In the knowledge-based economy, the value of products and services largely depends on the knowledge intangibles they embed (Drucker, 1993). The success of firms is increasingly becoming linked to the intellectual capital they are able to accumulate and re-invest in their markets (Davenport & Prusak, 1998; Nahapiet & Ghoshal, 1998; Sullivan, 1998). In this age of knowledge-based business, it is incumbent upon firms to pay increasing attention to the development of customer knowledge (Balasubramanian et al., 1998; Sawhney & Kotler, 1999).

However, researchers in marketing have generally assumed that knowledge creation happens only within the firm’s boundaries or, at the most, within the strategic alliances among firms. We argue that in the knowledge economy we need to move beyond this perspective of the firm as the knowledge creator that learns about customers and creates value for them, to a perspective of the firm as a co-creator of knowledge that learns and creates value with its customers. As already argued only in service marketing literature, customers are a vital source of knowledge and hence competitive advantage. The cooperation with them gives firms the opportunity to renew the source of their competitive advantage constantly. This is significant in a business landscape where unique and lasting competitive advantages are increasingly rare. Through co-operation with their customers, firms can better anticipate market changes (Anderson & Narus, 1991; Nonaka & Takeuchi, 1995), catalyze their innovation processes (von Hippel, 1982, 1986, 1994), and better respond to latent customer needs (Leonard & Rayport, 1997).

Thus, customers can no longer be treated as the “clandestine immigrants” in an ideal economic land with its own pre-defined rules, to which they have to conform passively. On the contrary, they appear like the native citizens of a new borderless country, where
production and consumption are deeply inter-linked processes and customers are active participants in defining the firm’s offerings. This perspective of customers as knowledge co-creators is consistent with relationship marketing, but goes beyond its traditional conceptualizations. Relationships with customers have traditionally been viewed as one-way: firms import knowledge about customers within their boundaries. In the networked world, firms can establish two-way relationships, defining new mechanisms for direct co-operation in knowledge creation. Entering this new land has deep implications, and requires us to question some of the fundamental assumptions about customer knowledge management. It no longer means only building up rich databases or collecting information through fidelity cards, aimed at understanding customer preferences and buying patterns (Wayland & Cole, 1997; Fournier et al., 1998). In the knowledge-based economy, customers play an active role in the firm’s processes of knowledge creation. It is not only important what the firm learns about its customers, but also what customers know.

This way of thinking demands new means to facilitate the participation of customers in the firms’ knowledge creation processes. And it demands new competencies on the part of firms. The purpose of this chapter is to explore this emergent phenomenon, and to offer managers a better understanding of the hurdles that arise in customer integration, and how to overcome them. We begin by introducing the traditional concept of knowledge management, and extending it beyond the firm’s boundaries. Next, we focus on the pre-conditions that need to be satisfied on the customers’ side to allow co-operation in knowledge creation. They include the need for common language, trust and motivation for knowledge sharing. We then turn our attention to the capabilities that firms need after selecting and motivating customers, to integrate customer knowledge, disseminate it within the organization and act on it to translate customer knowledge into new offerings. We introduce and explore the notion of firms’ absorptive, sharing and deployment capacities; and argue that if any one of them is missing or if there are disconnects between these steps, the entire mechanism breaks down. We examine the potential process and linkage failures at each stage and we suggest to firms how to overcome them. We conclude the chapter with managerial guidelines, from a technological, organizational, and cultural viewpoint.

**BEYOND THE BOUNDARIES OF THE FIRM: NEW PERSPECTIVES ON KNOWLEDGE MANAGEMENT**

In a world dominated by information-intensive products, organizations still produce goods, but also individual and social interactions, and several kinds of knowledge (Nonaka, 1991; Vicari, 1991; Nonaka & Takeuchi, 1995; von Krogh & Roos, 1996). The increasing spread of information and of the activities aimed at their production makes strategic knowledge the main source of power and economic revenues. Turbulent environments demand speed and flexibility. Kogut and Zander (1996) argue that “a firm (can) be understood as a social community specializing in the speed and the efficiency in the creation and transfer of knowledge”.

The point is that these social communities are becoming increasingly broad: their boundaries are often vague, and the critical sources for their success are often outside the firm’s direct control (Prahalad & Hamel, 1990). Hence, the ability to create and manage
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