Collective Knowledge Formation as a Dynamic Capability in Local Government

Paula Pusenius[1,2], Harri Laihonen[2], Lotta-Maria Sinervo[3] and Kristiina Takala[3]
[1]LAB University of Applied Sciences, Lappeenranta, Finland
[2]University of Eastern Finland, Kuopio, Finland
[3]Tampere University, Finland

paula.pusenius@lab.fi
harri.laihonen@uef.fi
lotta-maria.sinervo@tuni.fi
kristiina.takala@tuni.fi

Abstract: This article explores collective knowledge formation that supports socio-financial sustainability in local governments. The study aims to complement rationalistic and business-oriented knowledge management research by examining the social processes through which information is collected, interpreted, shared, and utilized. It addresses criticisms of knowledge management for its excessive internal focus, tackling tame organizational problems, and prioritizing data over meaning. In the context of local governance, characterized by complexity, hybridity, and a strong commitment to sustainability objectives, understanding factors that support collective knowledge formation is crucial for enhancing shared understanding of sustainability. The article applies the knowledge formation framework to analyze empirical data from three development workshops conducted in two Finnish cities. Preliminary findings suggest that leadership dialogue, which integrates political, strategic, and operational perspectives, can serve as an arena for collective knowledge formation. The findings also emphasize the importance of a shared knowledge base, recognition of core values, and a thorough understanding of organizational operations as enablers of effective knowledge formation processes. Additionally, these processes must occur at various organizational levels to effectively support the sustainability transition.

Keywords: Knowledge management, Knowledge formation, Public sector, Sustainability

1. Introduction

Local governments play a crucial role in promoting sustainability (Guarini, Mori and Zuffada, 2022). While sustainability has been increasingly explored in public management research, particularly in relation to the UN's sustainability goals and sustainability reporting, a gap remains in understanding how sustainability is institutionalized and how new goals impact managerial practices (Zeemering, 2018; Sinervo et al, 2024; Sinervo and Laihonen, 2024). This article argues that building a socially and financially sustainable local government requires reconciling diverse perspectives and goals. This process calls for dialogue and collective knowledge formation, where different viewpoints are negotiated and prioritized. The purpose of this article is to enhance the understanding of the factors that support the processes of knowledge formation involved in implementing socio-financial sustainability strategies in public management.

This article aims to complement the rationalistic and business-oriented KM research by examining the social process of knowledge formation, where information is collected, interpreted, shared, and utilized (Laihonen, Kork and Sinervo, 2023). In this way, the article aims to address the criticism faced by KM, particularly concerning its excessive internal focus (e.g., Kraaijenbrink, Spender and Groen, 2010), prioritizing data over meaning (Spender, 2014), and focusing on tame organizational problems (Dumay, 2020). Moreover, KM research in the public sector has been criticized for insufficient attention to the political-administrative nature of public organizations, the interaction in public policy implementation, and the complexities associated with defining and utilizing knowledge across administrative sectors and among public officials (Laihonen, Kork and Sinervo, 2023). There is thus a clear need to better exploit and understand KM within public administration (cf. Agrifoglio, Metallo and DiNauta, 2021).

We are particularly interested in identifying and understanding the intangible factors that enable collective knowledge formation in managing socio-financial sustainability. Specifically, we explore the antecedents, moderators, and consequences of knowledge formation. By analyzing how public managers discuss and interpret social and financial sustainability, we aim to contribute to the existing literature on knowledge management capabilities. This literature has primarily focused on an information science perspective, defining KM capability as an organization's technical proficiency in utilizing, generating, and safeguarding knowledge (e.g., Gold, Malhotra and Segars, 2001; Tseng and Lee, 2012). KM capabilities that build on intangible resources, such as individual experts' skills, internal and external networks, organizational practices, and cultural aspects, have received less attention (Laihonen and Mäntylä, 2018; Laihonen and Saranto, 2022), even though leveraging

these intangible resources may provide a more significant competitive advantage than relying on easily transferable tangible resources (cf. Hall, 1993).

The rest of the paper is organized as follows: The next section reviews the theoretical background of knowledge formation and capabilities. Section three outlines the study's empirical context and methods. Section four presents the empirical results, and finally, section five offers concluding remarks.

2. Theoretical Background

2.1 Knowledge Formation in Public Administration

Knowledge Management (KM) has diverse origins, including resource-based and knowledge-based perspectives. Despite their foundational role, these approaches have faced criticism for being overly focused internally and lacking clear definitions of resource value. This criticism also extends to KM, which has evolved from these theories. Spender (2014) highlighted that KM literature often prioritizes data over meaning. More recently, Dumay (2020) noted that KM tends to address straightforward organizational issues. Hujala and Laihonen (2021) added that the emphasis on organizational efficiency overlooks other essential aspects of performance, including quality, effectiveness, and sustainability.

Previous literature reviews on KM in the public sector have shown a strong focus on data production and analysis (Dumay et al, 2015; Massaro, Dumay and Garlatti, 2015). This body of research predominantly adopts models from the business sector, often neglecting the unique characteristics of public administration. Specifically, it has been noted that such research frequently overlooks the political-administrative nature of public organizations, the dynamics of public policy implementation, and the challenges in defining and utilizing knowledge across different administrative sectors and among public officials (Laihonen, Kork and Sinervo, 2023; Laihonen and Pusenius, 2025).

Instead of viewing KM through a rationalistic and business-focused lens, Laihonen et al. (2023) propose approaching KM in public administration as a social process in which information is gathered, interpreted, shared, and used. Their knowledge formation framework illustrates how knowledge is developed in public administration by integrating three perspectives: institutional complexity (Lounsbury et al, 2021; Thornton, Ocasio and Lounsbury, 2012), organizational responses (Greenwood et al, 2011), and individual sensemaking (Weick, 1995).

First, *the institutional complexity*, understood as the collective interpretation of public administration tasks and purposes in the face of various institutional powers (Lounsbury et al, 2021; Thornton, Ocasio and Lounsbury, 2012), has been largely overlooked in KM studies. This is despite the significant impact of regulatory, normative, and cultural factors on knowledge processes within public administration (Currie and Suhomlinova, 2006) and their influence on individual decision-makers. Second, the strategies, structures, and practices of public organizations are viewed as *organizational responses*, serving as methods to manage institutional complexity (Greenwood et al, 2011; Pache and Santos, 2013). These responses have a significant influence on how individuals perceive their environment and shape their perceptions and definitions of organizational success. Third, *individual sensemaking* of decision-makers in public administration plays a crucial role in knowledge formation. Public decision-makers hold legislative, administrative, or juridical positions and, as part of their sensemaking processes, they determine which information is relevant to their decisions (Weick, Sutcliffe and Obstfeld, 2005; Weick, 1995). By responding to institutional demands, they shape their environment and engage in collective knowledge formation, which helps envision future directions and anticipate actions, thereby reducing the complexity of their operating environment (Isabella, 1990).

The framework emphasizes the interaction of individuals' sensemaking processes in developing organizational responses and considering institutional complexity in public sector KM. This framework addresses key gaps in current public sector KM literature by highlighting the social process of knowledge formation, where individual and collective knowledge are continuously shaped through interaction. Knowledge formation is viewed as an iterative process, with policymakers playing a crucial role in interpreting societal issues and utilising information to address complex problems, thereby giving meaning to public policy. This approach helps to understand public policymaking as a social process that reflects institutional complexity and the intertwined nature of social problems and ambiguous solutions.

In the empirical part of the article, we examine how collective knowledge formation takes place in leadership dialogue (Figure 1). Leadership dialogue serves as an arena for knowledge formation on socio-financial sustainability, clarifying the shared situational picture and aligning service needs with resources. By following

the literature on dialogic management, we consider that dialogue fosters knowledge formation through critical self-reflection and collective learning, which involves listening to and understanding others' experiences (Isaacs, 1999; Spender and Strong, 2014). The dialogic perspective on public management combines approaches from strategic dialogue (Bourgoin, Marchessaux and Bencherki, 2018), dialogic accounting (Brown, 2009), and performance dialogue (Moynihan and Pandey, 2010; Laihonen and Mäntylä, 2017). It highlights the social processes where collective knowledge formation occurs and illustrates leadership dialogue as an arena where sustainability information is debated and prioritized.
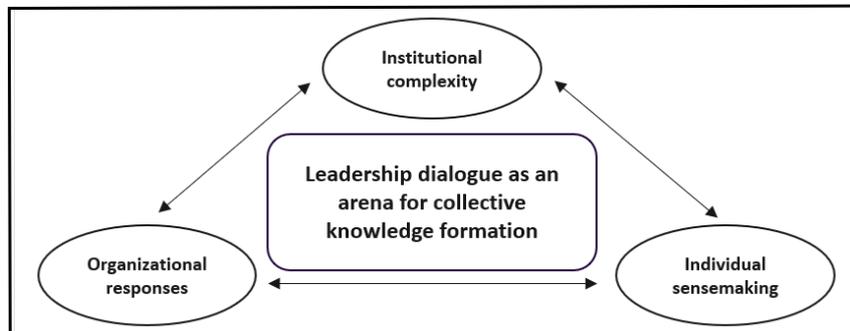
Figure 1: The empirical approach of the study: Leadership dialogue as an arena for collective knowledge formation in public administration (adapted from Laihonen, Kork and Sinervo, 2023)

2.2 Antecedents of Knowledge Formation

The knowledge formation framework lacks an empirical understanding of the antecedents of collective knowledge formation and the capabilities needed from the organization and individuals to support and participate in the process. We approach these prerequisites from a strategic management perspective, referring to capability as an organization's ability to leverage its existing resources through various path-dependent routines to achieve specific goals (e.g., Helfat and Peteraf, 2003). A resource is defined here as an asset that the organization owns or can access (Helfat and Peteraf, 2003). Conversely, a capability is the organization's ability to utilize these resources (Amit and Shoemaker, 1993). Capabilities are formed through the combination of individual and team skills, processes, organizational structures, decision-making rules, and disciplines (Teece, 2007). In addition to effective processes and routines, as well as essential resources, capabilities encompass an understanding of strategic direction. Previous literature on KM capabilities has predominantly focused on the information sciences perspective (e.g., Gold, Malhotra and Segars, 2001; Tseng and Lee, 2012) and lacks an understanding of the role of intangible resources in building organizational capability (Laihonen and Mäntylä, 2018).

Within the hierarchy of capabilities, ordinary capabilities are directed towards the organization's everyday activities, whereas dynamic capabilities modify and create ordinary capabilities, simultaneously transforming the organization (e.g., Helfat and Peteraf, 2003). Dynamic capabilities are defined as a learned and stable pattern of activity through which the organization systematically generates and modifies its routines to improve effectiveness (Zollo and Winter, 2002). The study of dynamic capabilities has evolved within the private sector; however, the definition of dynamic capabilities is also applicable to public sector organizations, as both sectors modify their routines to enhance effectiveness (Piening, 2013). It is also argued that public sector organizations are experiencing more environmental changes than private sector firms, due to frequent policy shifts and the enforcement of short-term perspectives aligned with electoral cycles (Boyne, 2002). Dynamic capabilities are thus recognized as essential for the success of public sector organizations (Piening, 2013).

In this article, we approach collective knowledge formation as a dynamic capability through Teece's (2007) framework, where microfoundations form the basis for an organization's sensing, seizing, and transforming capacities. These microfoundations can be viewed as best practices, manifested through various skills, routines, structures and processes in different settings. According to Teece (2007), sensing involves an organization's continuous scanning of its environment to identify and collect strategically important information. Seizing refers to the organization's ability to assess the value of the gathered information, convert it into actionable steps, and make informed decisions. Transforming involves the organization's ongoing renewal efforts, which include assigning tasks, allocating resources, and ensuring the workforce possesses the necessary knowledge.

3. Context and Methods of the Empirical Study

To observe how public managers discuss and interpret social and financial sustainability, and to explore the factors that support collective knowledge formation, we adopted a qualitative case study approach (Eisenhardt, 1989; Gummesson, 2000; Yin, 2009). In practice, we conducted three development workshops in two Finnish cities, involving participants from early childhood education, basic education, and various management and expert roles in finance, catering, cleaning, and property services. This research design aimed to capture how public managers developed a shared understanding of socio-financial sustainability.

The workshops in both cities lasted three to four hours. During these sessions, researchers initiated discussions with research-based perspectives and then facilitated various group activities to generate empirical data, which were later supplemented with researchers' notes and observations. Four researchers participated in each workshop, except for the first one, which had only two researchers present. This enabled researcher triangulation, enhancing the reliability and validity of the findings (Patton, 1999). The data were analyzed using data-driven thematic analysis (cf. Braun and Clarke, 2006). However, it is essential to note that, since each workshop began with an introduction by the researchers, the process was not entirely inductive. The analysis involved carefully reading the data and summarizing the initial sub-themes from individual observations. These sub-themes were then further developed into central themes, which were subsequently compared with the existing literature on the topic, ultimately leading to the identification of factors supporting collective knowledge formation.

4. Results

4.1 Main Challenges and Solutions for Collective Knowledge Formation

To identify factors that contribute to successful dialogue and knowledge formation on socio-financial sustainability, we asked workshop participants to first list the challenges in integrating the operations and finances of early childhood and basic education. They then proposed solutions to these challenges. After documenting these problem-solution pairs, participants identified the factors that support effective dialogue on socio-financial sustainability.

During the analysis, we classified the identified problem-solution pairs into three categories. The first category included issues and solutions related to general management. The second category addressed specific, everyday management challenges. The third category focused on issues related to dialogue and knowledge formation. Identifying the factors that create a successful dialogue on socio-financial sustainability proved to be surprisingly challenging. While participants were able to compile a long list of problems and some practical solutions, they struggled to articulate the more general factors that contribute to a successful dialogue. Nevertheless, dialogue acts as a mediator between general management concerns and daily challenges. Figure 2 provides a summary of the main challenges and solutions discussed in the workshops.
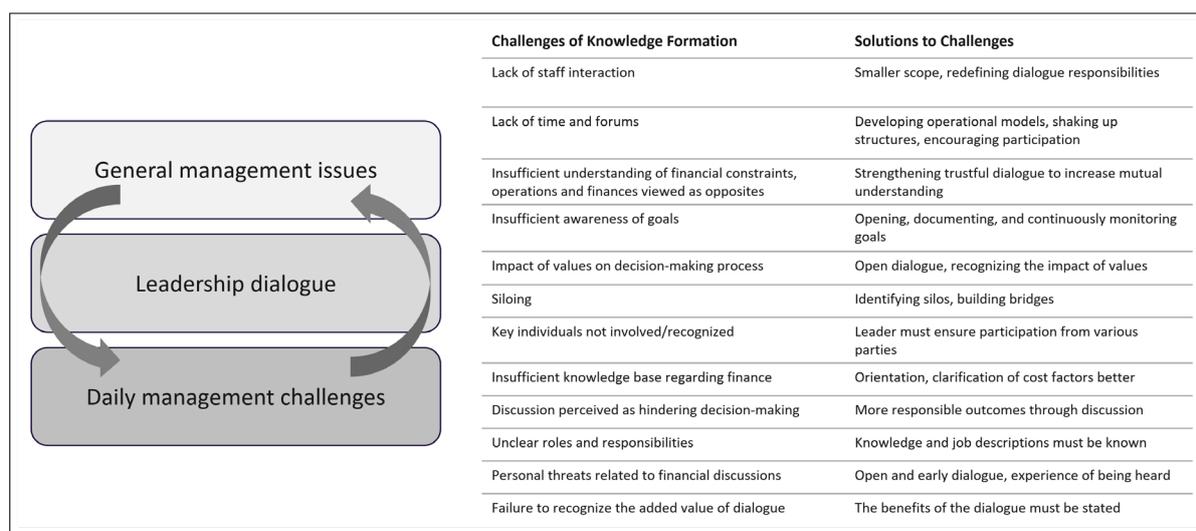

	Challenges of Knowledge Formation	Solutions to Challenges
	Lack of staff interaction	Smaller scope, redefining dialogue responsibilities
General management issues	Lack of time and forums	Developing operational models, shaking up structures, encouraging participation
	Insufficient understanding of financial constraints, operations and finances viewed as opposites	Strengthening trustful dialogue to increase mutual understanding
	Insufficient awareness of goals	Opening, documenting, and continuously monitoring goals
Leadership dialogue	Impact of values on decision-making process	Open dialogue, recognizing the impact of values
	Siloing	Identifying silos, building bridges
	Key individuals not involved/recognized	Leader must ensure participation from various parties
	Insufficient knowledge base regarding finance	Orientation, clarification of cost factors better
Daily management challenges	Discussion perceived as hindering decision-making	More responsible outcomes through discussion
	Unclear roles and responsibilities	Knowledge and job descriptions must be known
	Personal threats related to financial discussions	Open and early dialogue, experience of being heard
	Failure to recognize the added value of dialogue	The benefits of the dialogue must be stated

Figure 2: Main challenges and solutions for collective knowledge formation

4.2   Capabilities for Knowledge Formation

In the next phase, we focused on individual capabilities needed for dialogue and knowledge formation on socio-financial sustainability. Building on insights from previous workshops, three key capabilities were identified in both cities. During the workshops, participants worked in small groups to consider concrete ways to harness these capabilities in their management tasks. The overall spirit of the workshops in both cities highlighted that dialogue is fundamental to modern public management, necessitating time, courage, and systematic effort. Recognizing and committing to developing these capabilities together were considered crucial steps towards a sustainable municipal organization.

In the first city, the identified capabilities were: *Understanding one's role in a larger organizational context*, *willingness and courage to engage in dialogue*, and *creating and maintaining models that support dialogue.* Participants agreed that successful dialogue on socio-financial sustainability requires personal engagement, curiosity, and a genuine desire to understand others' perspectives. Clear roles, active communication, guidelines, and peer support were identified as key factors in promoting dialogue and engaging in collective knowledge formation. It was emphasized that open and constructive dialogue necessitates trust, respect, and a sense of social security. Presence and attentive listening were considered essential, and it was stressed that haste should not lead to superficial participation. Participants highlighted that the work community should have clear and transparent frameworks for influence, making work feel meaningful. The third capability focused on organizational structures and models that support dialogue, enabling collective knowledge formation to take place. Prioritizing the ability to facilitate discussion was identified as a prerequisite for successful dialogue, particularly in meetings involving multiple actors. Participants also stressed that dialogue should be seen more as an ongoing operational model, rather than a one-time effort.

In the second city, the identified capabilities were: *Promoting actions aligned with shared values*, *fostering a willingness to find solutions* as a guiding principle for one's activities, and *utilizing a shared knowledge base*. Participants first focused on management practices. The role of supervisors was emphasized in encouraging and guiding dialogue towards a solution, fostering a positive atmosphere, and the acceptance of mistakes. In addition, setting and communicating clear goals, as well as making achievements visible, support progress towards these goals. Collaboration, along with the equitable treatment and clear articulation of shared values, as well as making these shared values visible in practical work, were considered important. The availability and effective use of relevant, timely information, along with the promotion of shared understanding of this information, were considered critical components of decision-making and knowledge formation. Participants also regarded organizational structures and practices that support dialogue and knowledge formation on socio-financial sustainability. Key elements included creating safe spaces where psychological safety fosters genuine presence and effective dialogue. Trust, interaction, and clear rules for dialogue and participation were deemed essential for building these spaces. Additionally, recognizing and selecting appropriate participants for relevant forums was found to be crucial in ascertaining fruitful dialogue. Furthermore, clarity and systematic implementation of organizational strategies should be prioritized to ensure they are achievable in daily work.

4.3   Knowledge Formation in key Phases of Public Management

Finally, we aimed to concretize and operationalize the concept of knowledge formation in public administration by linking it to the key phases of public management—*planning, implementation, and evaluation*—and exploring how dialogue supports and enhances collective knowledge formation in these phases. The workshop discussions revealed that dialogue practices are path-dependent and closely tied to organizational culture.

The importance of dialogue and knowledge formation was highlighted, particularly in synthesizing diverse information, in creating a shared understanding of the situation, and in defining future actions. A comprehensive information base, integrating multiple types of information, such as financial and personnel data, legislation, regulations, norms, staff experiences, and information about children and families, was considered critical for collective knowledge formation. This information should guide both operational plans and budgeting. A continuously updated common operational picture, including tacit knowledge to understand the context behind the numbers, was regarded as invaluable, enabling the systematic advancement of socio-financial sustainability. Participants in both cities emphasised that it is not only about the quantity of information, but also about enhancing the flow of information to ensure that the right information reaches the right people. Here, the crucial role of KM involves producing relevant information and combining data from various sources to support informed decision-making. Participants also emphasized the need to develop improved evaluation and measurement methods, particularly for qualitative indicators, to monitor well-being and the effectiveness of services.

The importance of built-in management structures in all phases of the public management cycle was emphasized. Participants mostly referred to regular meetings where information is discussed and interpreted in collaboration with various experts. However, they also recognized the need for informal gatherings and discussions. It was noted that, especially in multidisciplinary and multiprofessional meetings, patience is often required when building a shared understanding, as each function and individual interprets sustainability goals differently. Indeed, managing socio-financial sustainability necessitates that dialogue takes place at various levels of public management. In the public sector, it is also necessary to acknowledge that political and operational dialogue often overlap. Additionally, it was also discussed how social media has lowered the threshold for participation, bringing politics and citizens closer to everyday service production and public management. This is an essential aspect of dialogic public management and collective knowledge formation, both of which strongly rely on engaging various actors and stakeholders and incorporating their needs and expectations into the discussion. This also relates to another recurring theme discussed in workshops: the role values that always guide dialogue and knowledge formation, whether consciously or unconsciously. Participants strongly emphasized that education services must always strive for the best outcomes for children, and maintaining this core mission should provide a clear guideline for making difficult decisions. Finally, strategies and planning documents were deemed essential for establishing a baseline for dialogue. However, it was noted that strategies often lag behind rapidly changing service needs, highlighting the capability to engage in operational dialogue when strategies do not provide answers to complex questions at hand.

5. Discussion and Concluding Remarks

In this study, we examined how public managers discuss and interpret social and financial sustainability and identified factors that facilitate collective knowledge formation during leadership dialogues in local government. The study enriches the existing KM literature by highlighting its social dimensions and uncovering the factors that support collective knowledge formation in the implementation of sustainability transitions. Our results underscore the importance of dialogue and collective knowledge formation as crucial elements of good governance. These elements foster the creation of public value through open communication and inclusive participation, which are critical for socially responsible and economically viable activities. Trade-offs between social and economic sustainability pose significant challenges for public managers (Zeemering, 2018; Sinervo et al, 2024; Sinervo and Laihonen, 2024). Therefore, it is essential for KM research to explore how it can contribute and assist public managers in navigating resource constraints and increasing service demands.

In this article, we focused on the factors that facilitate collective knowledge formation in public management, a perspective that has not been empirically examined before. Our study examined the process of knowledge formation during leadership dialogues in local government and identified the intangible resources and capabilities required from both organizations and individuals to support and engage in this process. Theoretically, we build on the concepts of knowledge formation (Laihonen, Kork and Sinervo, 2023) and capabilities (Helfat and Peteraf, 2003; Teece, 2007). Table 1 summarizes the identified resources and capabilities for leadership dialogue and collective knowledge formation, highlighting the central role of intangible resources. These resources encompass both organizational and individual aspects. Knowledge formation involves not only individuals and their competences and capabilities, but also requires organizations, specifically leaders and managers, to create enabling conditions for encounters and dialogue between different perspectives. Organizational structures, practices, and culture play crucial roles in facilitating dialogue and collective knowledge formation. On the capabilities side, our data highlights individual capabilities that are perceived as critical for collective knowledge formation.

Table 1: Resources and capabilities for collective knowledge formation

Resources for collective knowledge formation	Capabilities for collective knowledge formation
Organizational resources:	*City 1:*
Shared knowledge base	Understanding one's role in a larger organizational context.
Appropriate organizational structures	Willingness and courage to engage in dialogue.
Ongoing operational models for dialogue	Creating and maintaining models that support dialogue.
Open organizational culture	
Clear objectives	*City 2:*
Trust, psychological safety	Promoting actions aligned with shared values.

Resources for collective knowledge formation	Capabilities for collective knowledge formation
Shared values Sufficient time Communication between the siloes Communication across the levels Relevant participants in dialogue *Individual resources* Personal skills and competences Strong leadership skills Motivation for dialogue Communication skills	Fostering a willingness to find solutions. Utilizing a shared knowledge base.

The empirical data support the theoretical argument that dialogue and collective knowledge formation are integral components of modern public management (Laihonen and Mäntylä, 2018; Laihonen, Kork and Sinervo, 2023). Public managers recognized, at least implicitly, that in leadership dialogue, the viewpoints of institutional complexity, organizational responses, and individual sensemaking are present, conveyed, and integrated into the planning, implementation, and evaluation processes of local governments. This empirical finding supports the knowledge formation framework and reinforces our view that leadership dialogue indeed serves as an arena for collective knowledge formation. Leadership dialogue was considered necessary in all key phases of public management to sense the operational environment, seize relevant managerial issues, and transform actions into effective implementation (Teece, 2007). Notably, the emphasis on specific microfoundations supporting these dynamic capabilities varied between phases. Thus, collective knowledge formation can support the adaptation and renewal of public organizations, potentially serving as a dynamic capability of local governments. This opens intriguing research opportunities regarding the role of knowledge management as part of an organization's dynamic capabilities.

Ethics declaration: The ethical clearance was not required for this research. Research permission was obtained, and the study was conducted in accordance with established good scientific practices.

AI declaration: Microsoft 365 Copilot was utilized to improve text quality and clarity by checking grammar and spelling, and rephrasing content.

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