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ACQUISITION BASED DYNAMIC CAPABILITIES AND REINVENTION OF BUSINESS MODELS: BRIDGING TWO PERSPECTIVES TOGETHER*

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Abstract. Dynamic capabilities in merger and acquisition are complex events in the process of sustaining complete advantage of merging business for which we have incomplete understanding. The aim of the paper is to identify the role of dynamic capabilities in reinvention of business model of merging company in related diversification process by means of acquisition. The major contribution of paper is emerging conceptual model of research that connect acquisition based dynamic capabilities frameworks (Capron & Anand, 2007; Teece, 2007) with nine building blocks of business model (Osterwalder & Pigneur, 2009) together and illustration how acquisition based dynamic capabilities foster a reinvention of business models in ICT Industry. Presented methodology is encouraging to analyse importance and strengths of acquisition based dynamic capabilities and their role in changes of business models in M&A processes.

Keywords: dynamic capabilities, innovation, business model, acquisition, information and communication technologies, sustainability

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1. Introduction

Dynamic capabilities in merger and acquisition are complex events in the process of sustain complete advantage of merging business for which we have incomplete understanding, in part because researches have tended to consider only explanation of them. However, successful innovative ideas can be brought to global market by means of acquisition process. The aim of the paper is to identify the role of dynamic capabilities in reinvention of business model of merging company in related diversification process by means of acquisition that lead to sustained competitive advantages. Current research was organized to test three propositions that differs from traditional methods of studying merger and acquisition. The research argues that acquirer can buy a target

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company's dynamic capabilities, which it would then also fold into its re-invented business model. That's what Facebook did with WhatsApp in mid of 2014.

This case study of WhatsApp acquisition by Facebook was selected due to following reasons. Firstly, the success story of the case company is closely linked to entrepreneurial innovation (Olaniyi and Reidolf, 2015). Secondly, the numbers are in Facebook Inc.'s acquisition of mobile-messaging application WhatsApp Inc. extraordinary. The Facebook paid \$22 billion for a WhatsApp start up that generated \$10.2 million in revenue 2013 year and its net loss for the six months that ended in June 2014 was \$232.5 million. Thirdly, knowledge creation and dissemination, as well as innovation, are keys to promotion of competitiveness (Aleksejeva, 2016). All mentioned above is especially relevant to an Information and Communication Technologies industry, where technologies are developing at the astonishing speed. The research illustrates how organization deals with the commercialization of innovation by means of acquisition of engineering team, technologies and users' base.

The research main contribution is emerging conceptual model of research that connects acquisition based dynamic capabilities frameworks (Capron and Anand, 2007; Teece, 2009) with nine building blocks of business model (Osterwalder and Pigneur, 2009) together and, thereby, illustrates how acquisition based dynamic capabilities underpinning a reinvention of business models in Information and Communication Technologies Industry.

2. Literature review

Strategy is about building dynamic capabilities aimed at responding efficiency to future and existing contingencies (Ambrosini and Bownam, 2009). What's more, sources for competitive advantage lie in companies' ability to alter the resource base: create, integrate, recombine, and release resources. Teece et al. (1997) define dynamic capabilities as "the ability to integrate, build, and reconfigure internal and external competences to address rapidly changing environments". Capron and Anand (2007) define dynamic capabilities as "the capacity of an organization to purposefully create, extend, or modify its resource base". For long-term growth and survival of the enterprise, they must be cleverly managed, or orchestrated, by a dynamically capable management team pursuing a good strategy (Teece, 2014). Dynamic capabilities can usefully be thought of as belonging to three clusters of activities and adjustments: identification and assessment of an opportunity (*sensing*); mobilization of resources to address an opportunity and to capture value from doing so (*seizing*); and continued renewal of core competences (*transforming*) (Teece, 2009).

2.1 Acquisition based dynamic capabilities

There are very few researches on specific dynamic capabilities that have been identified and studied involve merger and acquisition. Teece argues it might be "because assets are bundled together often tightly linked inside incumbent firms, it may be difficult to obtain assets in the desired configurations through asset purchase or sale in mergers and acquisitions" (Teece, 2009). However, Capron et al. argue that "entrepreneurs must acquire additional resources, which will be „reconfigured “and „integrated “with existing resources if firms are to grow and successfully innovate technology - based products and services" (Capron et al., 1998). By Eisenhardt and Martin (2000), practice with homogeneous acquisitions (i.e., those in the related markets) was positively associated with the accumulation of tacit and explicit knowledge about how to execute acquisitions and achieve superior acquisition performance.

Important type of dynamic capabilities which enhances firm's potential for growth and underpin competitive advantage are acquisition-based dynamic capabilities (Capron and Anand, 2007). In their research, Capron and Anand (2007) suggest that acquisition-based capabilities consist of three main capabilities which are *selection*, *identification*, and *reconfiguration* which are very similar as *sensing*, *seizing* and *transforming* dynamic

capabilities of Teece (2007). Selection (*sensing*) is capacity to recognize when an acquisition would be the most suitable strategic move for gaining new resources. Identification capacity (*seizing*) is dynamic capability to find and negotiate with the most suitable targets. Reconfiguration (*transforming*) the capacity is about the dynamic capability to reshape resources within the target and acquiring firms (Capron and Anand, 2007). Thus, making strategically important investment choice on M&A involve such managerial activities as a selection (*sensing*), an identification (*seizing*) and a reconfigurations (*transforming*) as well as re-inventing and implementing new business model (Teece, 2007).

Proposition 1. The success of a merger or acquisition is gouged by the degree of similarities and complementarily between dynamic capabilities of two merging business.

2.2 Business model of merging company

Christensen et al. argue that “we must be able to describe exactly what we are buying. The best way to do that, we’ve found, is to think of the target in terms of its business model” (2011, p.2). In essence, a business model embodies nothing less than the organizational and financial „architecture“ of a business (Teece, 2010). The selection/design of business models is a key micro-foundation of dynamic capabilities - the sensing, seizing, and reconfiguring skills that the business enterprise needs if it is to stay in synch with changing market (Teece, 2005). From the point of view of Johnson et al. (2008) a business model consists of four main elements, the synthesis of which delivers value: customer value proposition; profit formula; key resources and key processes. Osterwalder and Pigneur (2009) with real 470 business practitioners from 45 countries extended number of elements and developed Business Model Canvas with nine building blocks: customer segment, value proposition, channels, customer relationship, revenue stream, key resources, key activities, key partners, cost structure. To re-invent a business model, authors recommended to apply “four steps framework: eliminate, reduce, increase and create” of Kim and Mauborgne (2005): to eliminate and reduce an elements of business model in terms of cost structure as well as increase and/or create as a new an elements of business model in terms of revenue stream (Osterwalde and Pigneur, 2009).

What’s more, Christensen et al. (2011) differentiate between two acquisition types. First one is “leverage my business model” (LBM) acquisitions, where companies are acquired for their resources and are incorporated into the acquirer’s business model. The authors argue that LBM acquisitions often underperform (Christensen et al., 2011). They are frequently priced too high, and they often don’t deliver the promised growth or cost savings (Kaufmann, 2016). Second one is “reinvent my business model” (RBM) acquisitions, where companies are acquired for their business models, generally disruptive business models. Disruptive companies and their business models are those whose initial products are simpler and more affordable than the established players’ offerings. Acquirer can buy another firm’s business model, operate it separately, and use it as a platform for transformative growth (Christensen et al., 2011). According to the authors, there is far more growth potential in purchasing other companies’ business models than in purchasing their resources (Christensen et al., 2011). Therefore, Christensen et al. (2011) argue that the most reliable sources of unexpected growth in revenues and margins are disruptive products and business models.

However, there are very few examples how to reinvent business model by means of acquisition of disruptive companies and how acquisition based dynamic capabilities foster a reinvention of business model of acquirer and, therefore, underpin competitive advantages of merging company.

Proposition 2. Business models of both acquirer's and the target's disruptive companies can successfully fold into new business model by means of acquisition based dynamic capabilities to create and capture new value proposition.

Proposition 3. Acquisition based dynamic capabilities underpin reconfiguration existing and acquired core competences of acquirer to facilitate new product/service development and, therefore, sustain competitive advantages.

The propositions were tested empirically by exploring illustrative case study of Facebook acquisition of WhatsApp in mid-2014.

3.0 Illustrative case study Facebook acquisition of WhatsApp

3.1 Facebook acquisition of WhatsApp in mid-2014

The numbers are for Facebook Inc.'s acquisition of mobile-messaging application WhatsApp Inc.: the social network paid \$22 billion for a start-up that generated \$10.2 million in revenue 2013 year. The acquisition supports Facebook and WhatsApp's shared vision to make the world more open and connected by delivering core internet services in efficient and affordable manner. In order to evaluate *what* and *how* dynamic capabilities can be transferred in acquisition process to generate a new business model and thus sustain competitive advantage, as well as to test proposed propositions, we apply three steps research.

3.2 Illustration of acquisition based dynamic capabilities and reinvention of business model

Proposition 1. The success of a merger or acquisition is gouged by the degree of similarities and complementarity between dynamic capabilities of two merging business.

The research has explored dynamic capabilities of *selected* target's company and acquirer's company, the research result is presented in table 1 and table 2.

Table 1. Dynamic capabilities of Facebook before acquisition of WhatsApp

Products	Sensing (selection)	Seizing (identification)	Transforming (reconfiguration)	Result in (sustainability)
Facebook	Need to connect the US college students.	Facebook social platform was created as a way for students to keep in touch over the Internet and get to know each other better.	Over time Facebook has developed into global mass platform, adding new features (news feed, more privacy features, Facebook notes, the ability to add images to your blog and comments and more).	Facebook developed social platform providing excellent user experience, and thus reached 1.2 billion active users being the largest social network globally.
Facebook Mobile app	Growing use of mobiles caused the need to enable users to access the social network on their phones.	Developed the Facebook Mobile app for convenience and easy use on the phones.	Launch mobile app platform updates, improve privacy settings, and build apps that integrate with social network.	Facebook success on mobile devices boosts Facebook's profits with mobile app ad revenues accounted more than \$3 million over 2013.
Facebook Messenger	Impressive growth potential for mobile communications industry and users' preferences towards instant messaging services.	Launched Facebook Messenger to give people passionate about messaging a simpler and faster way to communicate with their friends mobile-to-mobile.	Continue to run tests to improve speed and performance as well as add new features to develop in Messenger.	Facebook Messenger is one of the most popular applications on the mobile platform today. However, it <i>failed to achieve the desired widespread</i> and generated a lot of controversy among users.

Source: developed by author

Table 2. Dynamic capabilities of WhatsApp before acquisition

Product	Sensing (selection)	Seizing (identification)	Transforming (reconfiguration)	Result in (sustainability)
WhatsApp	Growing use of mobiles and need to transform personal communications previously dominated by the wireless carriers.	Devised a simple process of connecting mobile users, focusing on clean and fast communication service that works flawlessly.	Continuous improvement resulted in launching updates, new versions for various OSs and new features (group chats, photo sharing, status updates, shared links and audio files).	WhatsApp has audience of 450 million users with <i>the highest level of engagement</i> ever and growth of 1 million users daily.

Source: developed by author

Having compared on tables 1 and 2, it became obviously, that Facebook failed to achieve the desired widespread in mobile communication whereas WhatsApp has got an audience with the highest level of engagement. Thereby, the success of an acquisition of WhatsApp was gouged by the strong similarities and complementarily between dynamic capabilities of Facebook.

Proposition 2. Business models of both acquirer’s and the target’s companies can successfully fold into new business model by means of acquisition based dynamic capabilities to create and capture new value proposition.

Having analyzed both Facebook and WhatsApp’ business models in depth, the research has identified acquisition based dynamic capabilities of Facebook in reinvention of their business model and delivering new customer value propositions.

Table 3. Acquisition based dynamic capabilities of Facebook in reinvention of their business model by acquiring WhatsApp startup

Building blocks of business model	Facebook business model	WhatsApp business model
	Acquisition based dynamic capabilities	
<i>Key partners</i>	Facebook app& games developers Content partners Internet operators Joint project (Internet.org) partners	App distributors Content partners Internet operators
<i>Key activities</i>	Social platform development and maintenance Apps development	Apps development Servers maintenance
<i>Key resources</i>	Brand and user base Technology infrastructure Software engineers Facebook platform	Communication engine Users in emerging economies Engineering team IT infrastructure
<i>Value propositions</i>	Unique value proposition: connecting the world Communicate with friend and share information easily and free Excellent user experience: news, events, voice or video chatting	Unique value proposition: simple and mobile, no advertising, first year free Communicate with friend from your phonebook Free messages (text, video, photo) Excellent user experience: “No Ads! No Games! No Gimmicks!”
<i>Customer relationship</i>	Long-term and loyal Network effects	Loyal users Strong emotional connection with app
<i>Channels</i>	Facebook.com Mobile apps Facebook Ads	Apps market (Google Play, Android Phone)
<i>Customer segments</i>	Internet users of developed countries Mobile users of developed countries Advertisers Developers	Internet users of emerging economies Mobile users of emerging economies
<i>Revenue streams</i>	Free app Advertising revenues Payments and other fees	“Freemium” model Subscriptions of \$0.99 annually with first year free
<i>Cost structure</i>	Employees, including engineers and developers Marketing, general and administrative expenses - R&D. Technology infrastructure maintenance	Employees, including engineers New technologies and product development Technology infrastructure maintenance

Source: developed by author

Facebook and WhatsApp had divergent business models; the disruptive business model of WhatsApp is simpler and more affordable as well as deliver a unique customer value proposition. However, the two companies had a convergence in their common mission - to provide users with a closer communication with each other, in different corners of the globe.

The acquisition based dynamic capabilities helped Facebook to reinvent of business model as follows. Facebook *sensed new customers' segments* for their business: Internet and mobile users of emerging economies and new *key activities* that should be developed: mobile apps products; Facebook seized *new key (idiosyncratic) resources* by acquiring WhatsApp engineering team and users' base in emerging economies as well as *key partners'* network by acquiring WhatsApp start up partners. Hence, Facebook transformed *new customers' relationship* mode: exploit a strong emotional connection of loyal users with mobile apps. to their business and new promotional *channels* by adding opportunities of apps markets (Google Play, Android Phone).

Therefore, Facebook transformed their *customer value proposition*, delivering new value to the customers and capturing new value for shareholders. As results, Facebook dramatically changed *cost structure* by eliminating CAPEX or reducing their OPEX on the new mobile technologies and apps development as well as potentially increase their *revenue streams* form Internet and mobile users of emerging markets and resulted in competitive advantage. Several comments on reinvention of Facebook business model in WhatsApp acquisition process from dynamic capabilities perspective is given in table 4 that underpinned second proposition.

Table 4. Reinvention of Facebook business model after acquisition of WhatsApp from acquisition based dynamic capabilities perspectives

Acquisition based dynamic capabilities	Reinvention of existing business model of Facebook
<i>Sensing</i> (select) the opportunities to change the business model in terms of <i>new customer segments</i> : to attract additional FB users the	Researches show that there are more than 100 countries found where Facebook is not in the top five most visited websites. For example, Belarus – VK, Brazil – Orkut, China – Qzone, Latvia – Draugiem, Russia – VK, Uzbekistan – Odnoklasniki. However, in most of these countries WhatsApp is well-known app. <i>This might make it easier to create new Facebook users.</i>
<i>Seizing</i> (identify) new <i>partners' relationships</i> and acquire <i>new resources</i> : enlargement in endorsement with WhatsApp	WhatsApp has more than 600 million active users, and reached <i>that number faster than any other company in history</i> . Every day, more than a million people install the app and start chatting, and they remain more engaged with WhatsApp than on any other service. <i>Incredibly, the number of daily active users of WhatsApp (compared to those who log in every month) has climbed to 72%.</i>
<i>Transforming</i> (reconfigure) the business model in terms of <i>new revenues stream</i> and result in by gaining market share in instant messaging	The note on Jan's desk "No Ads! No Games! No Gimmicks!" serves as a daily reminder of their commitment to stay focused on building a pure messaging experience. But, on the other hand, if Facebook starts adding advertising on WhatsApp, there will be additional revenue. Users spend a substantial time on WhatsApp, which means that advertising is likely to have an impact. <i>Facebook should be able to target WhatsApp advertising as efficiently as it does on the Facebook platform.</i>

Source: developed by author

Proposition 3. Acquisition based dynamic capabilities underpin reconfiguration existing and acquired core competences to facilitate new product/service development and, therefore, sustain competitive advantages.

In order to illustrate the *reconfiguration of existing* and acquired core competences that facilitate to sustain competitive advantages, the paper summarized *acquisition based dynamic capabilities* in traditional dynamic capabilities Teece's framework (2009) as shown in table 5.

Table 5. Acquisition based dynamic capabilities of Facebook Inc. by acquiring WhatsApp Inc.

Products	Sensing (selection)	Seizing (identification)	Transforming (reconfiguration)	Result in (sustainability)
Mobile communication application of Facebook	Exciting Facebook Messenger application does not cater growing mobile subscribers market in <i>emerging economies</i> . Competitors messengers are strong in Europe Advantages of continues evolving technology in mobile based messaging. Searching for fast growing mobile communication application in emerging economies.	Acquiring fast growing communication applications in emerging economies. Acquiring engineering team, brand new apps mobile technologies and users' base in emerging economies of WhatsApp	Became the owners of most popular mobile application in emerging markets and Europe. Capture European market development. Target WhatsApp advertising as efficiently as it does on the Facebook platform. Attract additional FB users.	Gaining market share in instant messaging. Predicted user base increased to 1billion by 2015

Source: developed by author

The research has shown that the combination of *acquisition based dynamic capabilities* to reconfigure existing and new core competences helped accelerate Facebook and WhatsApp growths and users' engagement across both companies. Thus, Facebook would be able to achieve leadership in the field of social media and successfully compete with Twitter.

4.0 Discussion and conclusion.

Innovation is a critical weapon for entrepreneurs attempting to find new opportunities of producing better good or services (Pauceanu, 2016). When tested propositions by exploring dynamic capabilities and business models of Facebook and WhatsApp, we found the acquisition enables Facebook to significantly enhance its mobile messaging capabilities and enjoy the opportunities that are opened in a rapidly growing mobile communications industry. Acquisition of unique operating system of WhatsApp is a positive strategic move of Facebook that leads it to sustained competitive advantage. In addition to gaining market share in instant messaging with WhatsApp acquisition, Facebook will also be able to increase market share in online advertising. Therefore, propositions have been confirmed.

Recently published statistic figures show that 1.12 billion mobile monthly active users are using Facebook, while this figure was 600 million for WhatsApp around the world. Besides contributing to dynamic capabilities view on competitive advantages by adding fresh insights about successful acquisition practice, the research core contribution is in emergent theoretical framework for reinvention of business model in merger and acquisition process as shown in Fig. 1.

Acquisition based dynamic capabilities of acquiring organization:	Selection (sensing)	Identification (seizing)	Reconfiguration (transforming)	Sustainability (result in)
Designing new building blocks of business model of acquiring organization:	New key activities New customers' segments	New key resources New key partners	New channels New customers' relationship New customers value propositions	New revenue streams New cost structure New competitive advantages

Fig. 1. Conceptual model of research: bridging together acquisition based dynamic capabilities and reinvention of business models.

Source: developed by author

First acquisition based dynamic capabilities is to sense opportunities to change flowing building blocks: to select new key activities and new customer segments. Second acquisition based dynamic capabilities is to identify new key idiosyncratic resources and new partnership and seize them. Third is acquisition based dynamic capabilities to reconfigure new customer relationships and promotion channels and, thus, to create new customer value proposition. Therefore, an acquiring organization would result in new cost structure by eliminating and reducing some capital expenditure and operating expenses and new revenue streams by increasing and/or creating new activities. Thus, an acquiring organization sustains competitive advantage by means of re-invention of building blocks of new business model.

Presented methodology is encouraging to analyze importance and strengths of acquisition based dynamic capabilities and their role in changes of business models in M&A processes. The author suggests further empirical testing of presented methodology on illustrative case studies and possible further development this conceptual model.

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