NETWORKING AS A MEANS TO VALUE CREATION

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Abstract
In this paper, we suggest that value creation is becoming a function of networks. As corporations out-source to entrepreneurs, value creation is becoming increasingly divided among firms that co-operate voluntarily for increased efficiency. We believe, therefore, that entrepreneurship research should move beyond a focus on the individual entrepreneur – toward a focus on relationships and networks.

This paper compares the networks of interdependent players in the traditional bazaar, with those of the New Economy. Entrepreneurship and value creation in the traditional bazaar were conducted around personal relationships and alliances. Technology eventually allowed a shift to the impersonal transactions of the Firm-type Economy – an economic institution, which involves a mode of commercial activity such that industry and trade take place primarily within a set of impersonally defined institutions. In the emerging global scenario, we observe a return to value creation in multi-polar networks. The unit of interest is no longer the firm, but the multi-polar network, in which relationships are important.

The objective of this paper is to provoke colleagues to think about value creation in the new, multi-polar, Network Economy. Like the bazaar, which allowed physical concentration, and therefore functioned efficiently, the Web provides concentration and clustering of vendors. Potential buyers and suppliers meet efficiently on-line, and this reduces search costs and minimises disparity caused by geographic fragmentation. Internet searches reflect a certain pattern. A potential buyer finds several web-pages, thus learning about supplies and prices from several suppliers, and alliances – networks of suppliers. Indeed, we are coming full-circle to a multi-polar scenario of value creation.

Introduction

How can entrepreneurs – lacking economies of scale – create value? One solution is for small firms to develop relationships with larger firms, creating multi-polar networks. We see it happening; entrepreneurs are shedding their desire for independence, as they discover interdependence and relationships to be more profitable. The result is symbiotic marketing, which we define as, "a marketing effort by multiple parties, each of which benefits from the joint effort, such that added value is created." Symbiotic relationships are leading to multi-polar value creation. Value creation is thus moving beyond the firm, becoming a function of relationships and multi-polar networks. A look at the multi-polar networks of interdependent players in the traditional bazaar may enhance our understanding of the emerging relationships and multi-polarity of the New Economy.

Definitions

- The **BAZAAR-TYPE ECONOMY** is a social¸ cultural and economic system in which the physical clustering of vendors facilitates the consumer's comparative information search, by eliminating displacement time. Value creation is strongly influenced by relationships and networks; relationships and preferential treatment are integral to business. Consumers are not treated equally. Different people pay unlike prices. The price paid and the level of service provided is a function of relationships. Products and services are personalised, and this leads to customer loyalty.
- The **FIRM-TYPE ECONOMY** is an economic institution in which location is a competitive advantage. In the shopping mall, for instance, an exclusivity clause protects the vendor, limiting competition. The consumer's comparative information search involves displacement time, and an opportunity cost is involved when seeking perfect information. Business takes place primarily within a set of impersonally defined institutions. Value creation and the flow of commerce are both functions of strategies based on optimisation models. The purpose of transactions is to maximise wealth efficiently, and the means to this is rational and unbiased decision-making that treats buyers as equals. The price paid and the level of service provided

is established by the seller. Products and services are standardised, leading efficiency that in turn allows competitive pricing.

- The **NEW ECONOMY** is a system in which value is creating through the virtual clustering of vendors, facilitating the consumer's comparative information search. The price paid and the level of service provided is affected by status and relationships. Products and services are customised.

The Literature

Entrepreneurship literature has traditionally focused on the individual entrepreneur. This is true of Cantillon (1755), Schumpeter (1912), Knight (1921), Shapero (1975), Kets de Vries (1977), Kirzner (1979), Brockhaus (1980), and most modern studies in leading entrepreneurship journals.

In contrast, research in international business has concentrated on the firm. Traditional approaches, in the study of international business, focused on a uni-polar and hierarchical distribution of power and control. Internalisation Theory (Buckley and Casson, 1976; Morck and Yeung, 1991, 1992; Rugman, 1979, 1981; and Teece, 1985) taught us that, by investing in its own foreign subsidiaries, a firm could expand operations, while maintaining control at Head Office. Likewise, the Eclectic Paradigm (Dunning, 1973, 1977, 1980, 1988) focused on ownership-specific advantages and location-specific advantages that a firm can enjoy, while maintaining centralised control. A uni-polar scenario is also implicit in the Stage Models of Incremental Internationalisation (Bartlett and Ghoshal, 1989; Bilkey, 1978; Bilkey and Tesar, 1977; Buckley, Newbould and Thurwell, 1988; Cavusgil, 1980, 1984; Cavusgil and Nevin, 1981; Johanson and Vahlne, 1977, 1990; Johanson and Wiedersheim-Paul, 1975; Leonidou and Katsikeas, 1996; and Newbould, Buckley and Thurwell, 1978). Internationalisation can be achieved without giving up power and control; the internationalising firm can maintain its uni-polar distribution of power and control.

As entrepreneurs increasingly become involved in value creation across international boundaries, an alternate approach is gaining importance, considering a multi-polar distribution of power and control. Rather than focusing on the internationalisation of one centralised firm with a uni-polar distribution of power and control, multi-polar networks of firms can increase effectiveness. Power and control are divided among entrepreneurs who co-operate voluntarily for increased efficiency and profit. Literature pertaining to this networking perspective includes Acs and Dana (2001); Axelsson and Easton (1992); Bodur and Madsen (1993); Coviello and Munro (1997); Dana (2001); Fontes and Coombs (1997); Johanson and Mattsson (1988, 1992); Johanson and Vahlne (1992); Sharma (1992); Sharma and Johanson (1987); Welch (1992); Welch and Luostarinen (1988, 1993); Welch and Welch (1996); and Wilkinson, Mattsson, and Easton (2000). Here, the focus is not on the firm, but on a multi-polar system with many small-scale entrepreneurs involved in value creation via networks.

Multi-polar value creation is a relatively new phenomenon in the West. Yet, the concept is not new at all. We read about it in accounts of the Babylonians, over 2,000 years ago. While entrepreneurs in the West strove for independence, entrepreneurs of bazaar economies thrived in the long-established networks spanning Indonesia (Geertz, 1963), Indo-China (Dana, 1995; 1999; 2002), China (Dana 1998), Central Asia (Dana, 2000; 2002), and the lands of the former Ottoman Empire (Sayigh, 1952). Overseas Chinese networks likewise became important (Shenker, 1994). In Japan, also, symbiotic marketing was reflected in networks (Wright, 1989).

Asians brought their networks when they came to the West. Sociology provides us with a rich literature on immigrant entrepreneurs and their ethnic networks (Light, 1972). Loewen (1971) studied the Chinese in Mississippi. Wong (1987) also analyzed Chinese entrepreneurs. Other examples include a study of Han Chinese entrepreneurs in Canada (Brenner and Toulouse, 1990); and a description of Han Chinese in Vietnam (Dana, 1994).

Sociologist Howard E. Aldrich looked beyond ethnic networks and examined social networks. Aldrich and Zimmer (1986) concluded that networking might be an essential requirement for entrepreneurial success. Aldrich, Rosen and Woodward (1987) further demonstrated the impact of network accessibility. Further research includes Aldrich (1989) and Dubini and Aldrich (1991). Members benefit from being involved in a network; it is a symbiotic, interdependent relationship. Acs and Yeung (1999) used the term co-dependence.

While sociologists have focused on networks of small-scale entrepreneurs, we also see increasing collaboration between small and large firms. This allows the product of smaller firms to reach global markets more quickly than through independent expansion (Harrison, 1997). Bonaccorsi (1992), and Dana and Etemad (1994; 1995), explain how small-scale entrepreneurs can rely on large firms for parts of their internationalisation activities. Through this "scaling up" process, smaller firms can leverage their network resources to shorten the time span and reduce the cost and risk of their internationalisation. Similarly, performing specialised functions for large firms allows small firms to hasten their own learning curve, and to internalise sufficient expertise to become competitive at the global level. Thus, internationalisation increasingly involves symbiotic relationships among large and small firms. Reynolds (1997) noted that the recent expansion of markets has not been associated with an expanded role for larger firms. Instead, smaller firms are filling niche roles (Buckley, 1997).

Networks of small and large firms can facilitate value creation and thus enhance the competitiveness of both types of organisations. By supplying a portion of the high-volume needs of bigger firms, small firms can specialise, achieving their own economies of scale. As these smaller firms become more competitive, capturing scale economies not possible without large-firm linkups, the large firms in turn gain competitiveness by integrating those economies into their own value chains. The large firms also gain flexibility and economies of scope by accessing a number of highly specialised small firms, each producing a small range of components at very substantial scale economies. A further benefit to large firms linking up with smaller ones is the enhanced ability to tailor products or processes to fit local demand or content requirements.

The Traditional Bazaar

The bazaar is a social and cultural system, a way of life and a general mode of commercial activity, which has been in existence for millennia. In the bazaar, the focus is on relationships and alliances. In this scenario, consumers do not necessarily seek the lowest price or the best quality. An individual buys from a friend, sometimes to help the friend and sometimes to ensure that the friend will reciprocate. The multiplicity of related small-scale transactions results in a fractionalisation of risks. Firms are not perceived as rivals of one another. There is minimal – if any – brand differentiation among merchants. Economic rationality is not an issue. Segmentation refers to the geographic clustering of producers (Geertz, 1963). Prices are negotiated, as opposed to being specified by the seller.

As noted by Webster (1992), building long-term relationships can be viewed as a social and economic process. Unlike Western relationship marketing, which is customer-centred, whereby a *seller seeks long-term business relationships with clients* (Evans and Laskin, 1994; Zineldin, 1998), the focus in the bazaar is the relationship itself. In the bazaar, *both* the buyer and the seller seek a relationship.

While the entrepreneur described by Schumpeter (1911; 1928; 1934; 1942; 1947; 1949) is an innovator who causes disequilibrium to profit therefrom, the entrepreneur of the bazaar may simply identify an opportunity for profit (rather than create one). In this way, the entrepreneur of the bazaar corresponds to that of the Austrian school (Kirzner, 1973; 1982).

While competition in the West is understood to be competition between sellers, in the bazaar economy, competition implies a tension between buyer and seller, rather than between sellers (Geertz, 1963). The lack of information results in an imperfect market, and with few exceptions, retail prices are not displayed, but are determined by negotiations. The customer first tests price levels informally, and only later begins to bargain. Often it is the buyer who proposes a price. The establishment a long-term relationship facilitates future purchases. As transaction-centred costs begins to decline, mainly due to the rise in relationship (or social capital) the overall transaction costs (Williamson, 1985; 1996) begin to approach Williamsonian optimality, whereby buyer and seller feel highly satisfied with the transaction.

The Firm-Type Economy

The firm-type sector is an economic institution, which involves a mode of commercial activity such that value creation take place primarily within a set of impersonally defined institutions, grouping people according to organisation and specialisation. Its underlying assumption is that profit-maximising transactions occur based on rational decision-making, rather than the nature of personal relationships. The focus is on impersonal transactions. Weber's (1924) thesis applies.

In this type of economy, the decision space is occupied by product attributes; the buyer and seller are secondary, if not trivial, to the transaction decision. The interaction between the buyer and the product is deemed to be more important than that between the buyer and the seller. Transactions are based on economic rationality and are therefore impersonal in nature. Competition is an activity that takes place between sellers, who engage in segmentation, in order to partition the market into like-groups of predictable consumers. Prices are tagged, reflecting market forces. While Western marketing principles (Gronroos, 1989) apply here, market-orientation is linked to the maturity of the industrialisation process (Seglin, 1990). Where industrial development is limited, the framework for economic transition may have to rely more on new ventures and on joint initiatives.

Observations

Entrepreneurship, during the 20th century, took place within the context of the Firm-type Economy. In this context, businesses claim to treat clients as equals. It is assumed that profit-maximising transactions occur based on rational decision-making, rather than on the nature of personal relationships between entrepreneurs and consumers. *The focus is on impersonal transactions.* The decision space is occupied by product attributes and by services attached to them, backed by formal warranties. Consequently, the relationship between the buyer and the individual salesman is secondary, if not trivial, to value adding. The interaction between the buyer and the product (and/or service) is deemed to be more important than that between the buyer and the seller. Competition takes place among sellers. Geographic location is often a competitive advantage. Selling prices are dictated by producers or sellers, if not by government regulation.

In the 21st century, we observe a significantly different set of norms. No longer are all men created equal. Networks are adding value, creating brand loyalty via special relationships. A frequent traveller on Air Canada can earn "Super Elite" status, entitling this individual to differential treatment, preferential seating, special promotions, discounts and personal concierge service. Even more striking, this preferred customer can also benefit from preferential treatment on British Midland, and on the 13 other members of Star Alliance – a global alliance of firms, which were formerly competitors. This relationship leads to increased brand awareness, and brand loyalty, although differentiation is less evident than ever before. Airline seats are sold as a commodity, yet brand loyalty (or more precisely network-loyalty) prevails. The transaction decision is less concerned with product attributes, and more focused on relationships and preferential treatment. Formerly rival firms create value by co-operating in global alliances. The unit of interest is no longer the firm but the *multi-polar network*.

Interestingly, this reality is shared with the Bazaar-type Economy, where the focus is not on impersonal transactions, but rather on relationships. Space, time, production and sales must be well managed, and personal relations must be managed. A sliding price system results in a price within the prevailing limits. Price can vary greatly, depending on the relationship between buyer and seller. Thus, interaction tends to take place between the buyer and the seller, rather than between the buyer and the product.

Today, goods and services are being increasingly treated as commodities. The focus has shifted away from the features of the product, to the relationship between buyer and seller. Looking again at the airline industry, we note that not long ago, advertising by Delta Airlines emphasised the use of 4-engine aircraft, while United differentiated itself through the use of turbo-props and French-built Caravelles, with two aft-mounted engines. Today, the fleets of different airlines vary less than they did in the past. Almost every airline has Airbuses and Boeings, and passengers are less informed about details. Likewise, there is little difference between the mobile phone built by one manufacturer and that built by another.

Another characteristic of the New Economy is that the Web has become a hub for transactions, between consumers and suppliers, which are clustered together, reducing the time involved for comparative shopping. Often, it is the buyer who suggests a starting price – as is the case in the bazaar. The entrepreneur Betty Sinclair operates www.itsjustlunch.com, encouraging individuals to outsource even dating.

The Web allows entrepreneurs to globalise without the need to have several offices; internationalisation is decentralised. The Web also allows distributors like amazon.com to avoid high costs of inventory. In Japan, Rakuten launched a very successful concept, allowing vendors to sell produce very rapidly, through its http://www.rakuten.co.jp. This operates in a fashion very similar to that of the bazaar.

Indeed, attributes of the New Economy share much in common with the Bazaar-type Economy. In this economic system, the focus is not on impersonal transactions, but rather on multi-polar networks of relationships.

With little variation, the style and procedures of trade, in the bazaar, reflected a certain pattern. A potential buyer inquired about supplies and prices from *several* suppliers, in a concentrated area. This allowed the person to form a reasonably informed opinion about the state of the market at the time. Ongoing arbitrage thus accorded the structured bazaar functional efficiency. Notice how much value creation in the bazaar resembled the World Wide Web:

- *Knowledge Dissemination*. Up-to-date information is disseminated at unprecedented speed.
- *Absorptive Capacity*. The potential buyers collectively have sufficient absorptive capacity to make mutually beneficial spot market transactions. Hence, we see the success of auctions on the Web.
- *Efficiency*. The Web allows for the efficient performance of market functions.

Like the structured bazaar, which allowed physical concentration, and therefore functioned efficiently, the Web provides concentration and clustering of vendors. Potential buyers and suppliers meet efficiently on-line, and this reduces search costs while minimising disparity caused by geographic dispersion. Thus, the Web reduces overall transaction costs, as all parties concerned converge on a central location. Like the bazaar, the Web provides the following:

Information Search. Entrepreneurs disseminate their proprietary information regarding new products and trends. Consumers obtain details with unprecedented speed, facilitating comparative shopping.

Updating. Potential suppliers and buyers quickly update and upgrade their state of information and incorporate their new knowledge to assume a new position.

Temporal Equilibrium. Some potential suppliers and buyers behave as intermediaries, and they profit from arbitrage.

Opportunity for Co-operation. Again, firms are engaging in co-operative bargaining and negotiations, forming alliances.

Likewise, the style and procedures of Internet searches reflect a pattern. A potential buyer finds several web-pages, thus learning about supplies and prices from *several* suppliers. This allows the individual to form a reasonably informed opinion about the state of the market at the time.

In the bazaar, there was little if any differentiation among clustered sellers. There was considerable co-operation among retailers and among wholesalers. Multi-polar networks were essential for value adding, as profitability was a function of personal relationships.

In time, the firm-type economy evolved, shifting the focus from personal relations, to impersonal transactions. Everybody was entitled to equal treatment. Rather than haggle over prices, sellers simply posted their firm, non-negotiable, asking prices. Today, once again, we see a focus on status, relationships, price negotiations, and multi-polar networks.

Conclusion

In the bazaar, one found the geographical clustering of producers, according to the specialisation of suppliers. This made possible the efficient clearing of products. Consumers found convenience in the clustering of producers. This facilitated comparative shopping with minimal travel. On-line shopping likewise facilitates information search, comparative evaluation, and decision-making. Simultaneously, we see the formation of alliances among former competitors. Consolidators sell tickets at discounted prices, and on the Web, potential customers can state the price they wish to pay. As was the case in the bazaar, the buyer proposes the price. Code-sharing blurs product differentiation between airlines. Small airlines (such as Eurowings) work in teams with large flag-carriers. Yet, loyalty exists – focused on networks rather than on individual firms. Air Canada, Air New Zealand, the Austrian Airlines group, and Lufthansa give recognition and special treatment to each other's preferred customers. One fare is valid on any airline of the Star Alliance. Together, acting as a multi-polar network, the members of the Star Alliance compete against members of other alliances. The focus has shifted away from the firm, to the multi-polar network.

As summarised in the table, below, we seem to have come full circle, from the Bazaar-type Economy (with a focus on relationships and multi-polar networking), to the Firm-type Economy, and now to the New Economy in which relationships are again important. Multi-polar value-creation is re-emerging. Future research should reflect this.

Bazaar-type Value Creation	**Firm-Type Value Creation**	**Multi-polar Network Value Creation**
Focus on personal relations, alliances & networks	Focus on impersonal transactions	Focus on relationship marketing, alliances & networks
Geographical clustering facilitates information search	Exclusivity clause replaces clustering, complicates comparative shopping	Web allows for easy information search
Preferential pricing is based on status and relationships	Prices are indicated by the vendor and buyers are treated as equals	Preferential pricing is based on status and relationships
Would-be competitors co-operate, re-enforcing relationship networks	Competition takes place between sellers	Former competitors co-operate for mutual gain, thus re-enforcing relationship networks
Brand loyalty is influenced by preferential treatment	Brand loyalty is a function of product differentiation	Brand loyalty is influenced by preferential treatment
Effective unit is the network	Effective unit is the individual firm	Effective unit is the network

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