Chapter 13
The Quest for Economic Recovery: Innovative Development and KM Perspectives

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ABSTRACT
Most organizations respond to an economic crisis by focusing on operational efficiency and/or on intellectual capital utilization and innovation. The conjecture is that intellectual capital confers distinct competitive advantage to an enterprise via knowledge management and knowledge spillovers and improved innovation capacity. Despite mixed empirical evidence to support this claim, intellectual capital and knowledge management remain at the forefront of an organization’s agenda during an economic downturn. Recent surveys from the field indicate some dissatisfaction with practical knowledge management. These findings are difficult to interpret because at the same time organizations appear to adopt the position that management of knowledge resources is extremely important from a strategic perspective. The objective of this chapter is to provide some new perspectives on what drives success in the knowledge economy and to demonstrate how knowledge management is the ideal response to the challenge of innovation.

INTRODUCTION
The greatest challenge that businesses, markets and countries are facing today is the continuing international financial crisis (Pressman, 2011). In order to assess the impact of the crisis on economic performance, there is a need to clarify the concept and identify its structural characteristics by borrowing elements of systems theory.

In any complex system, a crisis is a period during which the system functions poorly (but does not break down); an immediate corrective action is necessary to stop further disintegration of performance; and yet the causes of the dys-
function are not known (or are so many) that it is difficult to take an informed decision to reverse the situation (Dayton, 2004).

In systems theory, an “attractor” is a subset of the state space of a dynamic system, i.e. a set of physical properties towards which a system tends to evolve, irrespective of any starting conditions. Parameter values that get close enough to an attractor remain close even if slightly disturbed. A crisis is the sudden appearance of a new “attractor” or the disappearance of an existing one. The parameters of a dynamic system converge towards the new attractor or diverge away from their previous values leading to a qualitatively different behavior. In general, crises result in discontinuous changes in the attractor, and different types of crises may be distinguished on the basis of the different types of changes that they induce (Ruelle, 1981).

While crises are unexpected and of an unknown cause, the dynamics of the system may exhibit slow transients over time before parameter values exit the neighborhood of the old attractor. This is the primary reason why the onset of crisis conditions is rarely recognized early and certainly not before system performance is seriously degraded (Santella et al. 2009).

More broadly, crises are defined as non-routine events that create high levels of uncertainty and are perceived as threats to an organization’s goals (Seeger et al. 1998). At the organization level, crises are thought of as imposed processes of transformation when the old system can no longer be maintained and there is a need for change. (If change is not needed, the crisis has led to systemic failure.)

In this context, an economic crisis can be described as a period of dismal economic performance for a business, a market or a country. The economy is a very complex system, and for it to dysfunction, the transient conditions have to be present over a long period of time. While an economic crisis is perceived as part of the business cycle, most economic crises are unexpected and it is usually difficult to determine their exact cause. Handling an economic crisis is thus a very complicated affair, and the need for change often contrasts with the ingrained organizational reaction to simply improve efficiencies.

Most organizations respond to an economic crisis by adopting one of two extremes: focus on operational efficiency or on intellectual capital utilization and innovation. Unfortunately there is a strong preference for the former. The majority of organizations in an economic crisis try to downsize and to improve their productivity by cutting costs across the board and choosing to reduce their innovation capacity. While many organizations may merely survive an economic downturn via such conservative approaches, most will not be better prepared during the recovery period and they will not be able to keep up with the competition. On the other hand, organizations that switch to the knowledge economy may eventually become winners, but they risk their survival when gambling their resources exclusively on innovation. Those rare organizations that focus on both efficiency and innovation typically survive an economic crisis smoothly.

Empirical evidence suggests that organizations should start considering an economic crisis as an opportunity rather than as a threat: an opportunity to reflect and to stimulate innovation. An opportunity to reconfigure business processes by eliminating outdated or unprofitable processes and products and by adopting new technologies (Caballero & Hammour, 1994).

Developing an effective knowledge management strategy is key to surviving an economic crisis and to prepare for the future. Yet the period of economic downturn is a time of uncertainty and ambiguity, and an organization is often hard-pressed to take stock of its intellectual capital and to make a switch that would require behavioral changes, while drastic cuts are being pursued at all levels. In order for knowledge management to succeed as a tool during economic crises, it has to
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