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OF THE LOCAL
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SYSTEMS IN
BULGARIA, POLAND
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**THEORETICAL
AND ECONOMIC
POLICY ISSUES**



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Vladia Borissova*

**INTELLECTUAL PROPERTY ROLE
FOR THE LOCAL PRODUCTION SYSTEMS
EFFICIENT FUNCTIONING IN TIMES OF CRISIS¹**

1. Introduction

The topic is determined by the global reorientation of the economy into a knowledge economy, based on the Europe 2020 – Europe's Growth Strategy. In this document, traditional resources such as labor and capital are supplemented with the resource of knowledge as a key factor to the economic prosperity on both micro and macro level. Intellectual property is increasingly becoming a crucial factor for the development of new production and expansion of market positions. The knowledge economy is based on such resources like knowledge, creativity

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and talent of the human capital and its creative results in both the material and non-material production and its functioning creates positive economic effects and sustainable economic growth. In this regard, managing the economic crisis on both macro and micro level depends on the selected direction of economic development. Reorientation of the national economy to new economic resources that can help to reduce the “speed” of entering into crisis and eventually help it exit it, requires the implementation of new models of business behavior for economic operators, especially for small and medium enterprises (SMEs), the big business companies and other participants in their functional units such as clusters and local production systems (LPS).

The new business models, which require the use of knowledge and creativity as a production resource, implement intellectual property as a key economic factor for business development. Business enterprises reorient their activities to creation of innovation or to external purchases of such, as a mean to handle the economic crisis. The business survival process in a state of global, national and regional economic crisis, requires from companies to be flexible in managing the decision making process for creating intellectual property or external acquiring it in taking into account the changes of the conditions and the environment of their market activity.

In this changing economic environment the role of the new economic recourses such as creativity and knowledge becomes very essential. Those resources allow flexibility and dynamic of the business activities. Which is a crisis are very valuable and competitive advantages.

Creativity as a process is determined by the knowledge and talent of the human capital. Talent is an inherent or not human quality, which can be enhanced and extended to grade functionality by the acquisition of knowledge. This is important because the acquisition of knowledge helps the optimization of business by giving professional qualification to the human capital and thus helping it to meet the business needs. And though talent is a quality that is not a subject to cultivation, it is a process that forms a way of thinking and stimulates creativity of the individuals. In other words, the principle that relates to knowledge is “accumulation” or – the more knowledge, the more creativity, more innovation, more

intellectual property, more competitive advantage, and more economic growth. It is important to note that most of knowledge required for business purposes is formed in higher education institutions. This regularity is essential, because at this stage the government policy is structurally important for the future development of the business (which industries are national priorities for strategic promotions and what is the government higher education policy for the point of view of the preparation of professionals for them).

Educational and research activities are related to intellectual property by training highly qualified personnel and development of innovations. They are related to the formation of the so-called “intellectual capital”, which is a major economic resource.

Creativity as a process is related to the formation of new ideas and their practical application to the production of original and functional scientific and technological innovations. Once the creative results are objectively presented, they become potential objects of intellectual property. Every technological innovation initially arises as a description of the idea of its creation. This description takes usually a form of scientific elaboration, sketch, schedule, etc. which has no three-dimensional innovation objective form as a product yet. Creative results i.e. innovations are always intellectual property but differ in their form. Thus, a innovation for product can be IP protected as an invention, another innovation for process, which doesn't present new capacity of productivity, but optimizes the old one, would be IP protected not as an invention, but as “know-how”. The object of intellectual property is determined by the type of innovation and its industrial or commercial use (for example, a trade innovation can be protected as a trademark, an object of intellectual property).

In this regard, intellectual property specifies the economic aspects of creativity as a resource. Thus, it may be industrialized and turned into a product that satisfies social needs. By the industrialization of creativity, the economic characteristics of intellectual property contribute to the development of entrepreneurship, by promoting innovation and increasing productivity, which leads to economic growth.

2. Intellectual property as a factor for economic growth and as an economic resource

The economic characteristics of intellectual property make it an important factor for economic growth. The link between creativity as a process, its results and the market realization of their economic potential is realized exactly through intellectual property. Intellectual property is the basic for the functioning of any business. If business is commercial-oriented, such as a distribution company, the intellectual property is in the way it's managed, in the trademark, in the product design, even in the list of customers or price offers. Regardless business is production-oriented, such as the production of cars with the usage of own technology, design or with the usage of licensed technology, but under its own trademark –all of them refer to intellectual property issues. Creative industries are perceived as a term that is identifying the industries whose businesses are primarily oriented towards the creation and management of intellectual property. Creative industries are built on the basis of a complex work network of creative enterprises, organized in a meaningful direction for economic sectors. Creative enterprises are those involved with the creation and commercial exploitation of creative products (innovations), labeled as intellectual property, they generate wealth, increase employment and expand trade in the material and non-material production sectors.

Creative industries are defined as a broad alliance of creative, innovative activities that become a center of economic policy and planning and are seriously state budget encouraged by the government in many countries. A global trend in national policy is to determine the creative industries and their network structures such as clusters and LPS, because they generate economic value that can be measured with purely economic indicators like domestic product, added value, employment, imports and exports of production. This is an important indicator how knowledge-based industries contribute to the pace of economic growth.

In this context, the international trade with products based on intellectual property for the period 2005–2010 increased with 9.7%. The value

of the international exports is about \$ 624.4 billion in 2010, representing 4.9% of total global trade.²

Except being an important economic resource, intellectual property is also a way of protecting business innovation, and hence it's a tool for optimum realization of their economic potential. Intellectual property, depending on the area of the economy it is created, can be represented by industrial property objects – these are innovations in the sector of material production. This sector is mainly occupied by conglomerates whose business is focused on high-tech manufacturing and SMEs whose business is predominantly scientific research. Clustered network structures of enterprises in the material production sectors are distinctive mainly for the chemical industry, machine building industry, food industry and others.

Local production systems based on the use of intellectual property in the field of material production are mainly companies with their own research and development activity or those who act as representatives of large international corporations who transfer their technology to them and give them business set guidelines for functioning and market positioning. An evidence of the importance of intellectual property as an economic resource and as factor for economic growth in a time of crisis is the tendency inherent for the domestic market where the business leaders are namely enterprises based on intellectual property management. Because of their flexibility they become the attraction center for the formation and functioning of cluster structures and LPS.

Beside foreign representatives, there also companies in local innovation and development businesses, who have developed a LPS using external funding sources through grants from the European Union fund programs. In the latter case, the company forms an economic advantage by working on preliminarily specified technologies and predefines process, which again is intellectual property (such as for example milk and dairy activities based on Dutch technology). These companies operate on the principle of acquiring technology from outside the company by obtaining license.

² Updated research paper, not published yet of the: V. Borissova, coll., *The contribution of the creative industries into the economic growth of the Bulgaria*, research paper, UNWE, 2007.

In the area outside the material production (the cultural sector and R&D sector) the role of intellectual property in economic growth in times of crisis is even more palpable. Traditionally, this sectors was seen as predominantly subsidiary sector, relying heavily on the state budget and a passive participant in the creation of value in the national economy. In the transition to a knowledge economy, more and more businesses began to actively participate in the creation of value to the end product created in the cultural sector and R&D sector. Even in 2007 the contribution of businesses operating in the sector outside material production towards the added value in Bulgaria is 2.41% of the total³. The figures are proof that the area outside material production can not only pay for itself but can also actively participate and contribute to the economic growth of the country.

This means that the entrepreneurs which identified intellectual property and succeeded to properly manage it to their own interest, realize economic advantage over those who rely on traditional business methods and economic resources. This sector is characterized mostly by clustered network structure of the business; and in terms of the film industry in Bulgaria there is a quite distinct major local production system, which acquires even regional character. Large clusters in the non-material production are formed by the publishing, musical, radio TV industries, including the software industry.

Intellectual property covers two major groups of objects according to the sector in which creativity is manifested. The group in the sector of material production is industrial property (inventions, utility models, industrial designs, trademarks, geographical indications, know-how, new plant varieties and animal breeds). The group outside the sector of material production is a subject to copyright and related rights (such as scientific and literary works, photographs, music, architectural objects, films, artworks, domain names, audiovisual works, radio and television programs, videos, sound recordings and performances, and etc.).

The objects of intellectual property as an economic resource are present in the company balance sheet in “intangible assets” section. The intangible nature of the objects of intellectual property is due to the innovative

³ See V. Borissova, coll., *The contribution of the creative industries into the economic growth of the Bulgaria*, research paper UNWE and Ministry of culture, UNWE, 2007.

characteristics of information they contain. This fact determines the objects of intellectual property as part of the merchant's property (the business unit) and positions them in balance sheet as intangible assets. The life cycle of the asset depends on the time required for its wear. In the majority of intellectual property objects, it occurs with the obsolescence of the information they contain, rather than their physical wearing out.

The composition of business enterprises beside rights and duties includes the so-called factual relationships, that are not a legal entity. They are economic relations between the trader and his clientele. When intellectual property (for example one trademark or design) is internally created, developed and enforced by the company, it is a part of her factual relationship until the moment it is evaluated. The direct link between the holder of intellectual property and the customers is realized through objects of intellectual property and due to the trade monopoly. Intellectual property can be created inside the company as a result of scientific and technical development activities conducted by its structural units (such as invention).

Another possibility for the enterprise is to acquire intellectual property outside of the legal ground, for example by merger, acquisition or purchase of companies, where the intellectual property travels with the asset at cost. This is because the value of the asset can be determined by the cost of the acquisition. Although there is an expense on the purchasing of the object of intellectual property, there are no liabilities because the acquired object goes with a trade monopoly by which the asset's value will rise in the future.

Main characteristics of intangible assets are:

- uniqueness in terms of invested intellectual labor and creativity for their creation,
- susceptibility to moral obsolescence, which is then not physical and is not as a result of its use,
- reproducibility – the economic potential of intellectual property allows multiple use of the asset simultaneously by a number of persons in different territories,
- over-profitability, generating excessive profits.⁴

⁴ See B. Borisov, *Licensing trade*, UNWE 2003.

Essential characteristic of intellectual property is also that the objects can be reused by several different companies at the same time, on the same or different territories. The use is always against a consideration in accordance with the commercial terms of business. For the majority of businesses, intellectual property is an essential part of their marketing (trademarks, industrial design, etc.). With proper identification and management of intellectual property in the enterprise, it could become a mean to overcome the negative effects over the business in the global economic crisis on local and national level.

3. Economic benefits from the use of intellectual property for business

The economic benefits from the use of intellectual property as a resource lie in the possibilities that the intangible nature of its objects grants to businesses. The economic advantages for the enterprises are licensed trade and trade monopoly.

The licensed trade is possible only for intangible objects, such as the objects of intellectual property. Licensing trade is the most cost-effective form of exploitation of the intellectual property objects as intangible assets. When licensing intellectual property, it is not alienated, but permission is given for its use for a specified time, in a given area against a consideration. Licensing enables multiple realization of the consumer value of the object at the same time both by the holder of the right and its users – the licensees. An object can be used by several persons simultaneously, with or without the involvement of the licensor. It depends on the type of the license.

The granting of a license is a strategic approach for the trade monopoly holder to optimally use the economic potential of the object. Licensing is a way to expand the market and maximize the excess profit realization for the term of protection of the intellectual property object.

After obtaining IP protection for the owner of the IP right over the IP objects the trade monopoly is granted. This exception to the practice of free market relations, where monopoly is unacceptable, is due to the fact that the innovation protected with intellectual property is a result of the intellectual efforts of a person or a group of persons and that the result of its economic ex-

exploitation will generate goods that will satisfy public needs. Trade monopoly is the “public reverence” to innovators because through it they satisfy public needs. However, to maintain the public interest and simultaneously tolerate creativity, trade monopoly is limited in time and space of action. But regardless of this, the presence of trade monopoly gives businesses a competitive edge and undeniably important prerequisite for economic growth.

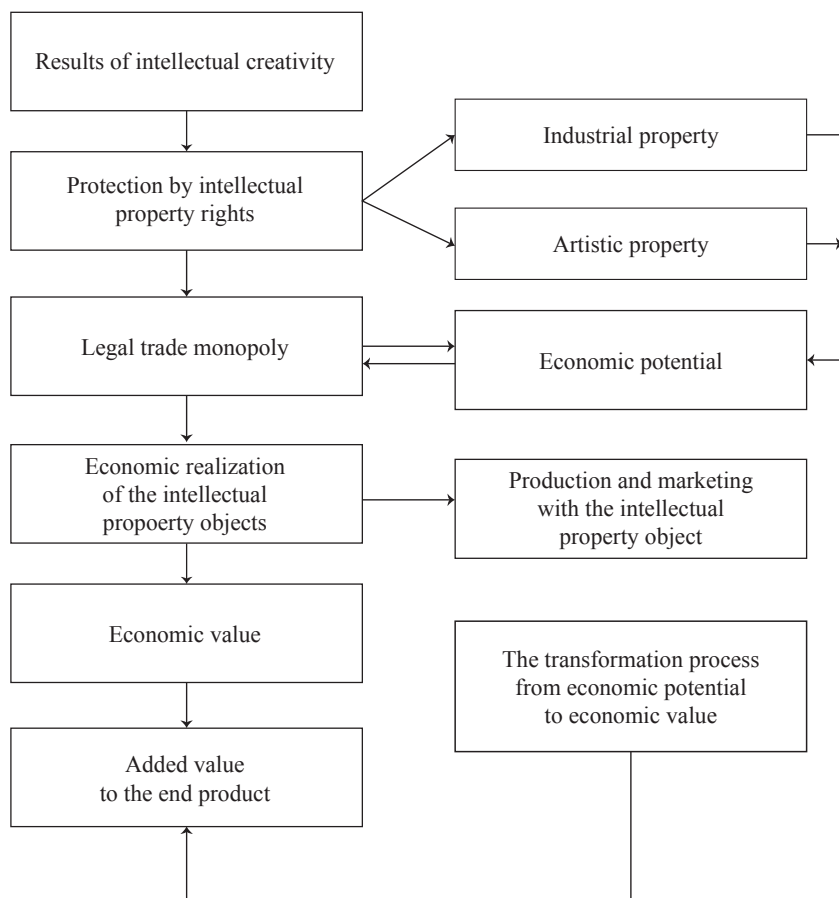


Figure 1. Economic aspects of IP

Source: own composition

Intellectual property objects have intellectual potential that is granted into the hands of one person in the form of trade monopoly, after obtaining legal protection, i.e. patenting, registration or automatically from the moment of their creation, regarding to artistic works. From this perspective, the legal protection provides its holder with a trade monopoly for the production and marketing through the use of the protected object within the territory of a given market.

In this regard, the economic benefits of owning a trade monopoly for business can be derived in the following areas:⁵

- realizing excessive profits. The trade monopoly holder benefits from the economic advantage to realize significant reductions in the manufacturing process of the production implementation of the object, for instance by reducing production costs and time compared to those of his competitors. Consequently, the trade monopoly holder except the average profit margin also realizes additional profits;

- maximizing the mass of profit. The mass of profit is maximized by the fact that on the market many people are looking for one product, but only one company offers it. This means that the “demand” belongs to the holder of the trade monopoly, which allows him to manage two significant market factors: volume and price of the offered goods. The optimal combination of production volume with price is a prerequisite for the realization of the maximum amount of profit gained;

- protection of investments. Obtaining trade monopoly means protecting the investments made for the creation of intellectual result (the innovation) Trade monopoly provides the time and calmness needed to launch production, including the incorporation of new production facilities. Conditions for the development of research in the production process of the object are created in order to improve certain characteristics and parameters, or develop another innovation;

- conquest of markets. Trade monopoly is a mean of conquering competitive markets. Offering new products manufactured at low production costs and time, from one source at a price consistent with the public eligible expenditures, will inevitably lead to the establishment of a stable market positions.

⁵ See: B. Borisov, *The intellectual property of the industrial firm*, UNWE, 2006.

The economic potential and the intangible nature of intellectual property objects makes it possible to use them as retrieving, subject matter of pledge, means for securitization of the company's assets and an opportunity for public-private partnership.

4. Business models to cope with the economic crisis for enterprises using intellectual property as a resource

Besides shifting towards expanding product range or product mix, the other opportunities in a crisis are: buying ready innovation (acquisition of license), retrieving, pledging or securitization of the company's intellectual property.⁶

4.1. Retrieving of intellectual property

When business suffers from unfavorable economic environment and cannot reorient production process to new resources, products and markets, then its intellectual property can provide such an opportunity. Prerequisite for the implementation of this business model of behavior is the intellectual property to belong to the enterprise, to have provided protection and to have a positive reputation. For example, the enterprise has its own innovation that cannot integrate into the production process, as it requires replacement of the entire production capacity. A condition for the company to retrieve the innovation is to own it, have a patent for it and not be rejected as unfit to market. Another example is a company with a well reputed brand that is registered and has developed brand value. It is possible that the enterprise have its own new and original design, for which it has already obtained a commercial monopoly through its registration.

⁶ For example, the enterprise that developed and established the world-famous brand "Victorinox", for the production of Swiss knives had to survive in the economic crisis and the extremely unfavorable market environment. The company expanded its product range based on developed complementary product and process innovations, leading not only to survival but even to sustainable business development.

In such cases, companies who own intellectual property that cannot become part of their main business activities because of technical, economic or business reasons, can retrieve that intellectual property, which will expand the scope of their business. And as experience has shown, in a crisis the surviving business is the one who is broad and flexible enough to be changed or extended. The retrieving of intellectual property provides the business with the opportunity to expand.

For the implementation of this business model, the prerequisite is a legislative base that the intellectual property objects can be a subject of a kind (non-monetary) contribution in the composition of the assets of the enterprise that is being set up or already is established as such. Subject of the retrieving may be objects of industrial property like inventions, utility models, industrial designs and trademarks. For non-monetary contribution objects of artistic property can be provided, which are works of science, literature and art.

The retrieving itself as a contribution can be made in two different ways. First, it may be executed directly as an asset, partition or money given by the importer of the contribution. The importer must be a bank or other financial institution. They have the right to retain the object for a period of time during which the money provided against intellectual property must be returned. The special feature for this type of kind contribution is that the non-monetary contribution is not an object, but the right to use the retrieved intellectual property. This is a form of a license where the holder of the right (the enterprise that retrieves) becomes a partner in another company with another business and another market position while maintaining its business and even creates prerequisites for survival in a crisis.

The retrieving as a business model is a prerequisite for regional development and may even stimulate the formation and support the functioning of LPS. Such opportunity exists for the municipalities that have identified their intellectual property and have taken the necessary actions for its protection. The suitable intellectual property management from the municipality can lead to positive economic effects by stimulating environment for the development of public-private partnership. The intellectual property of a municipality are: the name of the city, names of localities and neigh-

borhoods, crest or emblem of the city, monuments, landmarks, mineral waters, places and crafts with traditional elements, cultural events, websites, domain names, inventions, technical and software solutions, design and more, which are created in local companies or from municipal funding. In this context, retrieving the intellectual property of the municipality in the property of an enterprise in its territory would lead to the following positive results:

- improvement of the financial situation of the municipality by receiving the distributed dividends on its equity investment in companies located in its territory;
- if the municipality traditionally has a good reputation for certain goods or services, improvement of the competitiveness on its territory as a result of the use of intellectual property of the municipality as a guarantee of origin and quality. For example flat sausage Karlovska or Asenovgradski wine mavrud or Karnobatska grabe rakia or mineral water Gorna Banya.

4.2. Intellectual property pledge

Another business model of behavior of enterprises in the context of economic crisis is intellectual property pledge. This business model is corresponding with the dynamic market environment, where rapid decision-making and strategic business management changes are an essential condition for its survival. The pledge does not guarantee 100% security, but extends the possibilities for collateral, which expands the opportunities for lending of the enterprise, which accelerates the turnover. The more guarantees can be given, the more credits you can be obtained.

A subject to the pledge can not only be an object, but also rights. The contract is consensual, i. e. there is no real transfer of intellectual property. The advantages of this business method are that now the pledgor can use the stake intellectual property in their business. Failure to submit the subject matter of the pledge is to the advantage of the pledgee as well. If so, he is released from the obligation to care for the preservation of the bet.⁷

⁷ According to the Bulgarian legislation.

Due to the fact that company retains intellectual property that is pledged and against which it received funding and can continue to use it (e.g. innovation or trademark), it can increase the size of the object of the pledge by invoking another significant benefit of the pledge. If the enterprise needs additional funding or fails pledge certain intellectual property, it may pledge its future production, but only for the current or the next year after the pledge. The restriction is in the interest of the pledgor, as his obligation to return the pledge does not extend to all of his products. The pledgee may be any individual or legal person, i.e. another enterprise to which there is a due consideration, bank, investment fund or individual.

4.3. Securitization of intellectual property

The intellectual property securitization is possible in legislative conditions and in developed financial markets. Securitization is done through an investment stock company, like Real Estate Investment Trust – REITs, which converts illiquid receivables into securities (stocks or bonds), by which they buy them from their holders. This process is called securitization. Securitization of intellectual property can be applied by an enterprise that has licensed its intellectual property to another company, i.e. they are in a licensor and licensee relationship and the latter due to royalty. In this situation, if the licensor needs fast financing with money in cash, he doesn't have to wait for their monthly license fee. The licensor can provide the entire amount of receivable due for the period of the license of the REITs against which to issue shares or bonds. So REITs buys the receivables (the license price) of the holder against the price of the securities, which subsequently offers for purchase to the investors in the capital market. Securitization of intellectual property is also possible in the absence of licensing relations, but with the opportunity to define the future revenues from the use of trade monopoly on the object for a certain period of time. Based on such a market research, quantified future revenues become a subject to securitization for which the entity receives liquid assets. For example, the securitization of the revenue from trademark use which the enterprise will implemented in five years. The trademark is assessed

as intellectual property and on the basis of the trade monopoly and its positive reputation, its future profitability is determined, which has become the subject of securitization, i.e. the enterprise does not have to wait for five years to receive money in cash from its own trademark, it gets them right away from the REITs.

5. Conclusion

Intellectual property is increasingly becoming more important to the economic growth of the business and the economy as a whole. Its identification as an economic resource, its protection and management as an intangible asset of the company, are definite preconditions for business competitiveness and prosperity. In times of economic crisis or highly competitive market environment, intellectual property is a factor for economic growth that provides a variety of business models, mediating the formation and operation of enterprises in network structures such as clusters and local production systems. The intangible nature of intellectual property enables these network systems to withstand the changes in the economic environment through implementation of new, flexible business models.

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Abstract

The topic is determined by the global reorientation of the economy into a knowledge economy, traditional resources such as labor and capital are supplemented with the resource of knowledge as a key factor to the economic prosperity. Intellectual property is increasingly becoming a crucial factor for the development of new production and expansion of market positions. Reorientation of the national economy to new economic resources that can help to reduce the “speed” of entering into crisis and eventually help it exit it, requires the implementation of new models of business behavior for the SMEs, the big business companies and other participants in the clusters and the local production systems (LPS).

Thus the IP specifies the economic aspects of creativity as a resource it may be industrialized and turned into a product that satisfies social and cultural needs. By the industrialization of creativity, the IP economic characteristics contribute to the development of entrepreneurship, by promoting innovation and increasing productivity, which leads to economic growth. This article observes the IP as a factor for economic growth and as an economic resource and the upcoming economic benefits from its use for the business. The appropriate business models to cope with the economic crisis for enterprises using IP as resource.

Key words: local production systems, intellectual property, knowledge economy, creativity.