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Do First-Mover Advantages Really Matter for Internet Ventures in Emerging Markets? A Study of Localization and Platform Envelopment Capabilities on New Venture Growth

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Abstract

In the past decades, first mover advantages have been discussed widely as one of the critical success factors of venture performance. However, recent phenomena in emerging markets such as Indonesia show that late entrants in the Internet venture sector have better performance compared to the pioneers. The late entrants' Internet ventures start with not only a single service, but also multi-bundled complementary services. Therefore, the platform envelopment phenomenon, an entry path effort that utilizes existing competitor platform network effects, is happening. The platform envelopment, as well as localization activities, is widely seen in successful Internet ventures. Our research proposal aims to explore how these capabilities can help late entrants in Internet ventures achieve better growth rates than the pioneers. Furthermore, we also explore the organizational theory approach that discusses the role of new venture team prior experience and entrepreneurs' social networks, especially business resources networks, as the factors that help in the development of platform envelopment capabilities.

Keyword: Internet ventures, growth rate, platform envelopment, localization, dynamic capabilities, entrepreneur's social network, business resource network, late entrants, entry order.

1. Introduction

In rapid-growth markets such as emerging markets, there is consensus that being a pioneer in the market with outstanding products or services is very critical to creating successful new ventures. In this context, the first movers have several advantages ranging from economic, pre-emptive, technological, to behavioral (Nakata & Sivakumar, 1997). Furthermore, classic literature on first-mover advantages mentions that the pioneers tend to outperform the late entrants (Lambkin, 1988). Besides the advantages, the first-mover startups also have some challenges such as an uneducated market, changes in consumer tastes, changes in technologies, free-rider effects (consumer education, information spillover, skipping trials and errors), incumbent inertia (lock-in of assets or resources, organizational inertia), as well as an

enhanced level of information (resourcefulness, shared assets or experience) (Cho et al., 1998). These challenges often make the Internet ventures run out of cash. Their survival rate is pretty low even though the startups are considered as first movers within the industry with support from investors (Chang, 2004).

By having the advantages and challenges, the remaining question for first movers is whether the first-mover advantage really matters for performance. Interestingly, the recent phenomenon in the Internet ventures area shows that first movers do not always achieve sustainable performances. For instance, Friendster and Food Panda, the first movers for social media and food order applications, respectively, in Indonesia, have had difficulties growing further because of the fierce competition from late entrants with more complete and complementary functionality such as Facebook for social media and Go-Food from Go-Jek for food order applications. In past literature, there are also some discussions about latecomer advantages that make the entrants catch up with the first movers and early movers (Cho et al., 1998; Zhang, 2010).

Nowadays, there are a bunch of Internet application services created every day in Indonesia that offer not only the software functionality but also a business model to support society's daily activities. In order to produce innovative and breakthrough products or services in a relatively shorter time, some digital startups initiate benchmarking to successful foreign startups that originate from more developed countries. Then, they try to create clones of their products or services (example: Tokopedia clones Alibaba), and others try to create localizations of the applications by adjusting them to the local context (example: Go-Jek localizes Uber). The adjustments vary from business model, payment system, platform resources, and so on.

These kinds of startups usually attract much attention from the public if they can enter the market, especially the millennial generation, quite well (Lingelbach, 2012). Due to their popularity, they may achieve significant early stage growth. This situation attracts other users to join the platform and increases the platform value as a result of network effects (Parker and Alstyne, 2005). Furthermore, significant growth may attract investors to do series funding investment (Chang, 2004). In fact, the significant growth of the startups mostly does not come from the firms' retained earnings; instead, it is triggered by the resource injection such as capital or human resources from investor funding (Chang, 2004). The nature of Internet ventures is the need for a significant growth rate until a certain point to survive, scale, and sustain (Guo et al., 2016). Therefore, the main objective in this stage is more into growth seeking rather than profitability seeking.

Even though the market opportunity is huge, the efforts for any Internet ventures services to be used by the public to support their daily activities are far from easy. For the first movers, they may face problems such as an uneducated market that makes the retention cost quite high. On the other hand, the late entrants will have difficulties in heavy competition with existing Internet ventures platforms in the market that makes the customer acquisition cost quite high. The nature of Internet ventures themselves is that they need a critical mass of users in order to start utilizing the network effects within their platforms (Gawer & Cusumano, 2008; Parker & Alstyne, 2005). The sustainability of the Internet ventures itself also depends on the utilization of network effects. This situation triggers the Internet ventures to start with not only a single service, but also multi-bundled complementary services. Therefore, the platform envelopment phenomenon, an entry path effort that utilizes existing competitor platform network effects, occurs. The attacker's platform combines its own functionality with the target's platform functionality in a multi-platform bundle that influences shared-user

relationships (Eisenmann, 2011).

There are several examples of platform envelopment in Indonesia. Go-Jek localizes Uber's technological aspects and performs platform envelopment against several services such as conventional taxi bikes, Food Panda, courier services, and even Uber itself. LINE localizes the existing messaging application and adjusts it to the local context through its digital content. It performs platform envelopment against another messaging application and even mobile games. Tokopedia localizes Alibaba and also performs platform envelopment against forum-based marketplaces such as Kaskus or Indowebster. These Internet ventures achieve a significant growth rate in a relatively shorter time than others.

The previous literatures on platform envelopment have been discussed in terms of its concept (Eisenmann, 2011), resource transformation (Mohagheghzadeh & Shavn, 2015), and also some empirical studies (Kazan & Damagaard, 2016). However, there is limited discussion about the development of platform envelopment capabilities. In the strategic management area, given that dynamic capabilities are the antecedent of firm performance such as growth rate (Teece et al., 1997; Eisenhardt & Martin, 2000), the discussion about how platform envelopment capabilities are developed to achieve a significant growth rate is quite important. One of the objectives of this research proposal is to fulfill this gap through an organizational theory approach that discusses the role of the new venture team's prior experience and the entrepreneurs' social networks, especially business resources networks, as the factors that help in platform envelopment capabilities development.

The past literatures have discussed various resource-based view (RBV) and dynamic capabilities perspectives as determinants for Internet ventures' growth, but the discussion about the effect of entry order on their performance because of firm capabilities is still limited. We will also explore the localization and platform envelopment capabilities that discuss entering the competitors' platform market but still do not discuss Internet venture growth as the consequences and entry order as antecedents. Therefore, our suggested research question is how localization and platform envelopment capabilities can help late entrants achieve a better growth rate than the first movers or pioneers. All in all, this research proposal aims to propose a model that can fill this gap as well as add to the contribution within Internet venture performance literature.

2. Conceptual Background

2.1. *Latecomer Advantage*

Despite the disadvantages of being latecomers, such as consumers' switching costs (consumer loyalty, uncertainty, transaction costs), preemption competition (input factors, production capacity, market-side opportunities), and the learning by doing process (technological leadership, learning curve effect, overcoming market complexities), previous literature mentions that latecomers also have some advantages, such as changes in consumer tastes, changes in technologies, free-rider effects (consumer education, information spillover, skipping trials and errors), incumbent inertia (lock-in of assets or resources, organizational inertia), as well as an enhanced level of information (resourcefulness, shared assets

or experience). In order to overcome the disadvantages, latecomers come up with some strategies such as focusing, thin margin or loss bearing, and volume building. Having the advantages of latecomers, they utilize them with some strategies such as odd timing, time compression, human-embodied technology transfer, benchmarking, aggressive capital investment in new technology and equipment, and resource leveraging (Cho et al., 1998). Other literatures discuss additional advantages and strategies of latecomers, such as utilizing learning curve effects (Zhang et al., 2010), the mechanism of overtaking competition and innovation (Kim, 2012; Fan, 2006), and the competitive implications of emerging markets (Mpoyi, 2011).

2.2. *Dynamic Capabilities in IS/IT Perspective*

In the platform perspective, especially in two-sided platforms or multi-sided platforms, the user base is the most valuable resource to deliver better value due to network effects (Peteraf & Bergen, 2003). The process of managing the platform itself can be categorized as dynamic capabilities since the activities recombine the user base as valuable resources to produce a multi-platform bundle as new value-creating strategies (Eisenmann, 2011; Eisenhardt & Martin, 2000). This kind of dynamic capabilities is also seen in any literatures on multi-sided platform development such as platform design and development (Hagiu, 2009), managing platform openness (Eisenmann, 2009; Parker & Van Alstyne, 2008), adopting coring and tipping strategies (Gawer & Cusumano, 2008), managing the level and asymmetry of network effects (Bakos & Katsamakas, 2008), managing platform participation (Yoo et al., 2007), managing network effects and forward-looking behavior (Iansiti & Zhu, 2007; Evans & Schmalensee, 2007), and managing two-sided platforms (Rochet & Tirole, 2006; Eisenmann et al., 2006).

Beside some econometrics approaches, in RBV perspective, these literatures pay much attention to the user base and its network effects as the antecedents of dynamic capabilities. The discussions about other antecedents of dynamic capabilities in the IS/IT-related area are still limited. Thus, the area is a good opportunity for research.

2.3. *Aligning Platform Envelopment and Disruptive Business Models*

At the beginning, the classic theory from Christensen (1997) mentioned that disruptive innovation is triggered by a technological point of view that addresses unserved new customers, usually price-sensitive non-consumers who do not need full-featured products or services, and therefore use 'inferior' products or services in 'normal' metrics but have higher capabilities in other metrics. These 'inferior' products or services might develop and gain momentum until they disrupt existing technology for the mainstream market. The concept was broadened to include both the technological side and the business model side (Christensen and Raynor, 2003). It was called a disruptive business model. Markides (2006) shows that disruptive business model innovation invades existing markets by providing new performance attributes from the customer point of view, simply redefining products or services and the methods for delivering value to customers. Christensen (2006) stated that adding the disruptive business model concept to disruptive innovation was very important since some cases for disruptive technology are actually business model problems, not technology problems. A single technology can be commercialized to the market by using a different business model (Chesbrough, 2007). Moreover,

every new technology invention or innovation actually needs a business market to bring it to the market (Chesbrough, 2010). Therefore, even if the incumbents have higher technology or are superior in disruptive technology metrics, they still can be attacked through disruptive business model innovation. For this reason, the term 'disruptive technology' is relative to the context. Furthermore, since the impact for the incumbents is still the same as with traditional disruptive technology (Christensen, 1997), disruptive business model is placed under the umbrella of disruptive innovation (Christensen, 2006).

Disruptive business model studies and strategic management literature align in many areas. First, from the firm's functionality perspective, the business model is creating and appropriating economic value (Zott and Amit, 2007; Chesbrough, 2007; Zott et al., 2011). Second, from a competitive analysis perspective, business models support the competitive advantage of the firm (Markides and Charitou, 2004), become one of the main elements of firms' competition (Casadesus-Masanell and Ricart, 2010), show the market position of the firm (Christensen, 2001), and inform market strategy (Zott and Amit, 2008). Third, from the firm transaction point of view, the business model explains the economic exchange, such as the value proposition for each stakeholder (Zott and Amit, 2008; Zott et al., 2011). The change of the business model components can change these three strategic management perspectives as well, resulting in disruption for the incumbents. Some firms also conduct merger & acquisition activity to drive disruptive business model innovation (Christensen, 2011).

The current widely discussed topic in the Internet ventures area, the sharing economy, is considered a significant disruptor for several industries (Zervas et al., 2014; Firnkorn & Muller, 2012). However, not all disruption is included in disruptive innovation theory (Christensen, 2015; Schmidt & Druehl, 2008). There are two kinds of disruption in disruptive innovation theory: low-end disruption and new market disruption (Christensen, 1997). It is common that the sharing economy creates consumers from non-consumers because the resources are obtained from peers platform members. From a supply-side perspective, the peers become micro-entrepreneurs by using their idle resources. Obviously, the majority of the peer members are not in the same business previously. The motorbike driver for Go-Jek can be anyone as long as they have a motorcycle with a valid license. Since the services offered by idle resources have different characteristics compared to the mainstream ones, the consumers from the demand side could be existing consumers in certain businesses or even non-consumers previously. Hence, the sharing economy model drives new market disruption.

In some studies, innovation in emerging economies is often correlated with disruptive innovation (Hang et al., 2010; London & Hart, 2004; Markides, 2012; Ray & Ray 2011; Schanz et al., 2011). Multinational companies drive innovation through adjusting the local context and then import the innovation to other emerging economies as well as developed economies for the low-end market. Over time, the results of the innovation may disrupt the mainstream market. The sharing economy model mostly disrupts the mainstream industry through an innovative business model that utilizes information technology. However, because of information technology, the sharing economy sometimes starts from the high-end market, which does not suit disruptive innovation theory. On the other hand, information technology also enables firms to offer more flexible services from idling resources such as products, skills, space, tasks, etc. This situation is able to create low-end disruption. For example, a motorbike taxi equipped by a mobile application with lower performance than a taxi in terms of convenience in commuting may disrupt taxis with the ability to reach any place faster. All in all, the sharing economy can act as disruptive innovation depending on its context.

The platform envelopment concept, coined by Eisenmann (2011), can also be seen as the disruptor for existing platforms. The attackers' platform attempts to achieve critical mass by acquiring the user base from the target platform. The multi-bundled services from the attackers' platform make the industry more integrated and harder to define specifically (example: Go-Jek is not only focused on the transportation business but also focused on several kinds of services). Even though platform envelopment activities approach is quite similar to head-to-head competition with a better offering, from the disruptive trajectory perspective, platform envelopment follows the trajectory path of new market disruption. For instance, Go-Jek acquires the Food Panda users who need transportation services through the Go-Food service. Thus, platform envelopment can be categorized as disruptive innovation.

2.4. *New Venture Teams' Prior Experience*

New venture is defined as the early stage of development and growth of any firm based on the age or size (Klotz et al., 2014; Amason et al., 2006; Zahra et al., 2000). Prior experience has been widely discussed as one of the most critical inputs in the new venture team domain that affects the outcomes of new ventures (Klotz et al., 2014). Shared prior experience will provide advantages for new ventures in terms of the strategic decision process that is related to firm performance (Baum & Wally, 2003; Kor, 2003; Eisenhardt & Schoonhoven, 1990). Prior functional experience helps new ventures' competitiveness significantly as long as it is aligned with the new ventures' competitive strategy (McGee et al., 1995). It is also related to the chosen strategic choices (Shrader & Siegel, 2007).

The diversity of prior performance also received high attention among scholars. The heterogeneity of the new venture team's prior performance affects significantly the firm performance in dynamic industry environments when the team is directed by a directive leader. In contrast, the homogeneity of prior performance works better with an empowering leader. The situation will be opposite when it is applied to stable industry environments (Hmieleski & Ensley, 2007). Most university-based new ventures have homogeneous teams with less developed dynamics than independent new ventures. Hence, independent new ventures have higher performance in terms of revenue growth as well as net cash flows than university-based new ventures (Ensley and Hmieleski, 2005). These literatures relate new venture prior experience to firm performance. In the strategic management literature, firm performance is the consequence of dynamic capabilities (Teece et al., 1997; Eisenhardt & Martin, 2000). However, in this matter, the new venture teams literatures have limited discussions about the relationship between the teams and dynamic capabilities. Following the strategic management logic, they may have some relationships.

2.5. *Business Resource Networks*

Entrepreneurs have three types of social networks based on the utilities to support new venture growth, including the advice network, emotional network, and resource network (Aldrich, 2003). The advice network supports entrepreneurs in terms of sensing opportunities for new products or services, facilitating specialized knowledge, new technology development, and several changes in the business landscape (Batjargal, 2007; Batjargal, 2003). The emotional network supports entrepreneurs to get emotional stability and psychic resources to grow their new ventures despite the obstacles

and risks (Anderson et al., 2005; Reynolds & White, 1997; Bruderl & Preisendorfer, 1998). On the other hand, business resource networks enable entrepreneurs to integrate various resources, including financial capital, supplies, labor, and new technologies (Batjargal & Liu, 2004; Stuart & Sorensen, 2007; Shane & Cable, 2002). These resources, accessed from the entrepreneurs' network, allow them to develop the capabilities for growing the firm (Lechner et al., 2006).

The entrepreneurs develop the network to acquire resources, especially from strong ties such as family or inner circle relationships (Pages & Garmise, 2003; Aldrich, 1999; Jack, 2005). It is very crucial in the early stage because entrepreneurs will have difficulties acquiring resources such as financial and labor without successful track records (Zimmerman & Zeits, 2002). However, some previous studies mention that strong ties such as family ties are essential in the early stage but limit long-term growth because the available resources from them are often limited (Jack, 2005).

2.6. *Internet Venture Growth and Performance*

The most important measurement for Internet venture performance is growth rate. As mentioned above, it is the metric that determines the survival and possibility to scale for Internet ventures. The literatures in IS/IT research discuss the determinants of Internet venture growth with various RBV and dynamic capability perspectives such as resource bundling strategy (Guo et al., 2015), opportunity and resource exploitation (Ge et al., 2016), investment decision-making (Eisenmann, 2006), IPO and strategic alliances (Chang, 2004), knowledge-based view (Lin, 2013; Saarenketo et al., 2009), growth strategy preferences (Zou et al., 2010; Bertoni et al., 2013), new venture teams (Batjargal, 2007; Klotz et al., 2014), investor type (Bertoni et al., 2013), and also entrepreneurs' social networks (Batjargal et al., 2007; Batjargal et al., 2013; Arregle et al., 2013; Li et al., 2015). Most of these literatures show that Internet venture growth stage strategies have path dependence on their resources and capabilities. These growth strategies also result in different performances.

3. Theory Development & Hypothesis

We developed the conceptual framework for this study as follows:

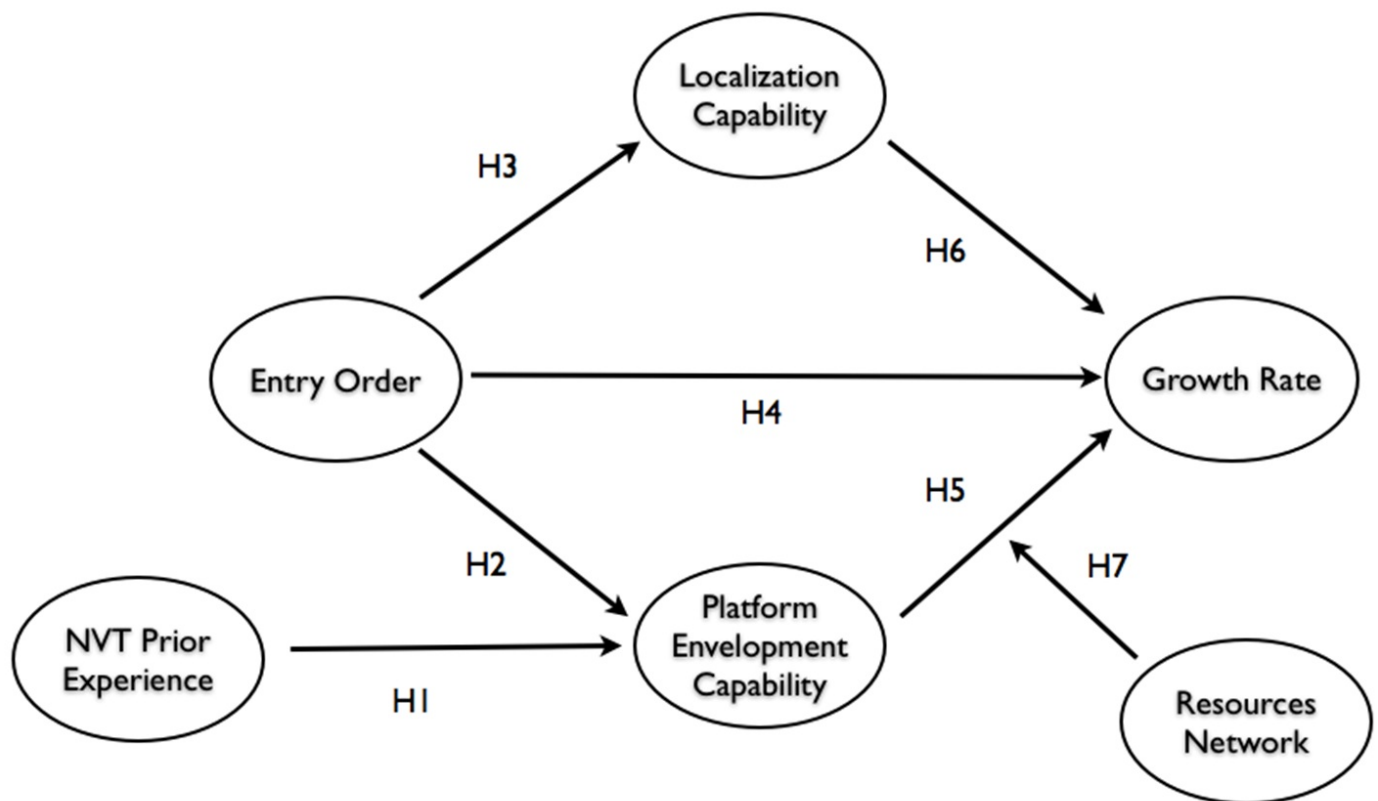


Figure 1. Conceptual Framework

This model describes the main research question about how localization and platform envelopment capabilities can help late entrants achieve a better growth rate than the first movers or pioneers. Furthermore, it also depicts how platform envelopment capabilities are developed and result in enhancing new Internet ventures' growth. We also include the business resources networks construct as a part of platform envelopment capabilities development.

In the next section, we will explain the conceptual framework more deeply and suggest some research propositions. We use three categories of entry order as suggested by Lambkin (1988) that consist of first mover, early mover, and late entrants. We derived the dynamic capabilities into IT/IS perspectives that are defined as managing platform capabilities, especially in platform envelopment capabilities (Eisenmann, 2011). We also use several growth rate variables that are mainly used for measuring the performance of the Internet ventures such as user base growth, revenue growth, and number of transaction growth as suggested by Guo et al. (2016).

3.1. Research Hypotheses

We define platform envelopment capabilities as the capabilities to acquire the user base from another overlapping platform with multi-bundled complementary services. In order to become the platform leader, Internet ventures should adopt a coring strategy to create centrality, as well as a tipping strategy to achieve momentum and critical mass (Gawer & Cusumano, 2008). Since the initiatives need to adapt the existing platform functionality, prior experience can help the firm to understand, implement, or innovate the process. Furthermore, prior functional experience is able to enhance the new

venture's competitiveness significantly when it is aligned with the competitive strategy (McGee et al., 1995). Because prior experience is also related to strategic choice (Shrader & Siegel, 2007), the choice to take platform envelopment as the entry path cannot be separated from it. Thus, we can formalize this phenomenon into Hypothesis 1 as follows:

- **H1:** *The new venture team prior experience will positively affect platform envelopment capabilities*

The network effects create the self-reinforcing feedback loop from demand-side or supply-side economies of scale and lead the firms to the winner-take-all competition (Evans and Schmalensee, 2002). Each Internet venture needs a certain amount of user base to kick-start the network effects. They have the option either to acquire the users from a clean-sheet user or an existing platform's user (Reinartz et al., 2005). In a digital platform perspective, clean-sheet users are more costly to acquire than existing platform users since it needs more effort to educate them. The alternative entry path that can be used is platform envelopment. Late-entrant Internet ventures can rely on existing platforms by tapping into them and utilizing shared user relationships as well as common functionality (Eisenmann, 2011). Furthermore, since the future is more unpredictable, most Internet ventures nowadays are taking the entrepreneurial path as effectuation. The effectuation venture principle firm will set the goals based on the resources that they have. Hence, they tend to use a resource bundling strategy such as platform envelopment to achieve venture growth (Guo et al., 2016). In this matter, late entrants have advantages since they have an existing platform to attack with more educated users. Thus, we can formalize this phenomenon into Hypothesis 2 as follows:

- **H2:** *The entry order will negatively affect the platform envelopment capabilities*

As mentioned in the previous section, the common latecomer strategy is benchmarking the existing ones (Cho, 1998). The late entrants to Internet ventures relatively have more benchmarks than early movers. Furthermore, they may enjoy the free-rider effect. These advantages will be amplified with the combination of IS/IT dynamic capabilities such as localization, which is considered as part of platform design and development capability, and also adapting coring and tipping strategy (Hagiu, 2009; Gawer and Cusumano, 2008). Thus, we can formalize this phenomenon into Hypothesis 3 as follows:

- **H3:** *The entry order will negatively affect the localization capabilities*

In the Internet industry, the first movers tend to have more competitors due to duplication as well as platform envelopment attacks. Hence, they should prepare some defensive strategies such as opening up the platform for strategic alliances purposes or matching up the attackers' platform with multi-bundled services (Eisenmann, 2011). Both strategies need extra efforts. Opening up the platform means co-investing in the platform development and also creating a differentiated version to meet the underserved customers previously (Eisenmann, 2008; Parker & Van Alstyne, 2008; Eisenmann, Parker & Van Alstyne, 2009). Since the first movers need more resources to keep the firm sustained from the attackers' platform, they should keep investing their earnings for this purpose. This action reduces the investment allocation for growth-seeking purposes. Thus, we can formalize this phenomenon into Hypothesis 4 as follows:

- **H4:** *In the Internet industry, the entry order will negatively affect the Internet ventures' growth rate*

The platform envelopment is the method to acquire a certain existing platform market, but it does not rely on Schumpeterian innovation that offers outstanding products or services in order to overcome the target platform network effects or switching costs. Instead, the attacker's platform utilizes the target's platform network effects that protect the incumbent previously (Eisenmann, 2011). The attacker's platform combines its own functionality with the target's platform functionality in a multi-platform bundle that influences shared-user relationships.

Eisenmann (2011) also mentions that the platform envelopment efforts are more likely to succeed with several conditions: the attacker's and the target's platform users overlap significantly, the attackers utilize price discrimination benefits, or there is high economies of scope. High user overlap in Internet ventures happens when the function of the target platform is associated with the complement function of the attacker platform. Price discrimination plays a role in platform envelopment when the attackers can provide better pricing as the result of functionality bundling (Nalebuff, 2004). This bundling will work when the common user base uses both services frequently. Lastly, high economies of scope can appear when the attackers are able to bundle their functionality with the target functionality quite well (Evans and Salinger, 2005). Hence, the attackers are able to sell the bundle of functionality with a single message and utilize the cost-sharing opportunities. The user base itself can be seen as the best opportunity to be exploited (Ge et al., 2016). Thus, we can formalize this phenomenon into Hypothesis 5 as follows:

- **H5:** *Platform envelopment capabilities will positively affect the Internet ventures' growth rate*

One of the critical success factors of a multi-sided platform is the adoption of coring and tipping strategy (Gawer & Cusumano, 2008) as well as platform design and development capability (Hagiu, 2009). Localization consists of these two capabilities through managing the adoption of technological capability from more developed markets. Thus, we can formalize this phenomenon into Hypothesis 6 as follows:

- **H6:** *Localization capabilities will positively affect the Internet ventures' growth rate*

Platform envelopment efforts will be more successful when the new Internet ventures have sufficient resources to acquire the user base from the target platform with multi-bundle complementary resources. In the platform development context, the platform itself should enhance the value for the platform members (Hagiu, 2009). Since the multi-sided platform consists of users with multiple sides, it needs more resources to attract the entire user sides than a single platform. The lack of resources will make potential new Internet ventures perform the platform envelopment process ineffectively. If the critical mass is not reached, the network effects will not work for a significant amount of the user base.

Since it is quite difficult to acquire tangible resources for early-stage Internet ventures, the business resource networks take an important role in helping entrepreneurs fulfill the needed resources (Zimmerman & Zeits, 2002). The strong ties, such as family ties or inner circle relationships, may help the potential capabilities to achieve higher performance by providing the resources at a much better rate and willingness than the markets'. However, in the long run, this help may limit venture growth because of limited resource stock or conflict possibility (Arregle, 2013). Thus, we can formalize this phenomenon into Hypothesis 7 as follows:

- **H7:** *The entrepreneurs' business resource network will moderate the relationship between platform envelopment capabilities and the Internet ventures' growth rate at the early stage*

4. Further Research

We will develop the operationalization method based on the research model for further research. Then, we will design and perform the quantitative research method with the managers of Internet ventures in Indonesia who are involved in or understand the localization and platform envelopment initiatives as the unit of analysis. They can be the local founding teams, business development or business strategy division, or the top management teams. Some qualitative research methods may be used to explore the unclear variables.

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