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**AALBORG UNIVERSITY**  
DENMARK

Master of Science in Economics and Business  
Administration, International Business Economics

## How Internationalisation Make Impact on Circular Economy

Jaspreet Kaur

Supervisor: Mohammad Bakhtiar Rana

## **Acknowledgement**

Primarily, I would like to express my sincere gratitude to my thesis supervisor, Mohammad Bakhtiar Rana. He always gave his precious time in my research project and provided his innovative ideas and constructive criticism for improving my project for which I am grateful to him. He was always there guide me through direct or digital supervision meeting. Secondly, I would like to thank all teachers and staff of Aalborg University. Last but not least I would express gratitude to my family and friends for encouragement and motivation for finalizing the project within the specific time.

## **Abstract**

Circular economy helps to eliminate environmental problems. Not only environmental problems but it also contributes to the better performance of the international business. The main aim of this thesis is to reflect how the circular economy is affected by OLI theory of Internationalisation. The following research project consists of two parts systematic literature review and qualitative case study of H&M and ZARA.

This research paper attempted to find how one sourcing of materials influence the implementation of the circular economy and how companies face challenges while implementing it. This thesis has endeavoured to contribute to the circular economy literature by explaining through the relation of OLI paradigms.

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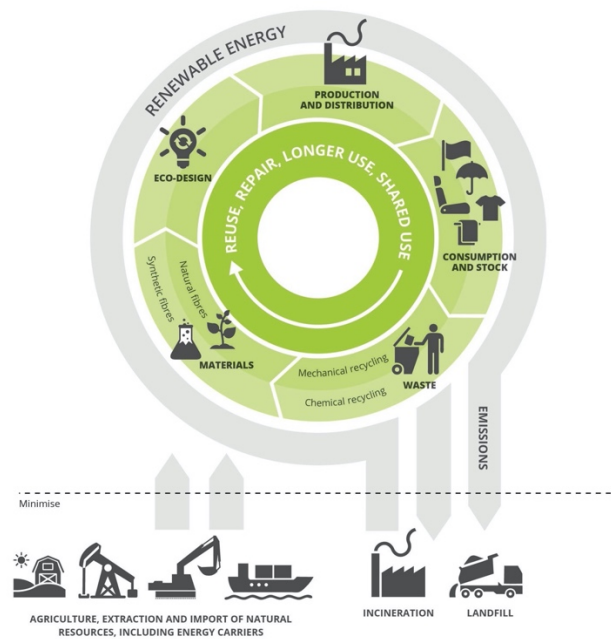
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# How Internationalisation make impact on circular economy

## CHAPTER 1: Introduction

The Circular Economy is gaining popularity in the business world. Circular Economy has been described as an industrial economy that relies on the restorative capacity of natural resources and goal to minimize if not eliminate- waste, utilize renewable sources of energy and cut off use of harmful substances. (Rizos et al., 2015). The circular economy concept can help to solve environmental problems at the global level such as overconsumption of resources. A circular economy needs changes in productions and consumption patterns and value chains.

The textile industry, including the fashion industry, has a significant environmental footprint all over its value chain. It includes natural fibres, such as cotton and wool are produced large areas of agricultural land and a huge amount of water, energy and chemicals and while processing manufactures also use fossil fuels. The use of chemicals has a significant impact on water. In the using stage, washing, and drying of textiles results in important water and energy use as well as the release of chemicals and microplastics into rivers and waste management. According to reports in 2015, greenhouse gas emissions from textile production approximately 1.2 billion tons of carbon dioxide equivalent, higher than international flights and shipping combined. (Manshoven, et al., 2019). Textile industries are one of the most polluting industries in the world. The consumption is increased in the textile industry because of fast-changing affordable fashion as the consequences it harms the environment. (Vehmas et al., 2018)



### **Vision of circular economy in textile industry** Source- (Manshoven, et al., 2019)

According to the Eionet Report 2019, not only the environment but the textile industry has a large number of social impacts. In the 2019 survey of US executives within the automotive, electronic, food and agriculture and health care industries, 78 % of these companies have already adopted or plan to adopt the circular economy framework, as they know the importance of this strategy to their future competitiveness. (*Learning from consumers: How shifting demands are shaping companies' circular economy transition, 2020*). The present EU approach scene is fairly waste-centric with a majority of waste-related mandates and guidelines, concentrating on the advancement of a 'waste hierarchy' management framework. Although, in a perfect world, such a framework would help to waste minimization and expanded reuse and recycling, in all actuality the present circumstance in the EU is a long way from this. Current product-related policies could not gain the desired resource efficiency way. The switch towards CE would be enabled by devolvement of policies. (Milios, 2017)



As the given figure below, this thesis will be divided into seven chapters. The first chapter's aim to provide introduction to the reader to the context of the research, background, description and problem formulation include research questions and problem justification. In 2nd chapter methodology part, paradigms in social science, a paradigmatic approach will be addressed. In the next chapter, the literature part the topic of research will be explained. I will define the Internationalisation and circular economy and how it works in terms of operations and production, outsourcing & insourcing of materials and how C.E correlated with customers orientations, and what are the challenges of C.E for companies. In the findings and discussion chapter, I shall explain the acquired results and findings according to the research questions and problem statement. Afterwards, in the conclusion part, a summary of the accumulated knowledge will be included. Overall, the thesis will be ended by the reflection of the study, which I come across while the research process.

#### **Research process**

chapter 1	Introduction
chapter 2	Methodology
chapter 3	Review of literature
chapter 4	Discussion and analysis
chapter 5	Major finding
chapter 6	conclusion
chapter 7	References

CHAPTER 1.1: Problem formulation

The objective of this chapter is to provide the reader with a better insight into how the problem was formed and what made the author choose this topic. Due to the global pressure companies are indulging into green practices and production of textile is increasing usage of natural resources and energy, excessive usage of water, toxic chemicals such as dyeing stuff. As a result, it is affecting the environment and society. Some of the companies have started implementing Circular economy because it develops closing loops and uplifts the Recycling and reuse concept.

Linear	Circular
Raw materials & waste	Raw materials only
Competition	Collaboration
Individuals	Ecosystem
Do less bad	Do good and positive
Added value	Shared value
Standardized production	Local and updated production
Downcycling	Upcycling

Figure. circular economy as a paradigm shift, Source- (Hemkhaus, et al., 2019)

This research paper aims to reflect what supports the adoption of circular economy's concept in production and operations of MNCs. Existing papers have not emphasized how internalisation context impacts MNCs circular economy. The following paper will use H&M and ZARA as case studies to show how one company has been able to adopt a circular economy despite externalization mode of sourcing as compared to a company with mostly internalized sourcing.

The major justification for choosing Circular economy is the sheer fact that the circular economy in companies is taken more seriously and companies want to make an impact on the environment, it can also influence the performance of the company. In business world competition is increasing day by day that's why companies want to create a value for their customers, so they are choosing circular economy. H&M is one of the leading companies in adopting circular economy.

The data will be collected through secondary data then will be analyzed to provide major findings. Based on the background research and the gaps in the available literature, the problem formulation and research questions are formed.

## CHAPTER 1.3: Research Questions

1. What underpin, to adopt circular economy concept in MNCs production and operation?
2. How and why the adoption of the circular economy concept is affected by the ownership, location, and internalisation issues?
3. How one company has been able to adopt a circular economy despite outsourcing as compared to a company with mostly internalized sourcing?
4. How it is influenced by customer orientations?
5. How circular economy is challenging?

## CHAPTER 2: METHODOLOGY

The methodological chapter will provide insights about the methods and tools to answer the problem formulation of this study. Various procedures undergone from choosing the methods of collecting the data and analyzing the to get the findings. The methods of the research and the philosophical positions of the study will be presented in this chapter. The chapter starts with philosophical position of the research study.

### CHAPTER 2.1: Philosophy of Science

Researcher must have clear understanding of research approaches. Paradigms refers to different thoughts, principles which the researcher has been used. There are four philosophical assumptions which are basis of the research, i.e ontology, epistemology, methodology, human nature philosophy of sciences contains two main viewpoints objectivist and subjectivist (Kuada,2012)

<b>Dimensions</b>	<b>The Objectivist Approach</b>	<b>The Subjectivist Approach</b>
<b>Ontology</b>	Realism	Nominalism
<b>Epistemology</b>	Positivism	Antipositivism
<b>Human</b>	Determinism	Voluntarism
<b>Methodology</b>	Nomothetic	Idiographic

Figure- The Objectivist-Subjectivist Dispositions in social science, Source (Kuada,2012)

**Ontology** - Ontology is defined as “the study of being” it asks questions like “what kind of world we are investing and structure of reality” and “ what is known and reality”. In the ontological assumption’s scholars assume that human beings have their own thoughts, interpretations and meanings. Then Researchers have to focus on opinions, feelings, experiences and inner thoughts. (Ahmed, 2008) There are two kinds of ontological assumptions, i.e. Objectivist and subjectivist. Objectivism ontology philosophy means one reality of the world and subjectivism ontology relies on multiple reality because of different human perceptions. Realism means world is real and world is tangible and made up of immutable structures. Nominalism is concerned about reality is constructed by individual integration with each other. (Kuada,2012) Realism ontology relates to physical world and it reflects cause-effect relation. (Ahmed, 2008)

This study project holds the realistic ontology because the data gathered from the literature review hence it has same applicability in same situation regarding circular economy in textile

**Epistemology**- Epistemology explains the nature of knowledge and the means of the knowledge, “how we know what we know” (Kuada,2012) It deals with nature of the knowledge and authors focus on how to go to uncover the adequate and legitimate knowledge. (Al-Saadi, 2014). Epistemological philosophy contains two assumptions, i.e. positivism and antipositivism. Positivism reflects that when authors can be objective and conduct investigations as an external observer. Antipositivism defines as socially constructed when researcher involves in social actives to gain the knowledge. (Kuada,2012)

This study holds positivism epistemology because study collected data about internationalization and circular economy activities in fast-fashion retailer companies. Hence there was no chance of data influence by author because researcher analyze as an external observer. There is no involvement of personal perceptions as a result this study has the objectivist approach.

**Human Nature-** It explains the perceptions of the researcher towards the human existence. (Kuada,2012) Determinist is authors activities completely determined by the situation or environment. On the other hand, voluntarist approach researcher autonomous and free willed. (Burrell and Morgalm, 1979) This study paper has features of determinist view point due to the objectivist approach.

**Methodology-** It provides information the choice and use of particular methods in the research process. How researcher can move further to acquire data. If researcher believes he/she can objectively observe the information from outside, then researcher will choose methodology that stresses on examination of relationships. On the contrary side if researcher required primary data by interactions of humans then he/she will go with the methodology that explores real experience of individuals. Nomothetic approach is concerned with the systematic protocol and survey-based studies and ideographic approach when researcher gets close to the people to gain the information. (Kuada,2012) As this paper has adopted the objectivist approach then this paper holds the nomothetic methodological approach because author acquired the knowledge as an external observer from exiting literature and reports.

## CHAPTER 2.2: Practical Research Methodology

This chapter refers to the data collection procedures of the dissertation. Data can be classified into two categories such as primary data and secondary data. Primary data is first-hand data collected by individuals, focus groups directly. Secondary data refers to collection of existing data such as company reports, government publications, computer databases etc. (Osang, et al., 2013)

Systematic literature review refers to identifies relevant studies, synthesize the data and summarize the evidence. **(Khan et.al, 2003)** This study carried out is the systematic literature review. The research work uses a document analysis to acquire relevant information, and grey literature has been used for research due to limited scientific research is done on this topic, it includes European government, business and company reports of H&M and ZARA.

At initial stage Aalborg university library's online website has been used which provided the opportunity to get access to a vast amount of publisher's website. Then some filters have been used to get more specific results. Mainly articles have been reviewed. Then some key words used such as "Circular economy", "circular economy and operation and production", "circular economy and internationalization theory" so on. The selection of papers then went through a

reading of the abstracts to get an overview about the paper. The methods of studies and results have been highlighted. Some of the keywords used in the thesis work for literature. These words are used in combination with each other.



Figure- List of Keywords

To conduct a systematic literature review following 5 steps approach has been used. In this study firstly, research questions have been formed through previous literature gap. what underpin, in terms of internationalization theory, to adopt a circular economy concept in MNCs production and operation? How and why the adoption of the circular economy concept is affected by the ownership, location, and internalization issues? How one company has been able to adopt a circular economy despite outsourcing as compared to a company with mostly internalized sourcing? How it is affected by customer orientations? To conduct literature, review the searcher for studies has been done. To get accurate and legitimate data, assessment of the papers followed. The fourth step is to summarize the works of literature for data synthesis. Last but not least step interpreting the finding, after data analysis the research has got some concrete findings.



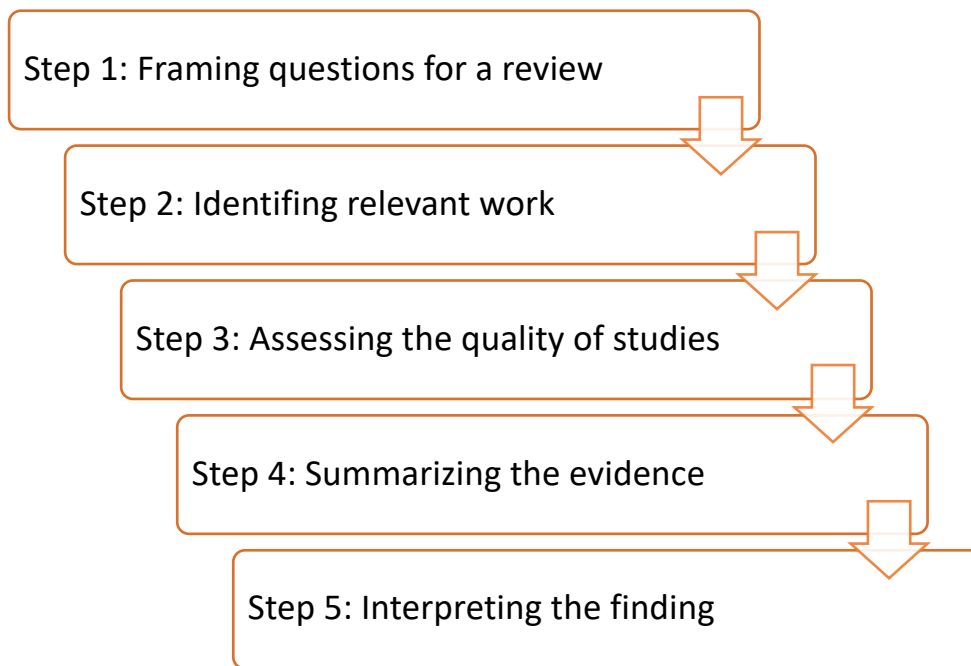


Figure-Five steps to conducting a systematic review **Source- (Khan et.al, 2003)**

## CHAPTER 3: REVIEW OF LITERATURE

### CHAPTER 3.1: INTRODUCTION

To write a literature review of this project, the literature review is divided into four major categories such as Internationalisation, circular economy and role of C.E in operations and production and C.E & sourcing and C.E & customers orientation.

### CHAPTER 3.2: INTERNATIONALISATION AND CIRCULAR ECONOMY

#### **Internationalisation**

The present globalization wave presents two primary parts: the globalization of the business sectors, a move towards a solitary world market with a greater level of integration and reliance, and the globalization of production, the developing element of organizations to

secure merchandise and ventures in various and remote areas, to find beneficial procedures in like manner to costs, quality prerequisites and accessibility of manufacturing factors. (*Batalla, 2015*).

## **Theory**

Throughout the history of theories, most of the economic theories' factors of international business activity based on assets, whether these assets be owned or accessed by the MNE's nevertheless, in the past two or three decades, the structure and significance of competitiveness enhancing assets have changed. Firms become more knowledge-intensive and relationally based who have tangible resources and intangible capabilities. And their geographic sourcing and growth have become more widely spread. (Dunning and Lundan, 2008)

### **CHAPTER 3.3: OLI PARADIGM**

The eclectic paradigm or OLI paradigm explains the internationalization firm process. To move further each step must be fulfilled. The main purpose of this model is to find out and observe the elements affecting the commencement and development of foreign production. There are major three conditions should be satisfied for outward FDI, 1. The firm must have ownership advantages over companies from other nations in serving a specific national market. 2. These ownership advantages must be exploited when used with inputs in a foreign country, 3. It should be beneficial for the company to use these ownership advantages itself rather than sell or lease them. (Eden and Dai, 2010)

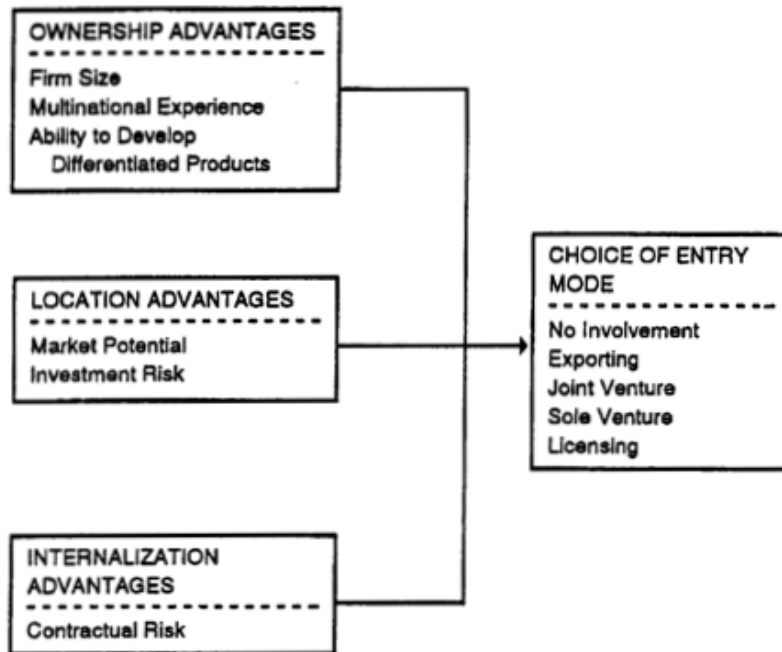


Figure- A schematic Representation of entry choice factors, Source-(Agarwal and Ramaswami, 1992)

## 1. Ownership Specific Advantage

Ownership advantages of a company are based on the monopolistic right possession about 5 particular assets such as Technology access of the company, team management knowledge, economies of scale, unique commercial idea and brands. However, all of these assumptions that the market is imperfect and recognizing the existence of market imperfections that create companies' competitive advantage. (Batalla, 2015). According to Chowdhury, 2015, define ownership advantage is where a firm capable to establish themselves through their brand name. trademark, superior production mechanism etc. study also explain that ownership specific advantage has been used as a significant issue in internalization besides this it can

make an impact on the overall performance of a company. To cite an example “coca-cola” has a famous brand name that enables them to attract the market all over the world.

Ownership advantages is First important thing before internalization. ownership advantages help to make a decision regarding buying or make. Parent companies putting pressure on subsidiaries companies for integrating knowledge and material flows and government engaging with companies in subsidiary companies. Ownership advantages consist of both human and physical assets. Two types of advantages are quite similar assets-based advantages (Oa) and the economics of common governance Ot and Oi should have a different category. They provide a pillar to the company to establish new asset-based advantages, provide better economies of scale and scope. Oa advantages basis of human skills and knowledge in the subsidiaries. OI advantages support Ot and Oa advantages by creating a reputation. I advantage involves formal and informal institutions such as code of conduct, norms and corporate culture of the company, in international context institutions may arise some problems such as corrupt government. OA advantages also related to the resource-based view. it reflects that firm can hold the complete position if assets are valuable, rare and difficult to imitate or substitute. (Lundan, 2010) Dunning has Explained 5 phases of ownership advantages in OLI. In mark I, ownership advantages through single-plant, multi-plant, multi-country. He stated that this trio of ownership advantages is geography-based because one plant location, multiple plant location and finally locations in multiple countries. (Eden and Dai, 2010) In the internationalization context, there are involves some risks regarding contracting such as the risk of deterioration of quality of services but these risks can be eliminated by enforcement of specialized knowledge to the contractual company. To reduce the investment risks in ownership advantages companies, possess a high degree of control modes on products and technology (Agarwal and Ramaswami, 1992)

Advantage	Contents	Outcomes
Oa	<p><i>Property rights and/or intangible asset advantages</i></p> <p>Product innovations, production management, organizational and marketing systems, innovatory capacity, noncodifiable knowledge; accumulated experience in marketing, finance, etc. Ability to reduce costs of intra and/or inter-firm transactions (also influenced by Oi).</p>	Efficiency Market power
Ot	<p><i>Advantages of common governance</i></p> <p>Advantages of scale and scope of the multiplant firm.</p> <p>Advantages specifically derived from multinationality itself (also influenced by Oi).</p>	Organizational effectiveness
Oi	<p><i>Institutional advantages</i></p> <p>The formal and informal institutions that govern the value-added processes within the firm, and between the firm and its stakeholders. Codes of conduct, norms, and corporate culture; incentive systems and appraisal; leadership and management of diversity.</p>	Legitimacy and trust resulting from nonmarket effectiveness

Figure- The nature and content of different ownership advantage Source- (Lundan, 2010)

## 2. Location-Specific Advantages

Location advantages include economic, political or institutional factors in the targeted countries. It is more likely that companies will invest in target countries if these advantages add up to the ownership advantages of a company. Most of the foreign operations are influenced by a major element such as market potential regarding growth and size. (Fischer & Roy, 2019). If a company decides that other companies produce or sell its products in a foreign market, it will be done through license and franchise contracts. However, if the company decides to manufacture in the foreign market itself. The company has to analyze location factors to decide on which company they are going to choose. In this case, if conditions are not ideal, to avoid the loss of its core business and core competencies the firm can decide just to export to foreign markets. On the other hand, if all conditions are suitable for manufacturing and marketing in foreign countries through the establishment of the subsidiary, the company will go further with foreign direct investment. (Batalla, 2015). Whereas according to Hessel's imperial study has revealed that this factor may include the availability of cheap labour, adequate resources of raw material in the targeted country. (Chowdhury, 2015)

Ownership and internationalization are integrated into an "organization" factor and location divided into two separate parts "place and space". Place defines is location-specific attributes and space focus on geographic distance. It refers to resource allocation from headquarters to subsidiaries. Whereas firms have to tackle several difficulties if they set up subsidiaries in unstable host countries. The study showed that cultural and institutional distance also affects slowly over time. (Dai, Eden and Beamish, 2013)

In the host the country, the investment can be in the risk due to uncertainty over the present economic and political conditions and government policies in the country. That is why it is researchers have suggested that companies should invest FDI in a country who has restrictive policies. Location advantages also affected by the market potential of the host country it indicates market size, growth potential. (Agarwal and Ramaswami, 1992) according to study, companies tend to more successful when they choose the market that is at greater psychic distances from the home country(Bhardwaj, Eickman and Runyan, 2011)

### **3. Internalization Advantages**

Internalization mainly emphasizes on primary transaction cost in the OLI paradigm. The main question arises here is to outsource or to internalize a process. (Fischer & Roy, 2019) The international advantages of OLI paradigm give information about the firm's propensity to internalise cross-border imperfections in the market. (Dunning and Lundan, 2008)

It refers to the company to develop ownership advantages at home country then should transfer these advantages to particular nations according to location advantages, through FDI which encourage the company to internalize the O advantages. There is a close relationship between O and I advantage because O advantages must be internalized. According to Dunning not only knowledge, brands, organization structure and managerial skills but the cultural, legal, and institutional environment and industry market pattern is also involved. Internationalization based on firm-specific advantages (Rugman, 2010)

## CHAPTER 3.4: ADOPTION OF CIRCULAR ECONOMY IN TERMS OF OPERATIONS AND PRODUCTION

In this resource-constrained world, the global ecological footprint of human activities has increased. However, the linear economic activities resources are continually consumed, and production processes do not consider their unsustainable exploitation of earth's natural resources and impose risks in the long run to society. On another hand, if linear production replaces by circular production then substantial resource efficiency improvements can be gain. The major new circular economy components are reuse, repair, remanufacturing and recycling for resource-saving strategies. (Milios, 2017) In a circular business model, materials flows are retained through closed-loop processes, so that by this loop valuable resources are not lost but can be reused as result companies can control wastage. (Mugge, 2018)

The production and consumption of textiles are globalized with numbers of producers and billions of consumers escalate over the world in highly linear value chains involving raw material extraction, production, transportation, consumption and after use- disposal.

Whereas, the European Union is the major importer of textiles, particularly from Asia.

Asia provides production in low labour cost. In circular production main aim is to reduce production waste and the energy, material and water consumption. Overproduction is a major problem in the textile industry, it can be improved by the push to pull sales model and support firms to produce demand-driven products. (Manshoven, et al., 2019)

The C.E concept emphasises on closing loop in the production-consumption by adopting restorative systems towards a better balance between economy, society and environment It' main objective to efficient usage of natural materials, reduce the wastage, enlarge utility of



products and reduce the carbon emissions. There are several types of methods of the circular economy like Cradle-to-cradle, sustainability, industrial ecology, blue economy, circular business models, closed-loop value chain, green supply chain and closed supply chain. (Santibanez Gonzalez, Koh and Leung, 2019) Ecodesign plays an important role in the production process of the circular economy because eco-design considers durability, long-lasting style, and design for disassembly. Eco designs need innovative designs and professional education of designers. Most important it requires knowledge, technical expertise, tools, training and new technologies and recycled products have a long process, so it takes time to produce. (Manshoven et al., 2019)

Circular economy saves material cost from recycling and reuse of materials, a closed-loop system refers to a multiplier effect in the supply chain to increase the investment and consumption. (Tseng, Chiu, Liu and Jantaralolika, 2020) there are two kinds of Environmental strategies 1. Reactive and proactive. Reactive strategy refers to a strategy which is helping to solve already existing problems and proactive approaches refer to prevention from the occurrence of the problems. With these strategies for firms is it convenient to create competitive advantage. Proactive environmental consists cost reduction through less wastage, proper usage of materials. (Chen, Ong and Hsu, 2016) Recycling material is a key component of the circular economy, but the quality of recycled textile material is lower. It shows that systematic sorting of fabric wastes and optimization of shredding parameters is crucial because it makes the production of yarns high quality. (Ütebay, Çelik and Çay, 2019)

Themes and focuses	Skills and competences
<b>CIRCULAR VALUE CHAIN</b>	
- <b>Materials and resources</b>	<ul style="list-style-type: none"> <li>- <i>finding the right suppliers of ecological materials</i></li> <li>- <i>acquiring new knowledge to process reclaimed material</i></li> </ul>
- <b>Ecodesign</b>	<ul style="list-style-type: none"> <li>- <i>Adopting, mastering and implementing eco-design skills</i></li> </ul>
- <b>Manufacturing and recycling</b>	<ul style="list-style-type: none"> <li>- <i>zero waste manufacturing</i></li> <li>- <i>Reverse thinking</i></li> <li>- <i>Applying new technologies to support ecofriendly and circular (re)manufacturing</i></li> </ul>
- <b>Retail and consumption</b>	<ul style="list-style-type: none"> <li>- <i>-New business models</i></li> <li>- <i>-servicizing</i></li> <li>- <i>-green marketing skills</i></li> </ul>
<b>TRANSVERSAL COMPETENCES</b>	
- <b>Sustainability and environmental management</b>	<ul style="list-style-type: none"> <li>- <i>Sustainability</i></li> <li>- <i>Environmental management</i></li> </ul>
- <b>User centered approach</b>	<ul style="list-style-type: none"> <li>- <i>Cocreation</i></li> <li>- <i>Trust and transparency</i></li> <li>- <i>Personalization</i></li> </ul>
- <b>Entrepreneurship</b>	<ul style="list-style-type: none"> <li>- <i>Creativity</i></li> <li>- <i>innovation</i></li> </ul>
- <b>Systems thinking</b>	<ul style="list-style-type: none"> <li>- <i>Collaboration and networking</i></li> </ul>

Figure- Major skills for circular economy. Source- (circular economy in the textile and footwear industry skills and competences for a sector renewal, 2019)

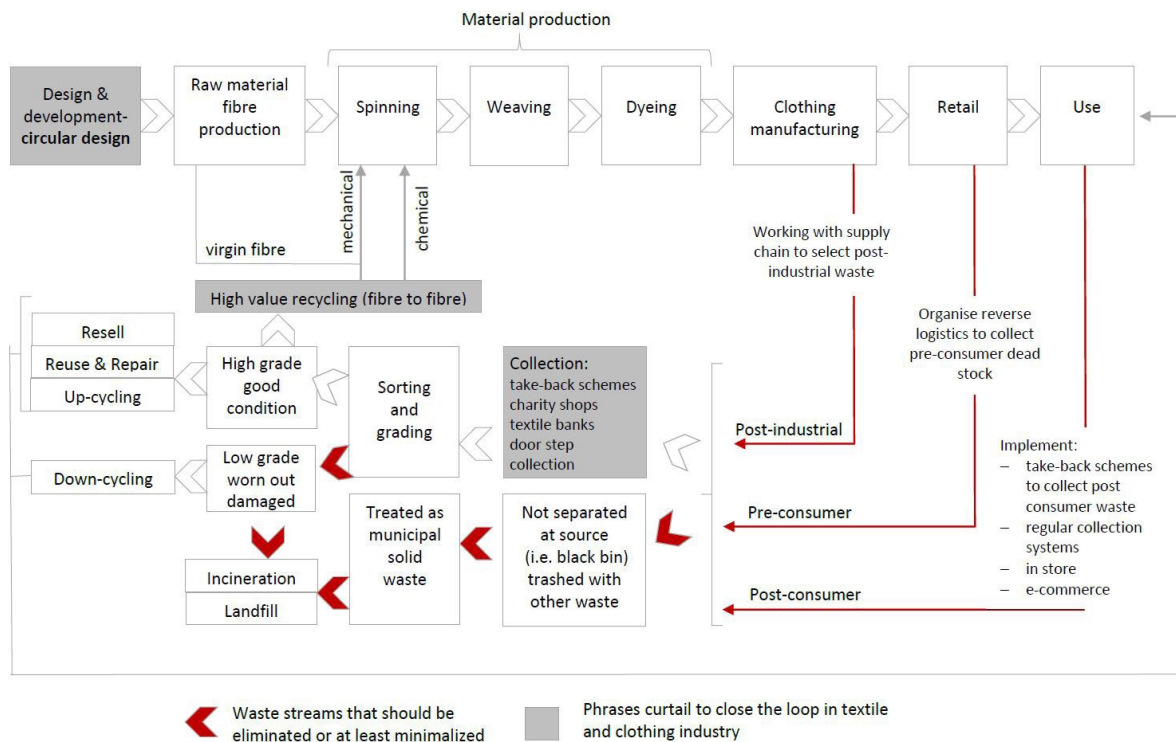


Figure- Closing the loop in the textile and clothing industry — a way to zero waste supply chain. Source- (Koszewska, 2018)

To grow the circular economy in the business A change in the attitude of consumers and producers is necessary regarding durability, repair, reuse, recycling. Lease based services such as leasing of cloths and carpets can help to generate durable and repairable designs. It is important to effectively organize the collection of used textiles and putt into sorting procedures and processing technologies to manufacture recycling fibre. (Manshoven et al., 2019)

To make effective use of the resources and move to renewable inputs includes these following factors; innovative new material suitable for a circular economy, remove barriers to adopt textiles production methods, make viable improvements in the production process, collaboration with retailers and manufacturers, innovative processes to use less water(Circular Fashion - A New Textiles Economy: Redesigning fashion's future, 2020)

There are 3 major stages of production as collection, recycling and waste treatment. The collection is a key phase of recycling; several collection systems have been installed by brands and public authorities. Most brands take back their clothes collection for product resale, reuse or remanufacturing. Another way is to reuse as Material. Companies use Fabric to upcycle products. Upcycling is a handicraft activity by creative individuals, but some professional designers are also encouraging it. it can be used as the production of children's clothing, reuse fabrics, for example, hotel linen etc. last way is waste prevention, waste can be minimizing through imposing some taxes or bans on incineration and landfills (Manshoven et al., 2019)

#### CHAPTER 3.5: CIRCULARITY AND OUTSOURCING

Supply chains include suppliers, manufacturers, distributors and retailers, consumers and other third-party partner and recyclers. These supply chain actors make an impact on the environment and economic performance. (Ameknassi et al, 2017)

Nowadays, Products and services are sourced globally. Sourcing could be components, sub-assemblies, modular assemblies and OEMs come from any part of the global. There are several reasons why companies choose sourcing globally such as low-cost manufacturing and tariffs, trade agreements between trade bloc countries, countertrade policies, environmental laws, the core competence of the specific company or nation. Despite that, customers demand's increasing, they can have a wide choice and proliferation of standards.(Yuen & Cheng, November 2013,)

Outsourcing is defined as the procurement of products or services from sources that are external to the company. Other authors also defined outsourcing situation as reallocation of production from one place to another. Domestic outsourcing involves a firm within the country of the outsourcing firm whereas, international outsourcing means to a firm outside

the country of the outsourcing firm. International outsourcing is becoming a popular way of sourcing of products & services such as India, have made foreign outsourcing a government priority and have agencies set up to keep up the easy transition of foreign-based firms into Indian outsourcing markets. (Schniederjans and Zuckweiler, 2004)

Outsourcing; the paper defines when an activity transfer from internal governance to external control. The theories such as transaction cost economics (TCE), resource-based theory (RBT), extended resource-based theory (ERBT) are used to explain the occurrence of sourcing. How much organizations ought to consider outsourcing of individual segments could be organized around two parts of the continuum, referred to as “major doers” (in-house dominance with complementary outsourcing) and “major buyer” (outsourcing dominance with complimentary in-house activities. (Nordigården et al., 2014) International outsourcing is braced in the economic theory of comparative advantage. In the context of international trade, if an outside company, nevertheless of its geographic location can perform activities more efficiently than an outsourcing company, the outsourcing firm should allow the outside company to do the work anywhere in the world and outsourcing firm focus on what they do better than other companies are called core competencies. Core competencies are a significant factor in the firm for long term survival in respective markets. (Schniederjans and Zuckweiler, 2004) It is clear that domestic outsourcing does not give any cost benefits but it minimizes the risks related to demand uncertainty, late and unreliable deliveries, maintenance of machinery. As a result, in-house strategy in the home country can be considered if feasible. (Sardar, Lee and Memon, 2016)

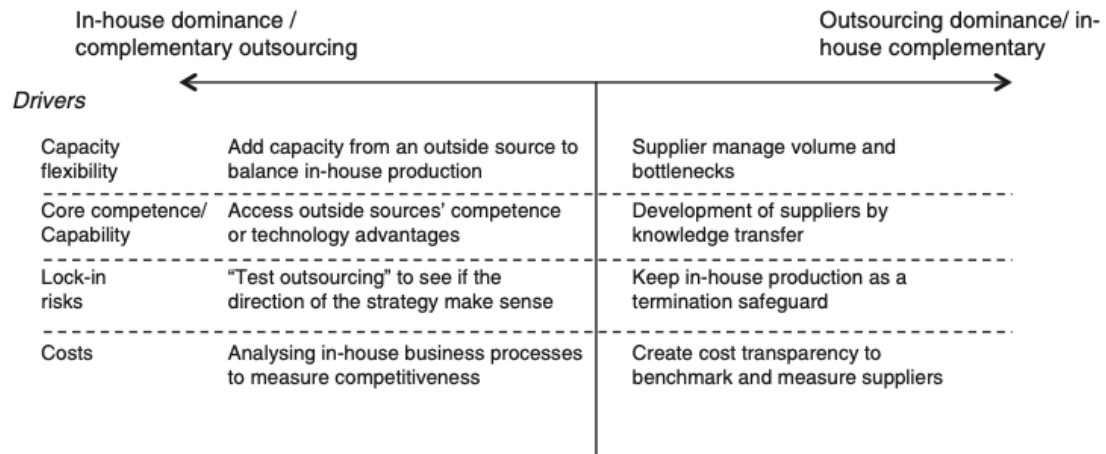


Figure- drivers for a mixed strategy Source-Nordigården et al., 2014

There are certain constraints must be taken into consideration in the purchasing decision.1. the demand must be satisfied, determine what quantities must be ordered to meet the demand, 2 the initial stocks present and the desired end stocks, 3. A safety period should be included if supplier delivery is unreliable as a result late delivery can occur some other expenses like replanning, adjustments, reception and invoicing 4. Purchasing conditions may include regarding minimum and maximum purchasing quantities from particular suppliers, which can be set either by the supplier or by the buying company, the discount must be accurately fixed, for example, suppliers often give a certain percentage of discount on the total price, 5. Purchase decision may also influence by specific local conditions. (Degraeve and Roodhooft, 1999) There are the main three-pillar for successful outsourcing- strategic analysis, selecting the providers and managing the relationship. (Embleton and Wright, 1998)

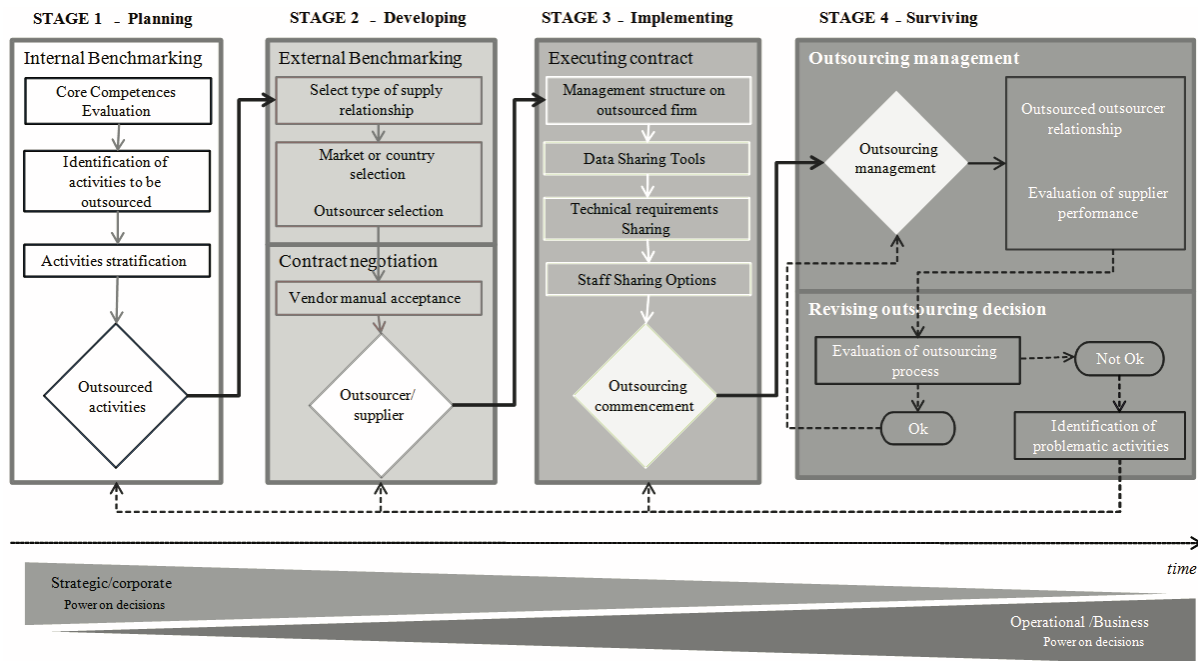


Figure: Source- (Moreira et.al 2015)

As per the given figure, there are four main stages of international outsourcing in the apparel industry. First and foremost is the stage of planning; in the international outsourcing process, an internal evaluation analysis is conducted to know which activity might be outsourced. It involves- (a) core competencies evaluation; the most common core-competences are design, branding, marketing. (b) identification of the activates to be outsourced; in the fashion industry they mostly choose operational activates to outsourced, (c) stratification of activates; if selected outsourcing activates are more than one, the company must prioritize. Most companies select to outsource is primary activity which involves assembly also known as cut-make-trim. Usually, companies prefer design activity in-house because of the company's competitive advantage. The second stage is developing, at this phase firm conduct an external benchmarking analysis to choose a suitable supplier. Next stage is implementing, in the implementation stage the outsourced company transfer all the important information and material by the outsourcer to complete the contract, they can share some technical, personnel and physical information. Last but not least stage is surviving stage it consists of the

management of the outsourcing relationship and a post-outsourcing analysis. (Moreira et.al 2015)

International outsourcing has some benefits such as cost-saving & time saving, core activities, create a corporate culture, greater flexibility and good quality by the specialist in a particular area. (Embleton and Wright, 1998) However, there is some hindrance such as customer deadline, destination lead time, risk and uncertainty. (Sardar, Lee and Memon, 2016) there are some other drawbacks such as control over the provider, quality of services, contract costs, providers have multiple buyers as a result they may not be able to give priority to each one. (Embleton and Wright, 1998). We should not neglect the social consequences of outsourcing. A tragic example of outsourcing to developing countries was an accident on 24 April 2013 in Bangladesh, when the Rana Plaza five-story building collapsed outside Dhaka because the structure of the building was not strong enough to balance, the owner built the top 3 floors illegally without permission and more than 1000 workers were killed.

Bangladesh is the largest exporter of clothing after China. The Bangladeshi factories produced apparel for renowned brands including Phantom Apparels, Phantom Tac, Ether Tex, New wave and German companies. A piece of shirt costs 3 US dollars in Bangladesh the same shirt costs over 13 US dollars in the united states. Some of the companies like Zara withdrew business from Bangladesh after this tragedy. (Chudzicka, 2013)

There are some of the risk factors such as currency exchange rate variability, use of non-tariff barriers, government and legal polities stabilities, social-cultural differences, (Schniederjans and Zuckweiler, 2004) In textile companies performance depend upon the quality of materials, speed up delivery and flexibility to change according to customers. There are some strategic procurement management factors helps to increase the level of service by sourcing such as supply base optimization, information sharing with suppliers, long term orientation



with customers, purchasing integration, creation of key suppliers, internal coordination.  
(Yuen, 2012)

### CHAPTER 3.6: Insourcing

Insourcing is defined as to begin performing in-house production activities. According to the business dictionary, “delegating a job to someone within a company”. All definition emphasized the job allocation to someone within the company rather than someone from outside the company. (Chudzicka, 2013)

There are 8 insourcing determinants such as 1. *Communication*- it is easier to communicate when the production process is in-house and when geographical space is lessened, 2. *Employee morale*- employees dedication level increases when workers know that their work efforts will be appreciated and rewarded, 3. *Control*- it is more convenient to evaluate things and quality control when sourcing is nearby, 4. *Security*- it includes safety and freedom from danger and risks. It reduces doubt and anxiety, 5. *Transportation*- Insourcing eliminates product transportation delivery problems and costs, 6. *Innovation*- some of the studies showed that insourcing R&D makes better results than outsourcing the same, 7. *Customer satisfaction*- customers are more concerned about the quality of goods rather than the price, so insourcing help to maintain the quality of production to take care of customer satisfaction, 8. *Speed to market*- not only price and quality affects the buying decisions but speed to market is also important. Insourcing eliminates delivery delays. (Sikula et al., *Insourcing; Reversing American outsourcing in the new world economy*)

Insourcing is acquiring popularity in business. Production factories, assembly plans mainly back to America from China and other cheap labour countries. Bangladesh is the world ‘largest manufacturer of clothing after China. Some of the famous companies like Zara withdrew the contract of production after the tragedy in Bangladesh (Chudzicka, 2013)

## CHAPTER 3.7: CHALLENGES OF CIRCULAR ECONOMY

Europe moving towards the circular economy. Implementation of C.E has some key barriers.

C.E barriers are classified into four categories such as cultural, technological, market and regulatory. These following barriers are closed to each other. Business is unable to develop more **circular designs because of lack of awareness and interest of consumers it comes under cultural barriers. Another main issue is the lack of technology to implement**

**C.E.** (Kirchherr et al., 2017) In the circular economy, the design stage is defined by the product performance. The designers and engineers of products will tackle the challenges

because design the sustainable product is not easy due to the blend of the fibres. To

implement the circular economy, it requires new design philosophies and more capable teams and resources efficient solutions. Another challenge is advance technologies, companies face

problems regarding lack of quality materials due to lack of advance machines for recycling

(Koszewska, 2018) Supply chain actors play a relevant role in C.E. so, according to the study the impact of fashion changes, standard and regulations willingness to pay for circular

products affect the circular production. (Bressanelli, 2019)

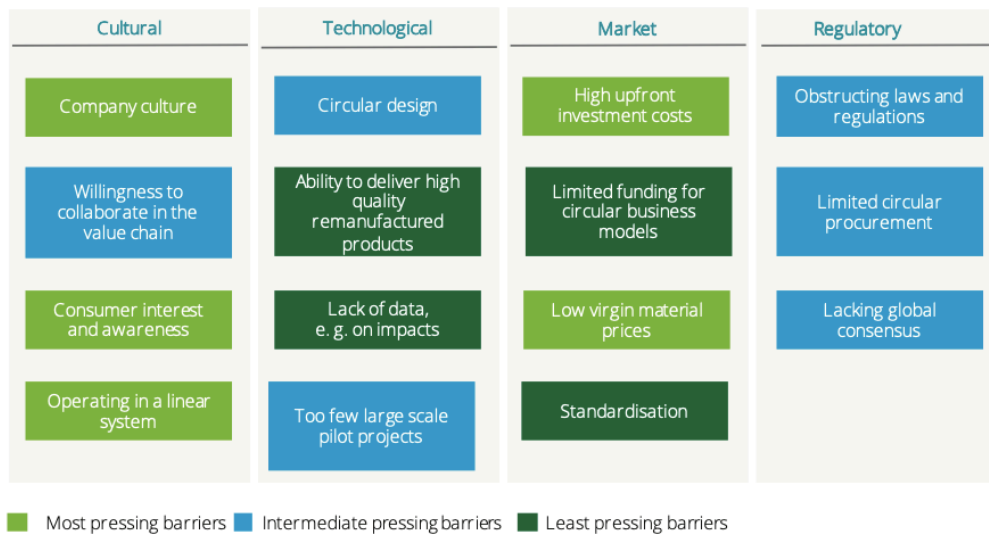


Figure- circular economy barriers. Source-(Kirchherr et al., 2017)

There are some of common barriers companies are facing while implementation of circular economy. Financial barriers; cost of implementation of c.e is high. To install the new technologies and designs required more investment, lack of government support and effective legislation; firms faces issues if government don't intervention in legislative framework, lack of information; one of the major barriers is lack of information in consumers regarding circular products and it requires great efforts to recycle and reuse the material; some of the studies showed that lack of internal technical skills is key barriers of the company; lack of support from suppliers and consumers.(Rizos et al., 2015)

In the transformation from linear to circular economy main challenge is face by companies is customer needs. In the H&M hosted launch event reflects companies should focus on customizing services and the second challenge is how to encourage customers through rewards and Rapid changes in fashion designs, usage stage is short as a result from circular design to sourcing the materials it takes time. (Praticco, 2016)

## CHAPTER 3.8: CIRCULAR ECONOMY AND CUSTOMER ORIENTATION

To understand the prospect of circular inner loops, consumers should change their perceptions and behavior towards the circular products and services. (Mugge, 2018)

According to ECAP (European clothing action plan) report (2019), as a part of the research in ECAP, a EU clothing survey was conducted to collect information around clothing related behavior across four nations- Denmark, Germany, Netherland and Italy. Some of the major results found that Dane household wear their clothing longest (5 years) as compared to Netherland (4.1 years) and Germany and Italy (3.8years). The way of disposing the old clothes is different between nations, to exemplify charity shops, charity bags or bring bangs. ECAP wants to increase awareness and encourage behavior change by the help of their partners, WRAP (waste and recourse action programme) and LWARB (London waste and recycling board). One of the main barriers for small and medium companies to commence circular projects is the lack of market support or demand from customers. Circular economy is an economic system that replaces the end of life concept of products with reducing, reusing, recycling and recovering material in production/distribution and consumption process. it works at micro level such as products, companies, consumers and meso level like eco industrial parks and it operates to the macro level like cities, region, nations, and beyond with the main goal to accomplish sustainable development. It is enabling by responsible consumers. (Otero,et al., 2019). The attitude behavior gap has not been completely understood. Consumer buying decisions are not rational and not always well connected with their values. (Vehmas et al., 2018)

According to survey from 28 EU member states, Norway, Iceland, Switzerland, Japan, Canada, and the USA, they collected insights from 50 interview with stakeholder from NGO's, business and consumer associations, public authorities and academia and consumer

focus groups. The conducted survey gave information on consumer's experiences with circular economy practices such as repairing, renting, leasing and purchasing secondhand products. It involves socio-demographic characteristics and self-declared attitudes towards CE. The results of the survey found that consumers were generally willing to engage in CE practices, but actual engagement was low. The lack of information could be a reason and lack of sufficiently develop markets. (Harms et al., 2018) According to a circular economy survey by ING 2019 revealed that 61% of respondents believe that their individual actions can have some positive impact in addressing global environment challenges.

Price is main influential determinant while making taking purchase decisions over sustainability factors. There are mainly three reasons for that: 1. Clothing sustainability is very complex, diverse customers, clothing is not an altruistic purchase, sustainability is low concerns when it comes to consumers purchase criteria. However, consumers are focusing on ethical issue, most of the customers interested in their own fashion needs. Some of the consumers believe they are not aware about the production conditions, how they are producing in developing countries. (Vehmas et al., 2018)

Circular economy has a great impact on quality of life. Quality of life of humans is defined by these 3 spheres of human activity; the psychological and moral, the social-cultural and the technical and economic. Customer choices are shaped by the information of existing products. The reduction of plastic consumption and more sustainable production influence the socio-cultural aspects of life. Companies are facing the changing behavior of consumers that is triggered by EU politics and enhancing sustainable people approach. (Nowicki et.al, 2019). To collect more wastage, waste collection awareness campaigns can help to create awareness among the consumers. Some of the brands are motivating to their customers to bring back old clothes and offers some discounts coupons for next purchasing. Some creative workshops

also motivate people to make something new from old clothes such as toilet bag, pencil cases and grocery bags etc. (Manshoven et al., 2019)

In European countries survey was conducted regarding insights of consumers engagement in the C.E. the study showed results that customers were willing to indulge in circular economies activities, but actual involvement was low. Only 64% customers prefer repair products. But 90% have no experience any renting or second hand purchasing. The main reason for this is because of lack of information about product reparability and lack of sufficiently developed markets (Consumer behaviour and the circular economy – putting people first – by Experientia, 2020). Demographic, economic, psychosocial, cultural and socio material conditions are main factors which influence the behavior of customers towards circular economy. (Camacho-Otero, Tunn and Chamberlin, 2019)

## Chapter 4: The Case Study of H&M and ZARA

H&M and ZARA are leading fast- fashion global retailers, they are running their business internationally and sustain the growth. In order to find the research, question these two largest companies has been used as a case study. These companies have strong ownership advantages for example, international experience and brand identity due to these advantages eliminate the risk of uncertainty about foreign market. Psychic distance is main component of location -specific advantages. Psychic distance means cultural and business differences to each nation's different features such as language, legal and political system and education level. When the psychic distance is low companies find less uncertainty for new markets. (Lee, 2019)

H&M was established by Erling Persson in 1947. The first store was opened in Sweden called "Hennes". Initially it was just selling women cloths. But It got huge response in its first

few years after next some decades the company expanded internationally, first opened in Norway in 1964. And later grew in other companies as well. H&M gained multinational experience due to its knowledge regarding foreign markets. In case of location advantages has less influenced the internationalization because psychic distance was not critical factor for H&M. For internationalization, location advantages were not affected H&M decisions. (Lee, 2019).

ZARA was established in 1975, Zara has become second largest clothing retailer with 2992 stores across 62 countries worldwide. Inditex also owns 7 other clothing brands such as Kiddy's class, Pull and Bear, Massimo Dutti, Bershka, Stradivarius, Oysho and Zara home. (Lopez and Fan, 2009).

One of the largest Spanish fast fashion retailer is part of fully vertically integrated. Zara has centralized the design and manufacturing and uses their own resources to execute latest innovative ideas. Mainly maximum factories of Zara in Europe despite In Asia cost of labour is much lower as compared to Europe. Zara prefer to keep production and operations in Europe and that is how Zara able to maintain quick turnover. Zara produces new designs and 11000 new items in a year. Zara's production period is just 15 days. That means Zara produces something new within every 2 weeks. This is how Zara create competitive advantage against its competitors H&M and GAP. In store of Zara employees ask to customers what design they want next, about design, fabrics. They use point-of-sales then they immediately send back these reports to headquarters in Spain. Zara's marketing strategies are completely different from H&M. They spend very less on advertising just 0.3% of sales (Bhardwaj, Eickman and Runyan, 2011).

H&M most of its production outsources from more than 700 textile suppliers. The main reasons behind the success of H&M is the location of its stores, flexibility of its production

and low prices. 90% of the turnover of H&M coming from international countries. H&M 's main expansion strategy is owning subsidiaries. However, Zara manufactures its clothes internally that is make it different from its competitors because its turnaround time. (Lopez and Fan, 2009) ZARA believes the focus on psychic distance is irrelevant for internationalization. (Bhardwaj, Eickman and Runyan, 2011).

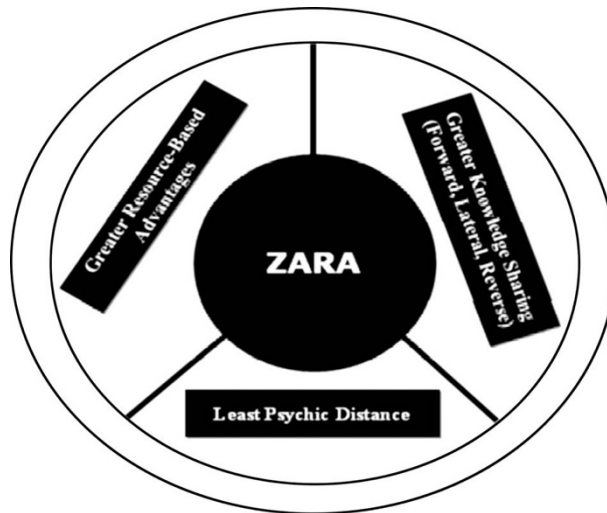


Figure Internationalization strategy components of ZARA Source-(Bhardwaj, Eickman and Runyan, 2011).

In 2016 H&M launched new collection and recycling technologies have implemented. With the help of this, it receives 25 to 30 truckloads a day in Germany. In 2016, H&M collected approximately 16000 tons of garments. (Koszewska, 2018). There are some sustainable operations practices adopted by H&M; 1. Eco material preparation- according to the reports H&M has the largest users of organic cotton for many years. H&M has indulged into the global project named better cotton initiative and it provides better farming techniques, 2. Sustainable manufacturing H&M also focuses on fair working conditions and environmental performance, it provides information about their suppliers. Bangladesh is a key manufacturing country for H&M. It provides training to suppliers and their workers; 3. Green distribution- H&M gives training course to truck drivers to reduce emissions and H&M set up an intelligent transportation system for direct shipments. 4. green retailing – H&M offers



15% discount coupon for their next buying if they bring back their old clothes put in the collection box for recycling (Shen, 2014)

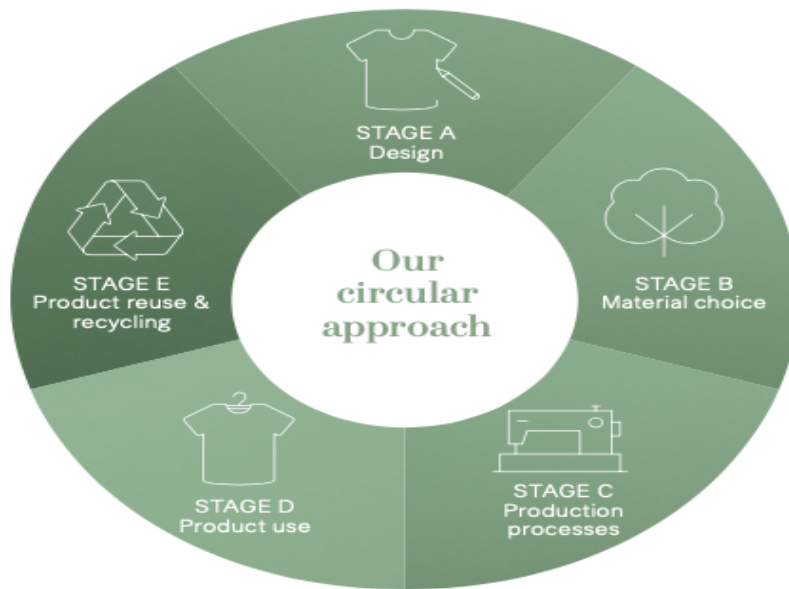


Figure- H&M's circular approach, Source- H&M sustainability report, 2018

## Chapter 5: Major Results

### *What underpin, to adopt circular economy concept in MNCs production and operation?*

Companies are adopting Circular economy, To reduce the wastage, gasses emission in the production process, to save natural resources, H&M is using closing loop so that they can recycling the clothes again and again instead of dump into landfills.

The mainly circular economy also helps to create competitive advantages in the foreign market and helps to survival in the long run. sustainability practices make H&M different from its competitors.

According to the sustainability report of H&M, 2018, they used 57% of recycled materials. H&M used 95% recycled cotton. “Collaboration and innovation are key to creating a fashion industry where clothes are used more and never become waste. As a core partner of Make Fashion Circular, and a brand with a significant global presence, the H&M group is playing an essential role in driving momentum towards this new vision for the industry.”

(H&M group sustainably report, 2018)

*How and why the adoption of the circular economy concept is affected by the ownership, location, and internalisation issues?*

## **OLI factors of H&M and ZARA**

Ownership- companies have some firm-specific advantages there are advantages of Zara and H&M.

Competitive advantages of Zara	Competitive advantages of H&M
Research and development  Speed of production  Latest designs  Customize designs	Technology  Skills and knowledge  Relationships with suppliers  Sustainable production

## How ownership advantages of H&M impact on C.E

Oa-Circular designs, product innovations, new technologies to sorting the old clothes, sustainable production management. Mostly It has circular asset-based advantages and these advantages internationalized to other foreign markets. H&M 's main vision is to 100% circular and renewable, 100% leading the change and 100% fair and equal. These ownership advantages of H&M may help to achieve their goals.

Ot- Advantages of scale and scope by production decentralization in foreign countries especially in Asia. H&M has around 800 independent suppliers mainly in Europe and Asia.

Oi- code of conduct, maintain a corporate culture, incentives provide training to suppliers so that they can maintain the corporate culture in foreign factories and subsidiaries. According to the 2017 sustainability report of H&M stated that 458 suppliers' factories were trained in workplace dialogue programme. They ensure that suppliers provide good quality products and delivered on time.

Location advantages- It involves targeted companies political and economic and institutional advantages. H&M mostly outsource the production from Asian countries because of the locational advantages. Their labour cost is quite low as compared to Europe.

Internationalization advantages- H&M's extensive experience and know-how and sharing the tacit knowledge to a local firm. H&M transfer its ownership advantages to its subsidiaries and as to production houses, H&M shares the know-how and experience and circular economy methods to suppliers. It provides training to the production and distribution workers to grow circular economy. Fast fashion companies' implementation of the circular economy is mostly infected by ownership and internationalization advantages.

***How one company has been able to adopt a circular economy despite outsourcing as compared to a company with mostly internalized sourcing?***

In order to answer the question, after analysis of the literature review, H&M is more successful for adopting a circular economy. Zara is creating competitive through its production speed up within just 15 days. But in the case of circular economy recycling products takes time to produce new products. On another hand, Zara is famous for turnaround production, it produces 3 times more than its competitors. Moreover, to implement circular economy requires new designs methods and production process. Zara is known for its quality but according to the literature recyclable products have less quality. Zara makes a variety of cloths they change their designs according to the months. Hence it is a challenge for the designers of the Zara to make recyclable clothes in such a short period. That's how H&M has been able to adopt a circular economy despite outsourcing and Zara faces some obstacles to implement circular economy mostly with internalized sourcing.

***How it is influenced by customer orientations?***

The circular economy is greatly influenced by customer behaviour. To Gain more popularity companies must change the consumer perceptions through creating awareness regarding how to dispose of textile wastage and by offering a discount coupon on next purchasing if they would put clothes in the collection box. In 2018 H&M collected 20,649 tones of textiles for reuse and recycling. H&M encourage their customers by providing information on how to care for garments and how to reuse and dispose of it. H&M launched a "take care" concept to inspire customers. After use, they bring them back for reuse and recycling. This concept helps to customers how to take care of their clothes.

The circular economy still faces a lack of awareness among customers regarding renting, leasing and repairability but there is also a lack of proper secondhand market. According to

the study reports customers mainly attracted by the price of the products and durability. Most companies face challenges such as lack of information and lack of technological advancement. Similarly, they need a huge investment to install technologies and provide training to the designers. In 2017 H&M tried a new transparency activity for customers here, they could see where garments were made, what materials were used and who made them. That was a good initiative to create awareness in customers regarding the materials. companies should conduct some awareness workshops, then customers can get attract towards circular economy. H&M provide customer rewards for sustainable actions, that's how they encourage the customers to reuse, re-wear and recycle.

***What are the challenges faced by companies to implement the circular economy?***

1. Lack of awareness- customers are unaware of how to dispose of old clothes.
2. Lack of technological advancement- companies don't have advance technologies and for launching recycling machinery they need huge investment.
3. Rapid changes in the fashion industry- fashion is changing day by day. Recyclable material is a time-consuming process. Then they have to focus on a new circular design.
4. Production of good quality clothes and durable.

## Chapter 6: Conclusion

*This chapter provides the overall conclusion of this research study as well as the limitations of the study.*

Sustainability and environmental value creation are continually gaining more momentum in the textile industry. Every company wants to expand its business internationally. To grow the companies needs competitive advantages, companies can grow through by creating competitive advantage of the circular economy. Not only for growth but nowadays in business practices such as production and operations need green practices. Because the current linear economy harms the environment with chemicals and excessive usage of resources. This study

was carried out on the circular economy perspective which is helping the environment by less wastage of materials, creating a closing loop, recycling and reuse of products.

The study conducts into 5 main parts on fast fashion companies. The research was carried out on the existing data from the H&M and Zara as case companies. This study tried to contribute how OLI paradigms have an impact on circular economy to answer this research questions literature review was conducted and after analysis of review, the second part is regarding How one company has been able to adopt a circular economy despite outsourcing as compared to a company with mostly internalized sourcing. To explore this research question comparison of both companies' sourcing of material has been done. Another part explored the relationship between customer behaviour and the circular economy. Last part related to how the implementation of the circular economy has been challenging for companies. There are several issues faced by the companies mentioned. In summarizing this study has provided some new insights about circular economy and Internationalization theory.

### **Limitations of the study**

This research study tried to explore every aspect related to the study. Despite that, there are still some limitations of the research which might be considered in future studies. This study project is based on secondary data and used qualitative data. The geographical background the case companies are also from a similar institutional background (H&M- Sweden), (ZARA- Spain).

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