which contemporary Islamic scholars have applied the prohibition of trade interest (ribâ al-buyû`) to paper currency. This paper will employ two approaches in discussing these conditions. One will be an economic analysis supported by historical and statistical economics and the statements of leading experts in the field of finance. It will also explore the opinions of Islamic legal scholars who have explored the same issues by analyzing various prophetic traditions form an economic angle and who have arrived at the conclusion that paper currency since 1973 does not fulfill the conditions of a commodity which can serve as an absolute monetary entity. This is the same conclusion that this present research arrives at. The idea that today's paper currency is subject to the prohibition of trade interest is a new one that has no precedent in the opinions of the Pious Predecessors.

Nevertheless, this view of paper currency is the one that enjoys wide acceptance today. It takes Ibn Taymiyah's position as its basis, but does so by ignoring the conditions that he asserts for a commodity to be regarded as an absolute monetary instrument. This is problematic, since the necessity of these conditions being met is acknowledged by all those who agree with Ibn Taymiyah.

There are a number of consequences to our conclusion that paper currency does not fulfill the conditions of being an absolute monetary entity. The most important of these is that...
currency can be traded in unequal amounts, both on the spot and at a later date, as concluded by Dr. al-Ashqar. This removed many of the obstacles and difficulties that Islamic economists have imposed upon the money market and upon bank deposits.

Literature Review

The Conditions for an Absolute Monetary Entity

I personally accept the view which is widely held today that the prohibition of interest in the trade of gold and silver is due to their being absolute monetary entities. This is an alternative view narrated from Mālik, Abū Hanîfah, and Ahmad b. Hanbal, the respective founders of their schools of thought. It is the view which has been embraced by nearly all contemporary Islamic scholars. However, I also hold the view that the ruling can only be extended to commodities other than gold and silver if the conditions for being an absolute monetary entity are indeed realized by those commodities.

These conditions have been elaborated by Ibn Taymiyah and his student Ibn Qayyim al-Jawziyyah, and have been acknowledged by all thinking people, Islamic scholars, and economists including Alan Greenspan, one of today's foremost economists and former chairman of the Federal Reserve.

There are a number of these conditions, which Ibn Taymiyah manages to summarize as three, when he says:

Minted gold and silver serve as the price for all that which can be bought and sold. A price is the standard of value by which the value of wealth is assessed. Therefore, that which serves as a price must itself be clearly and precisely defined in value, subject to neither increase nor decrease.

He also says:

This can only be realized when the value of the commodity remains at a constant state, neither rising nor falling in value.

His student, Ibn Qayyim al-Jawziyyah says:

Minted gold and silver serve as the price for all that which can be bought and sold. A price is the standard of value by which the value of wealth is assessed. If the price itself is subject to rising and falling in the way the prices of trade goods rise and fall, we are left with nothing that can be used to assess the price of goods, since everything is a trade item. There is an indispensable need for people to have a standard of pricing for everything they buy and sell. This requires that prices are of a known value, and this can only take place when that which is used to express

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2 Ibn Taymiyah, Tafsîr Āyât Ushkilat ‘ala Kathîr mi al-‘Ulamâ’ (589).
3 Tafsîr Āyât Ushkilat ‘ala Kathîr mi al-‘Ulamâ’ (589).
those prices remains constant in itself and is not assessed against anything else. Otherwise, it would in turn be another trade item whose price fluctuates in the market. As a consequence, all market activities would be severely compromised, and people would suffer from economic stagnation and great hardship. We have indeed seen this in cases where people have adopted base-metal coinage as money and suffered great difficulties and injustices on account of it.

Ibn Khaldûn writes:

God created the two precious metals, gold and silver, to be the price for everything else of value. They serve as the measure of value for all other forms of wealth. They are the store of value for times of need. When other commodities are adopted on occasion, it is only on the strength of the intention to attain gold and silver, due to what other commodities are subject to of price fluctuations to which gold and silver are immune.

He goes further to explain that the minting of gold and silver money is only to give it a distinct identity as money and to safeguard it against fraud. When money is minted, people can trust it and use it as a standard and measure, and they can easily keep account of the money they possess.

Alan Greenspan says:

What medium of exchange will be acceptable to all participants in an economy is not determined arbitrarily. First, the medium of exchange should be durable. In a primitive society of meager wealth, wheat might be sufficiently durable to serve as a medium, since all exchanges would occur only during and immediately after the harvest, leaving no value-surplus to store. But where store-of-value considerations are important, as they are in richer, more civilized societies, the medium of exchange must be a durable commodity, usually a metal. A metal is generally chosen because it is homogeneous and divisible: every unit is the same as every other and it can be blended or formed in any quantity. Precious jewels, for example, are neither homogeneous nor divisible. More important, the commodity chosen as a medium must be a luxury. Human desires for luxuries are unlimited and, therefore, luxury goods are always in demand and will always be acceptable. Wheat is a luxury in underfed civilizations, but not in a prosperous society. Cigarettes ordinarily would not serve as money, but they did in post-World War II Europe where they were considered a luxury. The term "luxury good" implies scarcity and high unit value. Having a high unit value, such a good is easily portable; for instance, an ounce of gold is worth a half-ton of pig iron.

In the early stages of a developing money economy, several media of exchange might be used, since a wide variety of commodities would fulfill the foregoing conditions. However, one of the commodities will gradually displace all others, by being more widely acceptable. Preferences on what to hold as a store of value, will

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5 Greenspan, "Gold and Economic Freedom".
shift to the most widely acceptable commodity, which, in turn, will make it still more acceptable. The shift is progressive until that commodity becomes the sole medium of exchange. The use of a single medium is highly advantageous for the same reasons that a money economy is superior to a barter economy: it makes exchanges possible on an incalculably wider scale.

Whether the single medium is gold, silver, seashells, cattle, or tobacco is optional, depending on the context and development of a given economy. In fact, all have been employed, at various times, as media of exchange. Even in the present century, two major commodities, gold and silver, have been used as international media of exchange, with gold becoming the predominant one. Gold, having both artistic and functional uses and being relatively scarce, has significant advantages over all other media of exchange.

According to Ibn Taymiyah, Ibn Qayyim al-Jawiyah, and all the contemporary thinkers who hold the same point of view, the following conditions must be met for something to be an absolute monetary entity:

1. The commodity must be something scarce and a luxury item. Things like air, water, and soil cannot serve as money. The commodity must be extremely difficult to produce or manufacture.

For this reason, Greenspan criticizes the abolition of the gold standard, saying:  

The abandonment of the gold standard made it possible for the welfare statists to use the banking system as a means to an unlimited expansion of credit.

2. It must be consistent in its value so that it can serve as a standard for measuring the relative value of goods and services. This is why precious gems cannot be used as money, since the value of individual gemstones can differ greatly and the stones cannot be divided into smaller units. Greenspan says:

Even though the units of exchange (the dollar, the pound, the franc, etc.) differ from country to country, when all are defined in terms of gold the economies of the different countries act as one-so long as there are no restraints on trade or on the movement of capital. Credit, interest rates, and prices tend to follow similar patterns in all countries.

3. The final and most important condition is that the commodity can serve as a safe store of value. Greenspan, writing in 1967 to warn against the growing trend to abolish the gold standard, says:

6 Greenspan, "Gold and Economic Freedom".
7 Greenspan, "Gold and Economic Freedom".
8 Greenspan, "Gold and Economic Freedom".

In the absence of the gold standard, there is no way to protect savings from confiscation through inflation. There is no safe store of value.

This can be compared to what he says elsewhere in that paper:

…several media of exchange might be used, since a wide variety of commodities would fulfill the foregoing conditions. However, one of the commodities will gradually displace all others, by being more widely acceptable. Preferences on what to hold as a store of value, will shift to the most widely acceptable commodity, which, in turn, will make it still more acceptable.

The Origin of the Ruling That the Prohibition of Interest Applies to Today's Paper Currency

When banknotes were first introduced, scholars disagreed considerably about whether they were subject to the Islamic prohibition against interest. Then the Islamic Law Research Council in Cairo issued a resolution in May 1965 that represented the consensus of one hundred fifty scholars. They concluded that the prohibition of interest applies to both base-metal coinage and to paper currency.

This has been the prevailing view up to the present day, in spite of the fact the conference where the resolution was issued took place eight years prior to the abolition of the gold standard in 1973. At that time, which was more than forty years ago, that ruling was a strong one and one that made a lot of sense.

Then in 1975, the Saudi Council of Senior Scholars issued a resolution supported by the majority that the prohibition of interest applies to paper currency. This also took place before the consequences of the collapse of the Bretton Woods system and the abandonment of the gold standard had made themselves apparent. We must understand that this was the first time in history the gold standard had been permanently and absolutely abolished. Before, it had only been temporarily suspended under certain circumstances, like during war.

The time has come to seriously reconsider the matter. The Islamic Law Council has recently reviewed this topic during its third and fifth sessions amid considerable disagreement and dissention. In the end, the Council issued resolutions upholding the ruling that the prohibition of interest applies to paper currency.

These deliberations of the Islamic Law Council were prompted by the plummeting values suffered by certain currencies, including the Lebanese Lira, the Syrian Lira, and The Sudanese Pound. The sessions concluded that the depreciation suffered by these currencies were isolated events contingent on the circumstances faced by those countries at those precise times. Because of this, they proposed remedies like tying loans to the dollar and other impractical makeshift solutions.
What they failed to investigate was whether all currencies since the abolition of the gold standard – the dollar included – were subject to a necessary and continual medium and long term depreciation in their purchasing power. In fact, it needs to be determined whether this was not the very reason for the world abolishing the gold standard in the first place between the years 1971 and 1973.

**Findings and Analysis**
In order for us to be able to properly reconsider and re-evaluate the extent to which paper money fulfills the conditions of an absolute monetary entity, we need to briefly trace the historical origins of today's paper money.

We need to distinguish between two historical phases with regard to paper currency, the first of these being from the end of World War Two until 1973, and the second being from 1973 to the present.

After the Allied victory at the end of World War Two, with the United States leading the way, the Allied Powers convened a conference in Bretton Woods, New Hampshire in July 1944. The meeting resulted in the signing of the Breton Woods Agreements, in which the participating countries agreed to peg their currencies to the US dollar at a par value. In turn, the United States agreed to link the value of the dollar to gold at the guaranteed rate of $35 per ounce of gold.

It can be noted that during this period of time, all of the world's currencies recognized by Western markets were fixed to the dollar which was in turn pegged to gold. The prevalent notion that all currencies are subject to the gold standard was not exactly accurate, even back then, though it was true to a reasonable extent. This is what Sheikh Muhammad b. Ibrahim, the Mufti of Saudi Arabia at that time, meant when he described paper currency as "money in a relative sense" about which, regarding matters of Islamic Law, it is nevertheless "better to approach conservatively."

Under the Bretton Woods system, each nation issued money in proportion to that amount of gold that its domestic production of goods and services could potentially bring in. It was not necessary for there to be any actual gold. The promise of convertibility into gold was enough.

It is possible to argue that, under this system up to 1973, the conditions for an absolute monetary entity were still being fulfilled by paper currency. Currency values were stable to a great extent, and when fluctuations occurred, generally depreciations in value, they were preceded by some sort of announcement. Trade in currencies had not reached anything like the level that we see today.

After Bretton Woods, and in the wake of World War Two, the United States printed millions of dollars both for domestic development and for lending to Western Europe. America used these dollars, which were either printed on paper or merely recorded as numbers in various accounts, to purchase the raw materials and oil that it needed, as well as services from all corners of the world. To prevent the printing of all this money from
resulting in inflation, the Federal Reserve Bank removed the money from circulation through the sale of US bonds. Private individuals, banks, and governments would hold these bonds which paid interest and which could be exchanged for dollars at any time – dollars which in turn were pegged to gold at $35 an ounce. Holding these dollar bonds was better than holding gold because of the interest that they paid. Holding gold, by contrast, yielded no returns and was moreover fixed in value against the dollar. Nevertheless, gold outflows continued to the extent that 3/4 of the total gold reserve was lost between 1944 and 1971.

Table 1:
US Gold Reserves between 1944 and 2004 (millions of ounces)

After a number of years, the United States began to feel – as it still does – the pressure of its dollar obligations acutely and realized that it was unable to fulfill its Bretton Woods commitment to convert upon demand every $35 to an ounce of gold. The national banks of the various countries, realizing that though America held the world's largest gold reserve it could not meet its commitments, froze their gold accounts, and actual conversions from dollars into gold came to a virtual standstill. Then in 1971, the United States adjusted the valuation of gold to the dollar, pegging it at first 38 then at 42 dollars to the ounce. In 1973, President Richard Nixon announced that the United States will no longer be committed to converting dollars into gold. In a short time, the price of gold climbed to $200 an ounce.

Those who now possess dollars do not demand from the United States any real commodities or services in lieu of them. Instead, they hold these monetary instruments in the central and commercial banks where they earn a modest rate interest which the United States government can easily cover by printing more money.
As this table of the interest rate paid by the United States government illustrates, the relative fluctuations in the interest rate correlates very closely with the inflation rate, especially over the long term. This means that the United States does not pay out genuine interest on its heavy debt burden. Rather, it gives in interest what corresponds to the devaluation of the dollar's purchasing power. As for the sharp rise we see in the inflation rate in 1951, I believe this to be on account of the Korean War.

**Stability of the price of gold from 1833 until the abolition of the gold standard in 1971**

Table Two, below, illustrates how the price of gold remained not only stable but relatively constant from 1833 until the abolition of the gold standard in 1971, after which it jumped to roughly six times its price in its dollar value.

<table>
<thead>
<tr>
<th>Year</th>
<th>Price of Gold</th>
</tr>
</thead>
<tbody>
<tr>
<td>1850</td>
<td>100</td>
</tr>
<tr>
<td>1875</td>
<td>150</td>
</tr>
<tr>
<td>1900</td>
<td>200</td>
</tr>
<tr>
<td>1925</td>
<td>250</td>
</tr>
<tr>
<td>1950</td>
<td>500</td>
</tr>
<tr>
<td>1975</td>
<td>3000</td>
</tr>
</tbody>
</table>

We can see how the price of gold remained stable up to World War One, after which its price went up in response to the number of dollars that entered the market. Then it rose sharply after 1973 until it represented the true value of the dollar in 1975. The price of gold then went on to fluctuate widely in response to various political and economic policies that were adopted by the United States government.

We can see this repeatedly whenever the value of the dollar drops and the United States faces a political crisis, like during the Iranian hostage crisis of 1980 which occurred during a period of high inflation, or in other words a period of decline in the dollar's purchasing power. At this time, the price of gold rose to $800 an ounce (which would correspond to $1600 an ounce in today's dollars).

In 1980, investors were still getting used to the idea of money that was not backed by gold. Their confidence in America's promises to back the dollar was less than it is today. Also, at that time the Eastern Bloc still existed. The sharp rise in the price of gold to what
in today's prices would be equivalent to $1600 led to a renewed call to return to the gold standard. This prompted President Ronald Reagan to appoint the economic radical Alan Greenspan as the Chairman of the Federal Reserve, a man who was vigorously opposed to the abolition of the gold standard. Greenspan was able to restore confidence in the dollar which would remain high for the next fifteen years.

Establishing That a Continual Decline in Purchasing Power is an Intrinsic Quality of Today's Paper Currency

Since the dollar is now the primary currency by which other currencies are guaranteed – in other words, it acts to back up other currencies as the gold standard used to do – it behooves us to look at how well the dollar itself maintains its purchasing power in the market without the United States government having to print more and more dollars to meet market demands.

Table 3:
The Inflation Rate, Dollar Availability, and Income

3.1 The Inflation Rate
3.2 Dollars in Circulation
3.3 Wage Rate
Since the United States dollar, and not gold, is what backs other currencies, it is logical for us to consider how well the dollar serves the purpose of being a store of value. These tables show us that prices and wages remained relatively stable from the 1940s until 1971, in spite of the wars that the United States participated in, like Korea and Vietnam. This is because the United States was still under obligation to convert dollars into gold. This meant that its issuing of dollars, though in excess of its actual gold reserves, was nevertheless still constrained. This was a period of nearly thirty years of relative stability for the dollar. By contrast, during the subsequent period of roughly thirty years (1971-2005) depreciation of the dollar's purchasing power became the norm.

In the modern economic regime, the dollar has replaced the gold standard. Instead of gold mines in South Africa and California, we have the Federal Reserve Bank in Washington. The difference between them is simple. Gold is difficult and costly to produce. More importantly, its supply is limited. The dollar, on the other hand, is merely a number in a computer, subject to the spending whims of the president.

Table Four tells the story. Going back roughly 250 years ago to 1750 and looking at the British Pound, we see relative price stability until 1938. It took nearly two centuries for prices to triple. After World War Two and the Bretton Woods Agreements, when America took over the world's economic leadership from Britain and the gold standard was supplanted, prices increased to forty times their level. It started off slowly after World War Two, with the increase being due to the introduction of dollars into the economy in excess of need. However, the situation was still reasonable until the gold standard was abolished altogether. Then the dollar's purchasing power depreciated by multiples in the course of half a human lifetime. This, no doubt, negates for the dollar the quality of being a store of value.
Turning our attentions to Table Five and its accompanying chart, we can see that the depreciation of a currency's purchasing power is something intrinsic to paper money after the abolition of the gold standard. This applies to the currencies that are used to back others, including those of Japan and Germany who have fought against the circulation of their currencies in order to keep their products competitive. The timeframe under consideration is from 1980-1999, in order to avoid the allegation that inflation after 1973 was due to rising petrol costs. This timeframe also avoids the affects of the Euro's adoption since 1999, the September 11 tragedies of 2001, and the war in Iraq. Furthermore, twenty years is the timeframe for mid-term investments.

Table 5:

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Table 4:
**Composite Price Index 1750-2003 Based on 1974 British Pounds Sterling**

Composite Price Index 1750 to 2003, January 1974 = 100 (linear scale)

Turning our attentions to Table Five and its accompanying chart, we can see that the depreciation of a currency's purchasing power is something intrinsic to paper money after the abolition of the gold standard. This applies to the currencies that are used to back others, including those of Japan and Germany who have fought against the circulation of their currencies in order to keep their products competitive. The timeframe under consideration is from 1980-1999, in order to avoid the allegation that inflation after 1973 was due to rising petrol costs. This timeframe also avoids the affects of the Euro's adoption since 1999, the September 11 tragedies of 2001, and the war in Iraq. Furthermore, twenty years is the timeframe for mid-term investments.

Table 5:
The specious nature of modern currencies, seen here, is aptly described by Alan Greenspan.⁹

Under a gold standard, the amount of credit that an economy can support is determined by the economy's tangible assets, since every credit instrument is ultimately a claim on some tangible asset. But government bonds are not backed by tangible wealth, only by the government's promise to pay out of future tax revenues, and cannot easily be absorbed by the financial markets. A large volume of new government bonds can be sold to the public only at progressively higher interest rates. Thus, government deficit spending under a gold standard is severely limited.

⁹ Greenspan, "Gold and Economic Freedom".

The abandonment of the gold standard made it possible for the welfare statists to use the banking system as a means to an unlimited expansion of credit. They have created paper reserves in the form of government bonds which-through a complex series of steps-the banks accept in place of tangible assets and treat as if they were an actual deposit, i.e., as the equivalent of what was formerly a deposit of gold. The holder of a government bond or of a bank deposit created by paper reserves believes that he has a valid claim on a real asset. But the fact is that there are now more claims outstanding than real assets.

Market Prices of the Currencies of the Ten Leading Industrial Nations from 1980-1999 with Respect to Purchasing Power (1980 adjusted values)

<table>
<thead>
<tr>
<th>Year</th>
<th>Japan</th>
<th>Germany</th>
<th>Switzerland</th>
<th>Austria</th>
<th>America</th>
<th>France</th>
<th>Canada</th>
<th>Britain</th>
<th>Spain</th>
<th>Italy</th>
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<td>1</td>
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<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
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<td>1.06</td>
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<td>1.12</td>
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<td>2.48</td>
<td>3.45</td>
<td>3.52</td>
</tr>
</tbody>
</table>
Discussing the Assumptions Underlying the View that Paper Currencies are Independent Monetary Entities

Assumption 1: Governments will exercise the utmost responsibility in issuing currency in order to preserve the currency's value and protect it from depreciation.

The idea that a country will restrict itself to issuing the correct supply of banknotes so that the purchasing power of its currency will not depreciate is a purely philosophical notion that is not reflected in reality. A currency will either be free-floating or be pegged to another currency. With respect to a pegged currency, its issuing authority has no control over increasing or decreasing its purchasing power, since this is wholly dependent on the other currency that it is pegged to. As for floating currencies like the US dollar, the countries that issue them continue to increase their supply ear after year, as we have seen in the previous set of tables.

Assumption 2: Banknotes are a safe store of value.

Alan Greenspan, while discussing the importance of the gold standard, writes: \(^{10}\)

> The law of supply and demand is not to be conned. As the supply of money (of claims) increases relative to the supply of tangible assets in the economy, prices must eventually rise. Thus the earnings saved by the productive members of the society lose value in terms of goods. When the economy's books are finally balanced, one finds that this loss in value represents the goods purchased by the government for welfare or other purposes with the money proceeds of the government bonds financed by bank credit expansion.

> In the absence of the gold standard, there is no way to protect savings from confiscation through inflation. There is no safe store of value.

The truth of this should be evident from tables that we have previously discussed.

Dr. Muhammad Sulaymân al-Ashqar has written an excellent research paper entitled *Money and Price Fluctuation* which he submitted to the Islamic Law Council of Kuwait in 1989. In it, he establishes through a study of the prophetic traditions that the value of gold has remained stable since the time of the Prophet up until today.

Assumption 3: The currency is not itself a trade item.

It is necessary that the currency is not itself an item of trade. Ibn Taymiyah writes:

\(^{10}\) Greenspan, "Gold and Economic Freedom".
If trade is permitted in what is used as the standard of price, like allowing the sale of minted silver coins for other minted silver coins at a later date, then the coins themselves become merchandise and cease to be a means of exchange.

Trading in something makes that thing merchandise. Sheikh `Abd Allah b. Manî` says:

People face confusion and uncertainty in their commercial transactions when gold and silver are bought and sold like merchandise and consequently become subject to supply-and-demand price fluctuations and extreme scarcity. This undermines the ability of gold and silver to function as money.

Trade in currency is the reality of today's monetary system. **It is necessary that whatever Islamic legal rulings are issued regarding modern currencies are based on that reality and not on some non-existent ideal.**

The currency market developed rapidly after the abolition of the gold standard and it soon became the international policeman that keeps governments from issuing currency above demand. If it were not for this trade, countries could issue as much currency as they liked without risking exposure until much later. The currency markets keep the price of currency in check through the law of supply-and-demand.

Our purpose here is that since it is presently possible or an unlimited supply of currency to be issued, some regulatory mechanism is needed to, at least, prevent irresponsible behavior and represent the true short-term value of that currency. The foreign exchange market carries out this function. Without it, countries would be able to issue as much currency as they like for a relatively long period of time without being detected.

This makes patently clear the difference between a monetary medium which has limits and one that does not. When a gold or silver standard is in place, a country cannot issue currency without possessing the gold or silver to back it up. As for today's banknotes, countries can issue as much of them as they see fit, leading to a depreciation of their value as a consequence.

How is it that the foreign exchange market is necessary for keeping currency prices in check? The teachings of Islam and of common sense tell us that if these banknotes had real value, the trade in them would be harmful. If currencies had stable values, there would be no trade in currencies. This is why gold for gold trading is proscribed, since the value of gold is stable.

**Some Views from Contemporary Islamic Scholarship**

Dr. Muhammad Sulaymân al-Ashqar, in his 1989 paper, determines that the analogy between paper currency and gold – by which scholars prohibit the trade of paper currency with interest, and which is based on the assumption that paper currency shares the
effective cause for the ruling (that of being an absolute monetary entity) – is a false analogy. He writes:  

Maintaining the present stance poses no difficulties for spot trading in currencies. However, whenever payment is deferred – and regardless of whether the transaction in question is a sale, a loan, a lease agreement, a partnership, or even a dowry – serious problems arise. The harm from these transactions is suffered by the seller or the lender. The seller waiting for his payment suffers from the depreciation in the value of the sale price. However, he is able to add to the deferred price whatever amount he determines will cover for that depreciation. This is not the case for the lender. As long as we hold the view that interest is prohibited with respect to paper currency, he has no way to protect himself from the affects of inflation. This means that, especially with long-term loans, the lender receives back only a small portion of the initial value that he loaned.

Let us assume that a Muslim state that adheres to Islamic Law in its dealings loans another country (Muslim or non-Muslim) a loan of $100 million. If the purchasing power of the dollar depreciates at a rate of 6% annually, the lending state suffers a loss of $6 million dollars in the first year, six percent of what remains in the second, and likewise for every year until the loan is paid back.

Losses of this nature will be suffered primarily by those who are firm in their Islamic faith. Therefore, the analogy with gold is a false analogy. It is my opinion that applying the prohibition of interest to paper currency on the strength of that analogy is incorrect. This becomes clear when we understand that economists describe gold as possessing three unique characteristics that make it what Hanafi scholars describe as "a price in and of itself". Paper currency differs from gold in three of these characteristics. The three characteristics are as follows:

1. It acts as a standard of value, since it is fixed in its own value over historical time. Paper currency, by contrast, is not suited to serve as a standard of value except in spot transactions.

2. Gold serves as a store of value on the strength of its history. Paper currency is a store of value, but one that constantly depreciates over time.

3. Gold is a medium of exchange. This is the one characteristic that paper currency shares with it.

Due to these differences between gold and paper currency that make the effective cause for the prohibition of interest not fully realized in paper currency, we believe that there is no justification to uphold the analogy between the two in determining Islamic legal rulings.

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11 Dr. Muhammad Sulayman al-Ashqar, "Money and Price Fluctuation".
The following is the text of Dr. `Abd al-Rahmân Yusrî Ahmad's statement on this question.  

Muslim jurists in ages past used different approaches to address the issue of price fluctuation in base-metal currencies, which were essentially credit or fiat money. We do not find in their discussions anything that would suggest there were any tangible and constant dangers posed by this fluctuation. The monetary regimes of the past were essentially based on gold and silver, with base-metal coinage playing only a secondary role. This was the case until rather recently when reliance on base metals increased and the counterfeiting of gold and silver coins became rampant.

We cannot discern that any of the older generation of Islamic jurists were able to anticipate that the monetary regime would become one based exclusively on representative money or that the phenomenon of escalating prices and the depreciation of the value of those representative currencies would become the invariable norm.

We find where al-Maqrîzî, the famous Muslim historian, discusses the phenomenon of escalating prices in connection with severe depreciation in the value of base-metal coinage, which was at times so severe that it led people to abandon those currencies and refuse to deal with them. Nevertheless, like his contemporaries, he could not conceive of such a situation becoming the norm or the possibility of dispensing with gold and silver altogether.

In today's monetary regimes, all currencies are fiat currencies. All countries face the reality of inflation to varying degrees. Muslim countries are no exception. Indeed, some of them have suffered the hardest and continue to do so.

The reality is that our scholars' insistence on regarding paper currency like gold and silver in determining Islamic legal rulings stems from their fear that otherwise interest will be practiced with these currencies and people will abandon paying Zakâh on their savings. This fear is a consequence of some jurists wanting to compare paper currency with base metal coinage, which scholars of the Shâfi`î school of law have never regarded as money. They allowed the exchange of one coin for two. We have seen some contemporary scholars who wanted to compare paper currency with trade goods and consequently make the buying and selling of currency permissible and exempt it from the specific Zakâh levied on gold and silver…

However, the fears of those who wished to avoid such consequences have brought about even more serious consequences. Inflation is a permanent and undeniable fact of our economic lives, and it is a serious mistake for us to pretend that paper currency is a true substitute for gold and silver with the same Islamic legal rulings.

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being applicable. We should retract that view, and do so not to defend someone’s judicial opinion or to bolster some policy, but rather to rest our hands upon the truth of the matter and build our laws on a sound foundation.

The difference between trade interest (ribâ al-buyû`) and interest on a loan

Interest on a loan is possible for any kind of wealth, regardless of whether we are speaking about the six forms of wealth mentioned in the hadîth or any other form of wealth. There is unanimous consensus in Islamic Law that this type of interest is prohibited.

In this paper, we are not investigating the question of interest on a loan.

Trade interest, on the other hand, is restricted to the six types of wealth mentioned in the prophetic traditions and to any other wealth that it applies to by way of analogy. This is the issue that we are exploring.

To return to an explanation of interest on a loan, it has two manifestations, both of which relate to payments deferred to a later time.

The first of these is an interest rate that is specified at the time the loan is taken. The second type of interest on a loan is when interest is later added to an existing sale with a deferred payment in exchange for the seller extending the time period before payment is due. This was the type of interest that was prevalent in Arabia before the advent of Islam.

As for trade interest, it occurs in the exchange of like commodities, like the sale of one camel for three camels or one ton of pig iron for two tons, or one dollar for three dollars. However, this type of interest is only considered for the six forms of wealth mentioned in the prophetic tradition and what takes the same ruling by way of analogy.

The prophet said: "Gold for gold, silver for silver, wheat for wheat, barley for barley, dates for dates, salt for salt – when these are traded, it must be like for like, hand-to-hand. If any of these items are traded for other than their own kind, then do so in any way that you see fit, as long as it is hand-to-hand." [Sahîh Muslim]

Trade interest is not prohibited for wealth that is neither addressed by this tradition directly nor by way of analogy.

There are two types of trade interest. The first is ribâ al-fadl which is an increase in spot trading, and the second is ribâ al-nasî’ah which is an increase with a delay in payment. Interest with a delay of payment is prohibited for its own sake. Interest is prohibited in on the spot trading as a preventative measure.
II – Solutions for money lending in consideration of paper currency not being subject to the prohibition of trade interest

We have hopefully made it clear that the effective cause for the prohibition of trade interest for gold and silver – which is their being absolute monetary entities – is not realized for paper currency.

We have also shown that according to the four canonical schools of Islamic Law which do not regard the attribute of "absolute monetary entity" to be the effective cause for the prohibition of trade interest, they also do not prohibit trade interest for paper currency.

Consequently, we can conclude that the prohibition of trade interest does not apply to today's paper currency. This means that it is permissible to sell two riyals for one dollar at a later date. It is permissible to sell 100 riyals today in return for $150 riyals at a later time. This is no different than selling on camel for two or three, which is a sale that the Prophet made.

It is no different than selling 40 sheep on the spot in return for 80 sheep paid over the course of four years, which was approved by the Saudi Council of Senior Scholars under the supervision of Sheikh `Abd al-`Azîz b. Bâz in their resolution #6904. The text of that resolution is as follows:

It is permissible to sell livestock in unequal quantities and with a deferment of payment.

This is established by the prophetic tradition narrated in Musnad Ahmad and Sunan Abû Dâwûd from `Abd Allah b. `Umar who said:

Allah's Messenger told me to dispatch on camel-back a military detachment which was under my authority. I sent them forth on the camels that were with me until all the camels were dispatched and some people were left behind.

The Prophet said to me: "Purchase some camels with the young charity camels to be paid when they arrive so that this detachment can be sent."

I went ahead and purchased a mature camel on the spot for two or three immature camels from the charity wealth to be paid when they arrived, and in this way sent off the remaining members of the detachment. Then when the charity camels arrived, Allah's Messenger paid them out.

Al-Dâraqutnî relates this tradition by meaning. Also alBayhaqî narrates it in his Sunan by way of `Amr b. Shu`ayb from his father then from his father.

And with Allah rests all success.

The Permanent Committee for Research and Legal Pronouncements:
Also refer to: Pronouncement # 20021 concerning the sale of sheep along with 100 riyals, with the hundred riyals on the spot and the sheep deferred

Also refer to: Pronouncement # 3791 concerning the permissibility of selling on meter of cloth for two meters at a later date.

The following is the text of Dr. Muhammad Sulaymân al-Asqar's recommendations to the Islamic Law Council of Kuwait in 1989 concerning the permissibility of selling one riyal for two or one dollar for two:

The first solution is for the Council to abandon its adoption of the third opinion stated above (which says that paper currency is analogous to gold and silver and is subject to the prohibition of interest), and this should be done since the effective cause for the extension of the ruling by way of analogy does not exist in paper currency. Then the council should adopt the second opinion stated above, which is the opinion of the Shâfi`î, Mâlikî, and Hanbalî schools of law concerning base-metal coinage, that it is merchandise and that as such it can be traded in kind in unequal quantities, on the spot or with a deferment of payment. There is no prohibition of selling currencies for their own currencies, for other currencies, or for gold and silver. There is no prohibition against the purchase of gold and silver with paper money paid on the spot or later.

This solution does not solve the problem of loans, because the legal axiom is that all loans that come with a benefit to the lender are prohibited. However, it is possible to instead of loaning money to sell it with a deferred payment. Instead of loaning out paper currency for a year, it is possible for someone to purchase currency with some other commodity or with other currency to be paid later on. A person, for instance, can purchase 1000 Jordanian dinars at present for 1200 Jordanian dinars a year from now.

This first solution is in conformity with what the majority of jurists have said regarding base metal coinage. Paper currency resembles base metal coinage far more than it resembles gold. Base metal coinage and paper currency are both examples of fiat money, whereas gold is commodity money. Base metal coinage and paper currency are both subject to fluctuations in value, especially depreciation, and can even lose value altogether if certain governments refuse to recognize them.

Conclusions

There are, nevertheless, contemporary scholars who hold the view that paper currency is not subject to the prohibition of interest, with some of them expressing this view even
before 1973 and the abolition of the gold standard, among them is Sheikh `Abd al-Rahmân Sa`dî.

I have presented a brief explanation of the economic issues that are relevant to explaining how much paper currency differs from gold and silver after the abolition of the gold standard in 1973. The nature of paper money is demonstrated clearly with the help of charts and tables, as well as with the statements of one of the leading economists of our time.

A number of researchers have expended considerable efforts to find ways of facilitating financial matters for the Muslims after they realized the great difficulties that Muslims were facing due to the changing nature of money and finance. They have revised their opinions about a number of commercial transactions that most scholars of the past had assumed to be prohibited, and instead ruled that they were permitted in order to alleviate hardship. It is high time that they revised their stance on the prohibition of interest on paper money, which was never regarded as prohibited by the scholars of the past.

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