

Strategies of Domestic and Multinational Firms in the Czech Republic

Talpová Žáková Sylva

Abstract

The strategic behavior of companies in the globalizing and changing markets may be characterized by the extent to which a company's strategy is adapted to its environment. The goal of this paper is to compare the strategies used by multinational and domestic companies in the Czech Republic in reacting to the environment and to ascertain which of the strategies is the most advantageous. Consequently, this study provides essential information for strategic decisions for both domestic and multinational companies.

Key words: strategy, multinational company, domestic company, environment, performance

1. INTRODUCTION

Globalization and economic crisis are manifest in varied intentions in all aspects of the markets. The Czech Republic is no exception. Although there is an economic crisis and the impact on companies in the Czech Republic is significant (Pirožek & Komárková, 2010), management at foreign companies is still considering foreign investment. It is precisely in times of crisis that firms get rid of assets which are not critical to their business. This allows those with adequate financial resources to increase market share and increase revenues via mergers and acquisitions, something which was not possible for the most part before the crisis. According to research conducted by AT Kearney, the Czech Republic is in the top twenty countries identified by management of the largest global companies as ripe for foreign investment (A.T. Kearney, 2010). The strategy of foreign multinational (MNC) and domestic companies (DC) in the Czech Republic is a current subject of interest on both the theoretical and practical levels. The strategic behavior of companies in this current period of globalizing and changing markets may be characterized by the extent to which a company's strategy is adapted to this environment. The goal of this paper is to compare the strategies used by foreign multinational and domestic companies in the Czech Republic in reaction to the environment and to ascertain which strategy is the most advantageous. More specifically, this study suggests some tentative answers to the following questions: Do the strategies preferred by the MNC and DC differ in terms of Porter's Generic Competitive Strategies? How is the choice of strategy related to the productivity of these companies? This study tests the assumptions on the sample of companies in the Czech Republic.

The struggle of domestic companies with foreign multinationals has been more emphasized recently, since with continuous globalization and crisis, foreign companies in search of new markets are taking over parts of the Czech market. The knowledge of strategies used by foreign newcomers as well as of domestic companies is therefore of a great importance to both groups of companies. Furthermore, as higher performance is a key goal for majority of the companies, it is essential for them to know which strategies are more advantageous for each group in terms

of financial performance. Such a knowledge enables companies considering entering into the Czech Republic to choose the most appropriate strategy to successfully compete in a particular market. Domestic companies, with the knowledge of strategies of foreign competitor, can more efficiently defend their markets.

2. THEORY AND RESEARCH QUESTIONS

2.1 Strategy Perspective

The more barriers to doing business in various parts of the world are reduced, the more diverse individual national markets become in terms of company ownership. Domestic companies must thus face constant new competition from around the globe which may often avail itself of benefits connected to the mother company abroad, not accessible to local companies for various reasons. On the other hand, domestic firms benefit from deeper knowledge of the local environment. MNC and DC thus operate under different conditions in this situation.

The underlying premise of this study is that the relationship exists among business capabilities, the environment and strategic type (Desarbo, Benedetto, Song, & Sinha, 2005). Since MNCs and DCs are specific with respect to organizational capabilities, market orientations, strategic objectives, environmental familiarity or global integration arrangements (Luo & Tan, 1998), these two types of companies may diverge in the means of strategies they pursue in the same environment. There are two main reasons for that. The first are the environmental conditions - for DC it is a known environment; to the contrary, MNC faces conditions partially or totally different from those of its familiar home environment, the environment in which it was born and developed (Luo & Tan, 1998). Moreover, MNCs often face a completely different market context than exists in their land of origin, since the market economy is still a fairly novel phenomenon in the Czech Republic. The second reason possibly leading to divergent strategies of DCs and MNCs are the resources (Bartlett & Ghoshal, 1987). A subsidiary of a MNC is not an autonomous company (Bartlett & Ghoshal, 1987), they may often benefit from their connection to the parent company in terms of centralized research and more beneficial conditions for purchase. But this connection may also enforce certain limitations on the subsidiary that DCs do not face (Luo & Tan, 1998). These include centralized management with its attendant limitations on the power of local managers and the necessity of fulfilling targets set by the parent company (Bartlett & Ghoshal, 1987). In the extreme case, the subsidiary can be a legal entity only enabling the headquarters a variety of value-adding operations (Birkinshaw & Morrison, 1995). Since the knowledge of headquarters as well as any other factors influencing the subsidiary strategy are related to the company, restrictions and advantages resulting from the connection to the headquarters are, for the purpose of this study, considered as resources and capabilities of the MNC. Similar reasons proposes Luo and Tan (1998), assigning the strategy-making differences to the restraints placed on the foreign companies. The first one is externally imposed by the environment, the second one is internally imposed by the role of the subsidiary in the means of competence and global-responsiveness setting.

Since resources and capabilities of MNCs and DCs and their fit with the environment are considered by the author to be the vital factor leading to disparate strategies pursued by these three types of companies and, subsequently, performance, the resource-based perspective has been adopted in this study in combination with environmental perspectives.

2.2 Domestic and Multinational Company

Strategic choices should flow mainly from the analysis of firm's unique skills and capabilities (Barney, 1986), and therefore both internal and external resources are crucial determinants of organizational strategy and performance (Barney, 1991). The author argues that since MNCs and DCs vary in the means of resources, these different types of firms are expected to employ divergent strategies in the similar environment.

The focus of this study is on the companies operating in the Czech Republic; hence both MNCs and DCs face up to the comparable environment in the means of environmental uncertainty. Still, strategies chosen by the companies might differ, so may the performance. The profitability of the firm depends on its technological and organizational resources, but also on its optimal match between the resources allocation and the environment (Wernerfelt, 1984). Different companies have different expectations about the future value of a particular strategy, and these differences reflect uncertainty in the competitive environment (Barney, 1986). Value was earlier a fundamental concept to both resource-based view (RBV) and relative competitive advantage. The RBV definitions of the value show that the degree of value held by each company is determined by the environment through opportunities and threats (Priem & Butler, 2001). If we assume that the set of environmental condition is similar for MNCs and DCs in the Czech Republic, the resources and the perceived environment might be the prerequisites for pursuing distinct strategies leading to variation in performance. A synthesis of the RBV and environmental perspectives has been emphasized in studies focused on RBV and its use in strategic management (Priem & Butler, 2001).

Albeit empirical studies have found significant differences among the strategic focus of MNCs and DCs (Pertusa-Ortega, José F., & Claver-Cortés, 2008; Anastassopoulos, 2003), their findings are often contradictory. Some authors (Luo & Tan, 1998) claim multinational companies often have organizational and technological know-how at their disposal which is more extensive than that possessed by domestic firms, enabling multinationals to opt for more innovative, proactive strategies than the domestic firms. Multinational companies often use an adaptive strategy (Fiegenbaum, Hart, & Schendel, 1996) and adapt to changing environmental conditions (Lavie & Fiegenbaum, 2000). Multinationals often spend more on marketing activities and research and development than do domestic firms, which tend to try to capitalize on their knowledge of the domestic marketplace (Anastassopoulos, MNE subsidiaries versus domestic enterprises: an analysis of their ownership and location-specific advantages, 2003). On the other hand, research by Ortega et al. (Pertusa-Ortega, José F., & Claver-Cortés, 2008) comes to the conclusion that it is more beneficial for domestic firms to use a combined strategy focusing on low costs and differentiation. Findings from empirical research are ambiguous though, and have come primarily from China and the USA, studies from European countries have been sparse.

2.3 Environment and Strategy

The importance of the environment for the organization and for achieving its goals has been widely recognized in the management literature (Bourgeois, 1980; Tan & Litschert, 1994; Desarbo, Benedetto, Song, & Sinha, 2005; Duncan, 1972). The normative literature within the business policy field emphasized scanning and assessing the environment and matching it with

organizational capabilities (Bourgeois, 1980). It has been proved in empirical research that managers in more uncertain environment usually tend to be more proactive and innovative, presuming a higher degree of risk (Miles R. E., Snow, Meyer, & Coleman Jr., *Organizational Strategy, Structure, and Process*, 1978). The organizational theory argues that certain environmental conditions influence the organizational administration and structure (Duncan, 1972). However, the consensus what environment is and how to apprehend it has not been reached so far.

In the earlier stages of management and organization research, specifically in the first half of the twentieth century, the environment was mostly ignored by the researchers, or at least held constant (Miles, Snow, & Pfeffer, *Organization-Environment: Concepts and Issues*, 1974). The importance of the environment of the organizations has been more recognized by researchers since the open-systems concept was introduced (Frishammar, 2006), which stresses the reciprocal ties that link the organization with the environmental (Burns & Stalker, 1961). Albeit various different approaches to the environment have occurred since then within different perspectives, systematic and exhaustive reviews of environmental perspectives are rare (Frishammar, 2006).

Environment is used to label the network of external influences and relationships in which each company is embedded (Miles & Snow, 2003 orig. 1978). The concept of the environment is elusive, as it may include every event on the world which has any effect on the activities of the organization (Pfeffer & Salancik, 1978). However, for understanding organization interaction with environment, this approach would not be appropriate. Every event confronting an organization does not have to be a factor actually affecting it (Pfeffer & Salancik, 1978).

For the purpose of this study, the environment is viewed through the lens of adaptive and resource-dependence perspective, since the author believes that the organization is able to adapt to various environmental conditions. Organizations are viewed as active and thus able to change as the environment changes. The world external to organizations is considered to constitute a real world that exists independently of an organization's perception of it.

Both the adaptive perspective and the resource-dependence perspective point to the importance of other social factors as important causes of environmental change, and to the importance of information when gaining the knowledge of the environment (Frishammar, 2006). The adaptive perspective gained a dominant position within organization theory, organization behaviour and management literature, either due to the prominent position of the realist paradigm in the field of strategy and environmental analysis or due to today's overrational view of manager and management (Frishammar, 2006).

2.4 Resources & Capabilities and Strategy

According to Barney, resources include both physical and intangible resources of the organization, and may be classified into three categories: physical capital resources, including the physical technology used in the firm, company's plant, equipment or access to the raw material, human capital resources, including experience, training, relationship or insight of the individual managers of the firm, and organizational capital including company's formal reporting structure, formal planning, informal planning, controlling and also relations between a firm and those in its environment (Barney, 1991). Furthermore, management skill may be also con-

sidered as a resource required for successful implementation of a particular strategy (Barney, 1986). In business-to-business markets, resources might be subdivided into external, including the value chain with various alliances, and internal including product development, engineering product interface or finance (Fredericks, 2005). Of course, some of these resources are not strategically relevant; some of them can even lead to strategies that reduce effectiveness and efficiency (Barney, 1991). Nevertheless, those attributes of the above mentioned categories of the firm resources that do enable a company to pursue strategy that improve its effectiveness and efficiency are, for the purpose of this study, firm resources (Wernerfelt, 1984).

2.5 Strategy Framework

There are two major typologies of strategies (Hambrick, 2003), Porter typology and Miles and Snow typology. However, further approaches to business strategy can be found in the literature, e.g. a high-performance “gestalts” proposed by Miller (Miller D. , 1990) or the three strategic types – operational excellence, product leadership, customer intimacy – described by Treacy and Wiersema (1997). With respect to the perspective adopted in this study and to dissimilarities between MNCs and domestic companies regarding empirical approaches to the research of the strategies employed by these two types of companies, the Porter’s typology has been chosen as a framework of business strategy. Porter’s typology reflects the corporate-level strategy.

Apart from pure differentiation strategy, pure cost strategy, and two focal strategies, also combinations of strategies are examined in this study and are depicted in Figure 1. Mixed cost strategy defines strategy of company pursuing either cost focus or cost leadership strategy, mixed differentiation strategy defines a strategy of a company pursuing either pure differentiation or differentiation focal strategy. Finally, the focal strategy includes focus on cost or focus on differentiation.

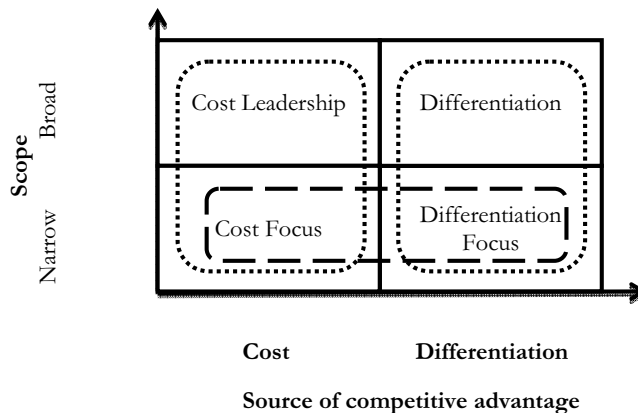


Fig. 1 - Examined Strategies. Source: Compiled by the author, based on (Porter, 1985)

2.6 Research Questions

General research questions:

- a) Are there differences among the choices made by MNCs and DC in the Czech Republic as regards strategy?

- b) What are the consequences of a particular strategy for MNC and DC?

Specific research questions:

- a) Do multinational and domestic companies in a competitive and hostile environment choose a particular strategy?
- b) Is a particular strategy chosen by MNC (DC) correlated with higher performance?

3. RESEARCH METHOD

The research literature was used to formulate a description of potential individual strategies chosen by companies and performance and business environment characteristics were selected. The research was implemented via a questionnaire directed at the CEOs of MNC and DCs in the Czech Republic.

The proposed questionnaire including the description of strategic choices and environmental characteristics was pre-tested with the sample of 10 respondents. Few necessary changes to the questionnaire were made.

The respondents, CEOs of companies, were questioned about the major strategy chosen by their firms and characteristics of the environment in which they do business. Environmental variables are to be averaged. The questionnaire was filled in by the researches personally during the interview with the CEOs.

Based on the character of chosen variables, a logistic regression model was subsequently employed to determine whether the strategies chosen by the firms are correlated with environmental variables, and a regression model was used to determine whether certain strategy choices are connected to higher company performance for multinational and domestic firms.

3.1 Environment

The environment as conceived in this study will be the perceived environment. The environment as perceived by management is more significant and relevant than any set of objectively measurable quantities (Miller D. , 1988). A further basis for selecting these variables is the fact that it is the perceived environment which influences managerial decision-making and thus the choice of strategy. Information on the perceived environment allows the researcher to see the environment from management's perspective (Tan & Litschert, 1994). The environment becomes known to the organization exactly through managerial perception (Miles, Snow, & Pfeffer, 1974). Information on the environment may thus be obtained from respondents. The focus will be on examining how organizations consistently respond to the surrounding environment.

The environment will be explored by examining two factors: the intense of competition and corruption. The variables and their descriptions have been selected by the author on the basis of empirical studies focusing on company strategies and their relationship to the business environment (Luo & Tan, 1998; Wright & al., 1995; Olson, Slater, & Hult, 2005). Lickert scale has been used by various authors for assessing environmental characteristics (see e.g. (Duncan, 1972)).

3.2 Domestic and Multinational Companies

For the purpose of this study, the subsidiary (here referred to as MNC) is a legal entity listed in

the commercial register in the Czech Republic, owned by a foreign legal entity. The domestic company is a legal entity listed in the commercial register in the Czech Republic, owned by Czech legal entity, without any foreign subsidiaries.

3.3 Strategies

Business strategy is concerned with how businesses endeavour to gain the competitive advantage (Varadarajan and Clark 1994). Because the competition in the global marketplace occurs at the business unit level (Porter M., 1986) and local firms are major competitors of MNC business units in host markets, it is reasonable to assess the environment-strategy relationship at the subunit level in comparison to domestic firms.

Managers of the firms sometimes depict the strategy, however, they have to adjust it or modify during the implementation. Except for companies with such articulated strategy (e.g. FedEx, see (Barney, 2002)), there are many other firms without precisely defined strategy, pursuing so called emergent strategies. The relationship among intended, deliberate and realized strategy was clearly depicted by Mintzberg and McHugh (1985). Since both the intended and the deliberate strategy often vary from the strategy finally realized by the firm, for the purpose of this study the realized strategy is to be examined, as managers cannot be sure whether the intended strategy will be realized without modification.

There is a number of possibilities for evaluating company strategies (Conant, Mokwa, & Varadarajan, 1990). A preliminary choice was made for this study to select strategies on the basis of a description; hence the data obtained will be represented using binary nominal variables. This method allows all of the strategies noted to be explored. The disadvantage of this method is subjectivity on the part of the respondent. Its advantage lies in the facility with which the data obtained may be processed and interpreted (Conant, Mokwa, & Varadarajan, 1990).

3.4 Performance

As in a number of previous studies, ROA has been chosen as an objective measure for this study (Banalieva & Santoro, 2009; Wu & Pangarkar, 2006). Although studies in international business have sometimes used other measures such as return on sales, in order to maintain maximum consistency with prior studies, ROA turned up to be more appropriate measure for the purpose of this study as ROA has been the most widely used measure of a firm's financial performance (Banalieva & Santoro, 2009). This indicator allows clear, rapid comparisons among firms of various sizes and business areas. Moreover, it is highly correlated with ROS (54%) (Banalieva & Santoro, 2009). Although there exist fundamentally more complex, sophisticated models to evaluate economic success, all the models share an identical basis. Contemporary researchers also incline to simpler methods for determining company success. The disadvantage of this indicator is its potential to be influenced by operating leases. This limit, however, is comparable to the limitations on other performance indicators.

3.5 Sample

The final sample included 133 domestic and 45 multinational companies. All of these companies belong to the branch G according to CZ-NACE classification and have more than 10 employees. Concretely, 75 % of companies have less 10-99 employees, 25 % of companies

have 100-249 employees. To avoid foreign natural persons who are not representing any multinational company, the criteria of legal entity and number of employees have been employed – particularly the Limited Companies and Joint-Stock Companies have been chosen.

3.6 Data collection

Primary data were collected in multinational and domestic companies in the Czech Republic through personally administered questionnaires in 2009. Secondary data were collected from annual reports of companies, available via company web pages, commercial register or Credit Info database.

Following previous research (Hambrick, 1983; Snow & Hrebiniak, 1980; Desarbo, Benedetto, Song, & Sinha, 2005; Nandakumar, Ghobadian, & O'Regan, 2010), questionnaires were directed at the Chief Executive Officer (CEO) level of multinational and domestic companies in the Czech Republic, or a competent member of the management. CEOs are said to have the best overview of the company's strategy (Zajac & Shortell, 1989; Pertusa-Ortega, José F., & Claver-Cortés, 2008).

4. RESULTS

Firstly, the environment-strategy literature was examined. The logistic regression model was run on data from DC as well as from MNC. For the domestic companies, results indicate that the environmental variable competition is positively related to mixed differentiation strategy (i.e. pure differentiation strategy and differentiation focus strategy) at the significance level $\alpha=0,05$. Thus, the differentiation strategy is therefore found to be predominant strategic orientation selected by the domestic companies in competitive environment. The results are depicted in Table 1. For the MNC, no predominant strategy has been indicated.

Tab. 1 - Results of logistic regression on domestic companies: environment-strategy. Source: Author

Dependent variable: differentiation			
	Coefficient	Std. Error	p-value
const	-1,37357	0,760712	0,07098
competition	0,45239	0,176175	0,01023
corruption	-0,116067	0,139827	0,40650

McFadden R-squared 0,037518

Also the performance implications of a company's strategic choice were tested, since performance is one of the crucial goals of the companies. The results show that for domestic companies, their predominant strategy, mixed differentiation strategy, makes contributions to the profitability of the companies at the significance level $\alpha=0,05$. The results are depicted in Table 2. Therefore, for domestic companies to compete in competitive market, a differentiation strategy is the most advantageous strategy. On the other hand, for the MNC subunits, it was found that the focus strategy is positively related to the performance of the company at the

significance level $\alpha=0,1$ and results are depicted in Table 3. For both models, tests (Breusch-Pagan, White's) indicated that heteroskedasticity is not present and normality of residuals was confirmed.

Tab. 2 - Results of regression on domestic companies: strategy-performance. Source: Author

Dependent variable: 1_ROA_2007				
	Coefficient	Std. Error	t-ratio	p-value
const	1,84211	0,133929	13,7543	<0,00001
diferentiation	0,361274	0,180776	1,9985	0,04774

R-squared=0,029586

Tab. 3 - Results of regression on multinational companies: strategy-performance. Source: Author

Dependent variable: 1_ROA_2007				
	Coefficient	Std. Error	t-ratio	p-value
const	-2,4508	0,199046	-12,3128	<0,00001
focus	0,582169	0,273562	2,1281	0,04113

R-squared=0,123980

5. DISCUSSION AND CONCLUSION

The strategies employed by multinational and domestic firms have only rarely been empirically examined and compared in this manner to-date. The authors of partly similar research in China (Luo & Tan, 1998) recommend carrying out similar studies in other countries. With knowledge of the strategic choices made by the companies it is possible to some extent predict the future development of an organization (Miles & Snow, 2003) and its future strategic choice.

This paper may bring benefits at the theoretical level concerning whether multinational companies and domestic companies active in the Czech Republic choose varying strategies in response to a competitive environment. The key results of this study suggest that for multinational companies' subunits and local enterprises, adoption of heterogeneous strategy-environment configurations can be beneficial in terms of financial performance, even when they compete in the same industry. The study has proved that domestic companies in response to competitive environment choose mixed differentiation strategy, including pure differentiation strategy and differentiation focus strategy. This can be driven by, on one hand, the endeavor of domestic companies to differentiate from their competitors, because they often cannot lower the cost to reach the price level of large multinationals, on the other hand, by their proper knowledge of local markets. Multinational companies are not homogeneous in their strategy choice in response to the environment.

Benefits will also come at a practical level. This study has several implications for both multinational companies' executives and local firm managers. A considerable contribution of this study lies in determining whether a particular strategy is associated with higher performance of the business. When operating in a competitive environment, multinational companies need

to be innovative and adaptive to preempt business opportunities, but not immensely proactive and aggressive to mitigate operational uncertainties. The focus strategy is according to this study positively related to the performance for multinational companies. In order to prosper at the market of the Czech Republic, multinational companies need to focus either on narrower group of customers who can be addressed by lower prices or by a special product. To the contrary, for domestic companies, the differentiation strategy makes contributions to the profitability of the companies. The more competitive the environment, the more domestic companies tend to use differentiation strategies – and those are related to a greater performance for them. It is therefore essential for domestic companies to differentiate the product, either for broader or narrower group of customers, in order to prosper in the Czech Republic. The large part of Czech markets has been taken away from Czech companies by multinationals, and those domestic companies, which have survived, need to offer unique products to maintain the market share and financial performance.

Of course, the strategy of domestic companies can be to a large extent accompanied by export strategies, since the market in the Czech Republic has become smaller for domestic companies with the presence of multinational companies. However, domestic companies can still survive at their domestic market, and with carefully chosen strategies defend the home market. These should be not only aligned with the environment properly, but also they should take into consideration the strategies used by foreign competitors.

To conclude, output of this study may serve as the basis for decision-making in companies already active in the Czech marketplace and, particularly, as important entry information for companies considering entering the market. Further research could explore the possibility to predict with some reliability the structural characteristics that are associated with a chosen strategy. Future research can also show if particular strategies do require specific styles of management.

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Contact information

Ing. Sylva Žáková Talpová

Department of Corporate Economy, Faculty of Economics and Administration

Masaryk University

Lípová 41a, 602 00 Brno, Czech Republic

E-mail: talpova@econ.muni.cz

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