ENTREPRENEURSHIP AND ECONOMIC TRANSITION IN CENTRAL EUROPE

Jean-Paul Larçon
Editor

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Printed on acid-free paper.

To my daughter Anne-Sophie

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Preface and Acknowledgements

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Research programmes of the Foundation associate HEC faculty to corporate members of the Foundation: Adecco, Arthur Andersen, HEC alumni association, Bain & Company, Banque Nationale de Paris, Bain & Company, Cartier International, Crédit Lyonnais, EDF/GDF, Ernst & Young, Casino Group, Gemini Consulting, Hewlett Packard, Lazard Frères & Cie, L'Oréal, Mars & Co, Paribas, Pernod Ricard, Price Waterhouse, Procter & Gamble, Publicis, Schneider, SNCF.

This book is the result of the HEC Foundation research programme on “corporate strategies in emerging countries”. The programme covers diverse emerging business environments: Latin America, Asia, Central Europe and CIS. Most of these emerging markets have previously demonstrated a high level of uncertainty: economic fluctuations, social turbulence, political instability, and economic nationalism. However, in spite of recent financial crisis in Mexico (1994), Central and Eastern Europe and Asean (1997), they are still very attractive to foreign direct investors resulting from the development of the private sector, new investment codes, the development of regional trade areas and high growth potential.

International management experts face interesting dilemmas for investigation and action on emerging countries. These economies offer a unique opportunity for companies to quickly build a strong presence in new fast growing markets thanks to privatisation, growth of international trade,

investment and globalisation. Yet, this opportunity implies risk and flexibility; firms have to adapt their strategic vision, management processes, and human resource policies to local conditions.

Former research has thus helped in identifying common characteristics such as the management of risks, transfer of technology, restructuring of the value chain on a world basis and new patterns of co-operation between local and international companies. Present research focuses on the specificity of economic transition in Central and Eastern Europe and the relationship between the changes in the economic environment and the opportunities for entrepreneurs, strategies and management processes.

The HEC School of Management has a strong established presence in the region since 1989, training MBA students, professors, managers from the Czech Republic, from Hungary, Poland, Lithuania, and Romania as well. This experience contributed to put the research into perspective and to follow the rapid pace of transition.

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We are glad to have among our authors professors not only from western schools such as Stockholm School of Economics, U. L. Bocconi (Milan), Vienna University of Economics and Business Administration, but also from the three outstanding Central European institutions that have joined the CEMS in 1998:

- Budapest University of Economic Sciences (Hungary),
- The University of Economics, Prague (Czech Republic),
- Warsaw School of Economics (Poland).

We are also glad to have the contribution of Saul Estrin of London Business School, one of the leading European experts on economic transition.

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HEC Foundation and the editor want also to express their special thanks and congratulation to professor Attila Chikán of Budapest University of Economic Sciences: in July 1997 he took the post of Economics Minister of Hungary's' new government headed by Prime Minister Viktor Orban. Attila Chikán is in favour of liberal economic policy, he wants both to assist foreign investors and help the growth of small and medium enterprises, and he will also prepare Hungarian economy and companies to EU accession. Professors and industrialists of the HEC community wish him the best success.

Antoine Bracchi
Honorary Chairman, Ernst & Young and
Chairman of the Board, HEC Foundation

Paris, November 1998

Introduction: Organisation of the Book

Jean-Paul Larçon

HEC School of Management, Paris

Economic transition is part of a transformation process involving major changes at the political, economical, social and psychological level. In less than ten years most countries of Central and Eastern Europe, at the exception of those affected by the war in former Yugoslavia, have re-established a democratic political life, moved rapidly from centrally planned economies to market economies and opened internationally their society and economy. Most of these countries after years of severe economic depression have now recovered and are increasing their participation to European business sphere and world trade.

Privatisation in CEE countries has been the core mechanism of the transformation process; and the transfer of property to private owners radically changed the goals, values and behaviour of all economic agents and decision-makers: employees, pensioners, consumers, companies, stockholders, managers, bankers, municipalities, government agencies.

For some foreign enterprises, CEE countries might be still perceived as a foreign distant, and uncertain environment but for others, ranging from small European family businesses to multinational companies (MNCs), the region in transition is just another facet of the enlarged European domestic market and business environment. Newcomers to the region do not usually face difficulties in operating in this neighbouring cultural environment, but one of

the major challenge for foreign companies is to adapt their management goals, structures, processes and human resource to rapidly changing local market and local business system. Successful companies in Central Europe have simultaneously been highly responsive to local specific transitional dilemmas and opportunities and integrated their regional approach within a broader framework of a global strategic management perspective.

The objective of this book is to clarify the mechanism of transition in Central and Eastern Europe (CEE) and to highlight its consequences in term of entrepreneurship and corporate behaviour.

Key issues, such as privatisation, development of financial markets, participation in word trade, restructuring industries and companies, foreign direct investment and international joint ventures, are quite similar from one country to another. If problems are similar, solutions are not differing so much even if the pace of transition varies a great deal as well as short-term priorities.

The more the process transition continues, the more similarities and convergence can be find in the evolution of local economic and business environment.

The two first chapters consider the region globally and emphasise two important features:

- First the emergence of an entirely new political and business environment, which has already opened the door for new and successful business strategies of international companies,
- Second the success and limits of privatisation: success by the irreversibility of the reform and the sharing of privatised economy, yet serious limits in term of efficiency. In chapter 2, Estrin argues that mass privatisation did not create the appropriate ownership structures and corporate governance and that it might lead to severe difficulties for efficient restructuring.

New business environment, privatisation, restructuring: in chapter 3 to 9 through analysis these aspects are dealt with in depth, using the most characteristic national examples. CEE countries are not homogeneous: they differ from historical, political, cultural point of views. Some are relatively rich like Slovenia or the Czech Republic, other much poorer like Romania and the Baltic Republics. Four countries are the concentrated on: Czech Republic, Hungary, Poland and Romania, a total population of 83 million inhabitants with three leaders of transition: The Czech Republic, Hungary and Poland and a late comer Romania.

In chapter 3 Nemcova draws the lessons of Czech Privatisation and confirms Estrin quote opinion looking at the positive and negative results of Czech voucher privatisation. She explains the links between voucher privatisation, the power of Investment Funds and the relationship between Funds and

Czech leading banks. She concludes on political success of privatisation and serious shortcomings in term of restructuring and corporate governance.

In chapter 4, **Musilek**, discusses the Prague Stock Exchange and a technically well adapted system of trading but which is lacking of serious regulation. The financial market is not yet in a situation to directly serve the needs of Czech companies looking for capital for long term growth.

In chapter 5 **Chikán** and **Czáko** concentrate on the issue of restructuring and competitiveness. They point out the four key areas that have influenced competitiveness: changes of the economic mechanism from shortage economy into a market one, the social acceptance of the changes, the characteristics of economic policy and the management of the firms. The authors see the substantial improvement of the performance of Hungarian companies as the result arising from market forces than government economic policy. They also identify managerial skills as a key element of differentiation between Hungarian high and low performing companies.

Continuing in Hungary in chapter 6, **Zsolnai** probes the ethical fabric of a transforming economy. The social reception of market economy in Hungary as well as the ethical attitudes and values of managers that are still in transition and may involve a lot of ambiguities and ambivalent feelings. The ethical posture of Hungarian companies differs strongly according to two dimensions: the intensity of competition on the local market and the degree of exposure to international competition.

In chapter 7 **Romanowska** explores the links between economic growth and Foreign Direct Investment (FDI). Poland, the largest economy of the region is now also the leading host country for FDI. Romanowska points out FDI as a key success factor in the transition process thanks to the transfer of resources and technology, the development of exports, and the positive influence on Polish companies' competitiveness.

In chapter 8 **Alessandrini** investigates the links between social, political and economic transition in Romania. The absence of political stability and a lack of clear direction in term of economic policy have had a very negative impact on Romanian transformation. Real progress in privatisation and in the establishing the legal framework for a market economy is recent and the Romanian government has still to face the difficult challenge of privatising and restructuring large SOEs and public utilities.

Final chapters study three specific aspects of transition: the role SMEs, the strategy of MNCs, and the impact of EU enlargement on business strategies.

Chapter 9 examines the effects of co-operation between small companies of Eastern and Western Europe. Quite spontaneously since 1989 small companies have rediscovered the trade routes of the past. **Zagler** and **Ragacs** draw our attention on the role of these co-operations especially in the process of diffusion of innovation and demonstrate their positive effect

on growth.

Chapter 10 focuses on the behaviour of multinational companies. Swedish MNCs were operating in the region before transition and old relationship helped developing new business. **Nordström, Vahlne and Torbacke** emphasise the sequential moves of five MNCs in the region and the differentiation of attitudes in term of risk taking. In most cases Eastern Europe strategies integrated into global corporate strategies.

Chapter 11 addresses the issue of EU enlargement. **Debié** outlines some of the difficulties of the enlargement process due to the of lack of political consensus in the West, ambivalent public support in CEE itself, lack of resources and absence of clear deadlines. Thus, companies operating in CEE still have to face the uncertainties of the agenda and maybe new internal regulatory barriers within CEE according to the status of the country regarding accession.

In spite of these limitations due to EU governance, the transition and enlargement process are offering an unusual window of opportunity for small and large firms, local and international companies doing business on a pan-European basis.

ABBREVIATIONS

ASEAN	Association of South East Asian Nations
CEE	Central and Eastern Europe
CEFTA	Central European Free Trade Agreement
CEMS	Community of European Management Schools
CIS	Commonwealth of Independent States
CMEA	Council for Mutual Economic Assistance
COMECON	See CMEA
CPE	Centrally Planned Economy
CR	Czech Republic
CZK	Czech Koruna
EBRD	European Bank for Reconstruction and Development
EFTA	European Free Trade Association
EU	European Union
FDI	Foreign Direct Investment
FPN	National Property Fund (Czech Republic)
GDP	Gross Domestic Product
GDR	German Democratic Republic
IMF	International Monetary Fund
IPFs	Investment Privatisation Funds (Czech Republic)
JV	Joint Venture
MBA	Master in Business Administration
MEBO	Management and Employee Buy Out
MNCs	Multinational Companies
NATO	North Atlantic Treaty Organisation
NIFs	National Investment Funds (Poland)

NIS	New Independent States: former republics of the Soviet Union, minus the Baltic States, and Mongolia
NGO	Non Governmental Organisation
OECD	Organisation for European Co-operation and Development
PAIZ	Polish Agency for Foreign Investment
Phare	A EU grant assistance programme for CEE
PLN	Polish Zloty
PSE	Prague Stock Exchange
SMEs	Small and Medium Size Enterprises
SOEs	State-Owned Enterprises
Tacis	EU grant assistance programme to twelve countries of the former Soviet Union and Mongolia
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
Visegrad Countries	Czech Republic, Hungary, Poland, Slovak Republic and Slovenia
WB	World Bank
WSE	Warsaw Stock Exchange