

**Barriers to Transition of Enterprises in BSEC Countries:  
From Central Planning to Market Economy**

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**1. Introduction**

The post-communist countries belonging to the Black Sea Economic Cooperation (BSEC) still face enormously demanding challenges that encompass the rapid collapse of traditional markets, legal and institutional uncertainties regarding ownership and governance, rampant inflation, cash flow blockages (e.g., the non-payment for goods delivered to customers and the wide spread unavailability of bank and trade credit), the appearance of technologically and financially superior global competitors from outside the region, lack of skills and of experience for operating in a market economy and workers and managers who are frightened, suspicious, or even hostile with respect to the monumental change required.

The need for transforming managerial practices in BSEC<sup>1</sup> countries from those employed in centralized, command economies to those appropriate for a competitive market-driven business environment is widely recognized. However, little is being done to understand the horrendous difficulties that attend this challenge. Knowing what to change and what to leave in place -either because of its intrinsic value or because of its impenetrable and unyielding nature- further complicates the situation.

It is of great importance to know how dynamics of change might relate to underlying conditions and to examine the process of transforming internal and external practices in BSEC countries. The purpose of this paper is to gain an understanding of some

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<sup>1</sup> Our study is concentrated only on the post communist BSEC countries, to be referred to in this paper as BSEC countries. We do not deal with Greece and Turkey, as their entirely different economic systems, conditions and constraints render them as not significantly comparable to transforming post-communist countries. Another study in some way complementary to ours has been conducted by International Institute for Applied Systems Analysis during 1996.

of the barriers to transition of enterprises in BSEC countries from central plan to market.

The business environment determines the situation in which managers must operate. Such a situation has opportunities and constraints. It is affected by economic, systemic (organizational), legal, political and national factors.

Economic factors refer to the changes and problems created by the upheaval of the macroeconomic system in BSEC countries.<sup>2</sup> Deep and prolonged recession, high and persistent inflation, lack and exorbitant cost of capital and stifling taxation, are among the most important macroeconomic barriers of cooperation.

Systemic factors refer to the difficulties that emerge with the creation of important institutions for the effective functioning of a market economy.

Political stability is a fundamental prerequisite for sustained economic transformation. Internal, external and ethnic conflicts cause serious problems to the economy of each country and as happened in Yugoslavia, results in isolation and collapse.

Unsuitable infrastructure is also crucial for successful transformation. It is mainly related to transports, communication and energy.

The suitable legal framework is a prerequisite for the development of business activities. It is related to the confusion over ownership, to privatization, to labor legislation, legislation on land, on property rights and on foreign investment.

The degree of understanding and skills of managers in market economy related knowledge, like marketing, finance and business strategy, as well as international experience, age and command of foreign languages determine what managers can accomplish in the volatile conditions of the BSEC countries.

Finally, attitudes and values determine the willingness of people to implement changes and transform their enterprises. Fears, stereotypes, ideology, mentality, old habits, persistent values of the old system, resistance to new ideas, conflicting rules of the game, entrenched behavioral patterns and corruption put additional barriers to transition from central plan to market of enterprises in BSEC countries.

The next section of the paper describes the methodology used. Part 3 of the paper examines the role of the business environment as a determinant of successful transformation of BSEC enterprises. Part 4 focuses on the workers' skills and

knowledge, while part 5 sheds some light on attitudes and values as factors affecting transition from central plan to market of enterprises in BSEC countries. We offer conclusions and proposals in part 6 of the paper.

## **2. Analysis and Methodology**

The study is based on two main sources: (a) review of relevant literature, (b) the authors' research, publications and direct experience on the subject, and (c) individual interviews of managers of state and post state owned enterprises as well as of post communist entrepreneurs who are employed in manufacturing.

The purpose of the interviews is to obtain information about specific instances in which efforts to marketization were successfully carried out and instances where such efforts were unsuccessful or prevented. Managers and entrepreneurs were asked to describe, in addition to certain information about the firm and personal background, one specific example of successful marketization effort in their firms and one specific example of an unsuccessful effort.

More specifically, the study was based on field interviews of 30 managers from state and post state owned companies and of 30 post communist entrepreneurs in three representative BSEC countries; the largest one: Russia, the smallest one: Albania and a medium one: Bulgaria. So from each of the three countries there were 20 interviews (10 with managers from state and post state owned companies and 10 with post communist entrepreneurs). This categorization helped us characterize the nature of resistance employed by managers and entrepreneurs in different microeconomic and organizational settings as well as in different countries with distinctive cultural and economic features and with a dissimilar pace of the transformation process.

The managers interviewed were asked to provide background information about their firms and to comment (a) on the principal barriers to effective transformation providing information about the role of the business environment (legal, economic, taxation, finance, foreign exchange, infrastructure, political, communication and transportation, trade barriers); (b) on the lack of skills and knowledge, and (c) on the attitudes broadly held not favoring marketization.

They were also asked to describe one successful and one unsuccessful effort of transformation, providing specific information about each effort (technique used,

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<sup>2</sup> See Salavrakos (1997).

managerial practice, company policy or something else); the people involved in making the decision, in carrying it out, and those being affected by its results; the duration of the transformation effort, and the principal reasons for success or failure.

Finally, they were asked to comment on their specific experiences regarding the principal current barriers to effective marketization of their firms, industry and country as well as on the most important facilitators to getting changes to occur successfully.

We followed the “Saturation Point” qualitative research method in our evaluation.<sup>3</sup> According to Bertaux (1980), the number of cases that need to be studied is not fixed to 10, 11, 30 or 31 stories, but to as many as are necessary to reach the saturation point on the issues revealed. As Bertaux and Kohli (1980) mention, “the method of the saturation point substantiates generalization and validity of the results exactly as does the random sample in qualitative research”.<sup>4</sup>

Previous literature on internal barriers to change from plan to market, giving more emphasis to individual or micro level of enterprises, is limited. International Organizations such as UNECE, EBRD, World Bank, and EU emphasize the role of macroeconomic factors for effective marketization and change in Central and Eastern European countries. We have used the following previous literature and studies as main sources for our analysis:

First, an article by Vlachoutsicos and Lawrence (1996) which deals with managerial learning in Russia.<sup>5</sup> The authors realize that Russia needs the managerial learning required in order to support a massive wave of entrepreneurship, especially for the creation of distribution and credit organizations. Also Russian managers need to be familiarized with a selected set of management skills and techniques relevant to dealing with the challenges of a competitive market. By using a number of interviews as the main methodological tool, it was revealed that an effective transmission of managerial techniques takes place only when this is based on joint problem solving. Therefore, it is of paramount importance that western managers study and understand the inner logic of traditional Russian managerial values and practices.<sup>6</sup>

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<sup>3</sup> See Bertaux (1980)

<sup>4</sup> See Bertaux and Kohli (1980). See also Gummesson (1991), Easterby-Smith, Thorpe and Lowe (1991), Crabree and Miller (eds) (1992), and Kirk and Miller (1992)

<sup>5</sup> See Vlachoutsicos and Lawrence (1996)

<sup>6</sup> See Kharkhordin and Gerber (1994)

Many of these values and practices seem to be rooted in the Russian Collectivist Value System (RCVS), which is elaborated in a recent study by Vlachoutsicos (1998).<sup>7</sup> Collectives are an organizational form largely unique to Russia. They are closely-knit work groups bound together with shared values and mutual support. The authors conclude that the degree of effectiveness and stability of the market economy to which the Russian system is transforming will greatly depend on the degree of transmutation of RCVS to the new values and practices which the new Russia will be able to contain and integrate. In a number of ways these conclusions can also be applied to the remaining post communist BSEC countries with similar cultures, all of which have been subjected to the Soviet systemic straight jacket for a long time. Thus, regarding the process of transformation, the challenge is to distinguish what to change and what to leave in place—either because of its intrinsic value or because of its impenetrable and unyielding nature. In an effort to meet this challenge, it is also important to distinguish the specific forms of market economy best suited to the particular cultural, systemic and economic situation prevailing in each country.

In another study, Aguilar, Loveman and Vlachoutsicos (1994), the main managerial challenges in Central and Eastern Europe are discussed. By using field interviews of 250 practicing managers, the authors found that the most effective method for improving performance in Central and Eastern Europe, is setting realistic goals, explaining the need for change to those involved or affected, motivating stakeholders, training, supporting the efforts requiring performance and persevering with patience. The success of business ventures in Central and Eastern Europe will depend on management's ability to reach through their organization's suspicions and defenses and to tap into the latent energy that lies within.

Also, Gacs and Cooper (1997), conducted country, topical and enterprise case studies to explore the impediments to exports that small transition economies face once the initial systemic changes and the switch to Western markets have taken place. Studies were prepared for eight countries in transition: Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Romania, Slovak Republic and Slovenia. The results indicated that adjustments at the enterprise level and in microeconomic policies (activities of government that alter resource allocation) influence export performance more than macroeconomic state intervention.

Finally, another source for this study is the extensive personal experience of the

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<sup>7</sup> See Vlachoutsicos (1998).

authors.

### **3. The business environment**

Among the most often cited barriers of enterprises in BSEC countries to transition from central plan to market were those that are related to the business environment of each country.<sup>8</sup> The business environment -including economic, legal, political and infrastructural considerations- must be such so as to permit and motivate the new, desired entrepreneurial and managerial practices. It formulates the situation (constraints and opportunities) in which managers and enterprises must operate.

The macroeconomic system is decisive for the creation of the necessary business environment in BSEC countries. Deep and prolonged recession, high and persistent inflation, lack and/or exorbitant cost of capital and stifling taxation, are among the most important macroeconomic barriers of performance and ergo of competitiveness in the arena of the international market including BSEC countries.

### **4. Skills and Knowledge**

A large number of respondents pointed to the managers' lack of skills and knowledge as major barriers to transition of enterprises in BSEC countries from central plan to market. The degree of knowledge and skills of managers determine what they can accomplish within and among BSEC countries. Business strategy, marketing, finance, strategy, human resource management, international trade experience and command of foreign languages were singled out as the internal functions in which business practitioners in BSEC countries were most deficient.

As two respondents from Bulgaria explained:

*Lack of experience and knowledge in a market economy environment, and especially in the marketing field, is one of the most persistently recurring reasons for failure. Professional incompetence is the principal obstacle.*

*Lack of training of managers is another problem. There are no*

*management studies at University level. There are only economics courses. Therefore managers do not apply the western practices of managers. They learn by doing. The old management structure is reluctant to accept the change. We need quality at the western European level but our conditions are at the eastern level. Having started to deal directly with foreign partners, we realized our weak points, poor quality.*

*Lack of professionalism is the problem. We still have people from the party. Or from the secret services. Even in financial markets people without professional experience and education.*

The above can be complemented with the following comment made by an Albanian respondent:

*At the beginning of the 1990s, there were about 27,000 students in all various branches of the Albanian system of higher education, a small percentage compared to the rest of Europe. There was a total vacuum of market oriented experts in such branches as administration, management, finance and banking, marketing, micro-macro economics, justice, and social and labor psychology.*

The ability of managers to develop the necessary skills and knowledge is constrained in a number of ways. One of the more serious of these is the enormous time pressure under which most managers are operating in trying to cope the many rapid changes taking place. Another is lack of the capital or financing required in order to pay for high quality management training.<sup>9</sup>

The lack of suitably qualified managers in BSEC countries should not be taken to imply that there were no managerial abilities under the Central Planning. Although it is true that many decisions were taken by the Party, it was impossible for the central planners to take the bulk of managerial decisions and to communicate the requirements

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<sup>8</sup> An outline of synthesis of findings from all sources of the study is provided in the appendix at the end this article.

<sup>9</sup> See Aguilar and Vlachoutsicos (1992), Kornai, (1980) also Lavigne (1995).

to the enterprise management in a suitably desegregated way.<sup>10</sup> Also, both output plans and inputs, though decided above, were often implemented on the basis of information and proposals submitted by managers. Central planners did not have all the information required when taking decisions so that much power was de facto decentralized to the level of the firm. A variety of innovations in product design and in methods of production were initiated at the enterprise level. Furthermore, in matters relating to the supply of inputs, there was much scope for manager's initiatives.<sup>11</sup> In fact, enterprise managers were very adapt and effective "shortage" managers, mostly oriented to obtain for their enterprises the inputs needed in order to be able to fulfill the production plan imposed by their superior ministry, rather than market oriented managers responsible to stockholders for profitable business. These managers, however, had to function without effective systems of incentives and rewards, where the enterprises were not responding to customer preferences and where there was no competition between producers of the same goods or services. Therefore, their skills had to be more political than managerial.

The privileges, which many managers of state enterprises heaped upon one another, created a very negative image.

This is what a Russian respondent commented:

*The work of the managers was left to their subordinates. Among the people, it was a status symbol to do practically no work whatsoever. Few of the men in power had traveled to foreign countries other than Communist ones. They could seldom read a foreign language and thus had all sorts of mistaken conceptions of the world around them. They were the objects of endless mockery by the general public, especially in the later years of the Breznev era, but they had little inkling of this and would scarcely have understood the jokes in any case. They put the breaks in any attempt by their subordinates to introduce reforms, although these were seldom of major import,*

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<sup>10</sup> For a detailed analysis of the nature of management in eastern Europe under the legacy of the central planning, see Vlachoutsicos and Aguilar (1992), as well as United Nations Commission for Europe, Trade Division (1992)

<sup>11</sup> According to Vlachoutsicos and Lawrence (1996), Russian managers did an effective job of providing leadership up and down the organizational hierarchy. They had also developed extraordinary skills at coping with persistent supply shortages.



*until it was too late to do anything. The life they lived was a lie.  
They sank the Soviet Union.*

The above lead us to the following insights regarding managerial education and skills in transition economies: First, there is a shortage of managers with such skills as marketing, sales and capital accounting, all of which are indispensable in meeting the challenges of the competitive market. Second, the distinctive - management system practiced during the Soviet era has left its imprint on present managerial practices in Eastern Europe and the CIS. Vlachoutsicos and Lawrence (1990) in their research in Soviet state enterprises found, for example managerial practices developed on the basis of the principles of Soviet democratic-centralism, which are very different from the systems practiced by western management.<sup>12</sup> Thus, they observed a decision making process that alternated between top - down phases, lower level discussion, bottom-up and proposal formulation, top deliberation and decision and top down commands. The alternation between bottom-up and top-down communication made it possible to reconcile grassroots participation with centralism. Meetings of the command phase had the leader at the head of a rectangular table with subordinates along the sides in sequence of descending rank. Nobody questioned who the boss was in all sessions.

Because of the very different managerial values and practices of Eastern Europe, western managers often face serious difficulties in understanding, with their local counterparts communicating and cooperating effectively. Some efforts have been made to overcome these challenges through briefing programs for western managers. However, developing such programs is especially difficult since western experts and BSEC managers have limited knowledge of each other's managerial experience and culture.

This situation has major implications for Western professionals charged with delivering the know-how and for sponsoring institutions as well as for BSEC organizations and their staff who are supposed to be the ultimate beneficiaries.

The following remarks by Russian and Bulgarian responders are characteristic:

*However, western "mentality" is also an obstacle to change when investors or economists want implement changes over there by "shock therapy", it reminds the old Stalinist mindset of "cleansing society by liquidation of bourgeois elements.*

*There is a communication gap between native and foreign businessmen. The general attitude is that foreign businessmen may have skills and knowledge but they cannot understand the peculiarities of the Eastern European economies and markets.*<sup>13</sup>

*The ignorance of the inner structure and product policy of the big industrial enterprises runs to wrong decisions, which is often the cause of the arrogance of the western managers.*

The above can be complemented with the views expressed by A. Kennaway (1995) in a recent paper:<sup>14</sup>

*Milliards of hard currency have been provided by western aid agencies. The money has largely gone in ill-thought-out loans and investments in projects that will not be carried out properly and also in the payments to consultants, mostly westerners who are not given the right terms of reference either at home or by the supposed beneficiaries. Nor do the westerners understand Russian conditions well enough. Finally, their reports are often not followed through and their audit is inadequate to see whether they are effective or not. The bureaucracy of western aid agencies is shameful; some of them give the impression that their main purpose is to spend the money allocated to them rather than to be concerned about the usefulness of the work. Furthermore there is growing evidence of collusive, personal, corruption between western aid executives and consultants*

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<sup>12</sup> Vlachoutsicos (1998)

<sup>13</sup> Still, many interviewees consider the communication they have with foreign businessmen important and believe that they can profit from their experience.

<sup>14</sup> See Kennaway (1995). See also Waller (1981)

*on the one hand and the local representatives and officials and Ministers on the other.*

Adapting the education package is not an easy task.<sup>15</sup> The gaps in the curriculum have led to missing concepts. “Efficiency” for example means something very different to a manager seeking only to comply with a central plan than to one seeking to boost profit and market share in a competitive system. Although language adapts rapidly, missing concepts and, as a result, missing words still seriously impede speedy and effective transfer of knowledge and skills.

## **5. Attitudes and Values**

Attitudes and values determine the willingness of people to implement changes and transform their enterprises. Among the most often cited factors of unwillingness of people in post-communist countries to implement change, are fears and uncertainties, attitudes and “mentalities”, ideology (collectivism), unreceptiveness to new ideas and corruption.

Several generations of living and working in a hierarchical, command society have resulted into a managerial mindset that is very different from that required to function effectively in an openly competitive business setting. This managerial mindset is derived from persistent values and habits of the past, of intense discomfort when taking initiatives and responsibilities, all of which deprive people to admit the new of the market reality, as indicated in the following remarks by Russian, Bulgarian and Albanian respondents:

*The psychology of the people and old stereotypes are very important barriers to transition from central plan to market of enterprises in BSEC countries. These barriers are unfortunately wide spread in all post communist countries and can be called unwillingness of people to admit the reality if the reality asks for more effort and responsibility.*

*The principal obstacle to change in managerial practices in this firm*

*is the employees mentality, their lack of entrust to improve their work.*

*The principal barrier is unwillingness of the staff to change their stereotypes. They wanted to continue working in the same way as before. This was due to the people 's psychology and their mentality formed in the past decades.*

*Unfavorable attitudes from the employees' side, but those are normal reactions to change (people are reluctant when changing the production, the rhythm).*

*In socialist conditions people used to say the following slogans "whether you stay, whether you lay-you will be paid your salary". Now we have to strongly fight with such point of views.*

Almost ten years after the collapse of socialist control planning system and the commencement of changes towards market based economies, people of BSEC countries are still affected by important elements of the past. This is also reflected in the behavior of managers related to layoffs. For example firing employees in order to reduce costs is a notion going against the socialistic concept of the workers collective which in contrast to Western Unions include everyone working in the enterprise, irrespective of their position, i.e. from unskilled industrial workers and clerks to top management.<sup>16</sup> In their identities as members of the workers collective, all members perceive themselves, and are recognized by superiors, subordinates and by society at large, as equals<sup>17</sup> and as integral and inextricable parts of the enterprise, entitled<sup>18</sup> to their position in the enterprise.

As a matter of fact an unforeseen consequence of the process of privatization in most BSEC countries has been that the threat outsider stockholders pose to old

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<sup>15</sup> See Vlachoutsicos and Lawrence (1990)

<sup>16</sup> See Slider, (185).

<sup>17</sup> With the process of bureaucratization of the Soviet system, this equality became increasingly perverse and therefore did not generate the pluralism, individuality and creativity it might have, had it been genuinely applied.

<sup>18</sup> This particular feeling of entitlement is comparable to that of Western stockholders about the company in which they own large blocks of stock. During the current mass privatization taking place in Russia this feeling has converted from political entitlement to taking part in enterprise decisions to economic entitlement to own part of the enterprise.

management and to the workers continued employment serves, in many cases, to reinforce the solidarity between old management and workers'<sup>19</sup>. Fear of the future, and the new and unknown Russian and foreign owners of the enterprise, further reinforces the strength of this solidarity. In the 1995/1996 research project "Russian National Survey" designed to track down the fortunes of privatised enterprises and directed by two US advisers to The Russian government, Harvard professor and economist Shleifer and Joseph Blasi professor at Rutgers University's Institute of Management and Labor Relations, revealed that two-thirds of general managers interviewed said that they and their employees would oppose selling a majority of shares in the enterprise to an outside investor even if he would bring the entire amount of capital necessary to modernize and restructure the firm.<sup>20</sup> Workers remain loyal to the old management by supporting it with the vote of their stock in exchange for being kept on the payroll, and thus continue to receive whatever fringe benefits, services and care enterprises still provide. Through this tacit understanding management can fence off outsiders, consolidate its position and preserve its clout as leader of an enterprise with a large workers collective, which local, regional and federal governments cannot politically afford to ignore.<sup>21</sup>

This is what a Russian respondent remarked:

*Refusal of many employers to play part in dismissal of people, which is derived from the communist mentality that wages must be differentiated according to employees' years in firm, not to their competence and knowledge.*

*Managers still spend much more time negotiating with the government than taking care after their own business.*

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<sup>19</sup> See Hanson, (1995).

<sup>20</sup> Blasi, Kroumova and Kruse, (1997).

<sup>21</sup> Clarke, 1994, pp. 178, 181. See also *The Financial Times*, 6 September 1996, p.10. It has been observed to the writer by Professor Phil Hanson, that it remains difficult for outside investors with a potential for strategic control to acquire a controlling stake. Small outside investors who allow insiders to retain control are, of course, no threat. Nevertheless, some strategic, outside investors -Oneximbank, Menatep, Inkombank, Kakha Bendukidze, etc, are gaining control of firms here and there. But continued low share prices relative to earnings or assets suggest that, for the most part, markets for corporate control remain hard to contest.

Fear and uncertainty is another impediment to transition of enterprises in BSEC countries from central plan to market. It is the fear of “being independent and self responsible not having an ‘umbrella’ for unfavorable situations”. It is the fear “of ignorance of markets”, the fear of “too many quick changes”, the fear of “losing the job”, the fear of “losing status and power” and the fear for “increasing unemployment”. They are all derived from a deep suspicion of changes and a risk averse behavior well justified by the objective uncertainty and the high volatility prevailing in all BSEC countries. Uncertainty as regards to the future economic contingencies is amplified by infrastructural weaknesses and an underdeveloped market culture.

This is what a Bulgarian manager remarked:

*The manager is ready to adopt and realize changes, but the Board of Directors is not going to take the risk. They are reluctant, slow and unwilling to adopt the change.*

*We are at the threshold of changes but they are of real importance only to owners and are connected with the battle to be on the Board.*

*Major problem in the process was the resistance of some of the managers because of the fear of losing their positions.*

*The uncertainty of the people increased in all areas. Uncertainties about the future make some people to care more of the relations with the managers than of the quality of their job.*

*This psychological barrier cannot be overcome only with a training of a lecture or discussions and brain storming at managers 's meetings. It needs overall environment and circumstances to work unilaterally in the same direction.*

Obviously, in the present macro economic environment in BSEC countries such fears are perfectly realistic and it would be naive to expect that fundamentals can

change soon. Nevertheless, many of the specific changes which are required for the survival of enterprises, have no bearing on manpower requirements and some actually help save jobs. In this sense workers' fears are not always realistic.

We have no evidence that workers evaluate each specific measure on its merit. What seems to be self-evident is that change in the economic system means loss of jobs. Hence any change is undesirable. This belief builds a major a priori resistance towards new methods, rendering fear of unemployment the key to the negative attitudes and behavior of workers vis-à-vis whatever specific changes they are called upon to implement.

Collectivism, the recognition of the power of the Workers Collective in state enterprises, was another attitude often cited as a serious impediment to change.

The following remarks of two Russian managers and one Albanian are characteristic:

*The principal obstacle to changes in managerial practices in my firm and in industry as well as in the whole economy is the mentality of workers.*

*Decisions were made under the terrible pressure of the workers collectives even if some measures were not efficient for the future of the company. For instance, the workers collectives required that the company hires only from within in spite of the fact that, for some jobs, it was necessary to hire from outside the company on a competitive basis.(i.e. with higher pay than the workers).*

*A general staff meeting was held in which the workers' collective considered the critical suggestions and new proposals.*

Communitarianism constitutes a coherent pattern of values and prescriptions of behavior. It is particularly evident in the CIS. The Russian Communitarianism value system is a persistently enduring feature of Russian life, which has predated communism and still persists as a major social force in the post-communist era.<sup>22</sup> All persons working in an enterprise, irrespective of their position, are all considered to be

equal members of the workers' collective of the enterprise. For this reason, workers have a strong feeling of entitlement to participate in the decision making process of the enterprise. This entitlement is recognized by their superiors, and even by general directors. Thus the "invisible fist" of collectivism often thwarts the "invisible hand" of the market in the process of transformation of BSEC economies.

Unreceptiveness to new ideas, rules and behavioral patterns of enterprises in BSEC countries are also barriers to successful transition from plan to market. Many of these attitudes can be attributed to fallen living standards, uncertainty about the future, and the people's difficulty to find new productive functions for themselves in the new market environment. The ineffectiveness of central state administrations exhibited up to now are displayed in their inability to address urgent social and economic problems. Without a well- functioning institutional system, good intentions can rarely be translated into reality. There is no certainty and considerable vacillation about the role government should play in the transformation process, and about the kind as well as the extend of regulatory and monitoring fiscal instruments the government should use for promoting technological efficiency, as well as provide appropriate incentives to the economy.

The old centralized system of management is by and large still in place and still acts as the main coordination mechanism between different levels of management in the existing institutional framework. Traditional practices of intervention of the central government in local management of the economy persist because of the inherited central planning culture, and the inherited operational rules and patterns of governing, but also because the network of the old management nomenclature has by and large not changed. Managers and policy-makers have been nurtured in the previous system. This succeeds in keeping most modern professionals with new knowledge out of influential positions and by and large tends to preserve the old style of career development.

A centrifugal shift of primarily political and secondarily economic power is occurring. A new consensus is gradually emerging on the importance of regional self-management. Wavering central governments, are obliged to increasingly concede more power and responsibilities to regional and local authorities. However, control of financial resources is not being relinquished at a corresponding rate. In this respect it

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<sup>22</sup> See Vlachoutsicos (1998).



has to be realized that as the economies of BSEC countries, albeit at widely different speeds, are being privatized, an increasing amount of economic power that under the old system belonged to the state, now is moving to private enterprises. These conditions limit the ability of regions to finance growth potential required in order to improve the structure of regional economies and to address their mounting social, economic and environmental problems.

Another major barrier to transition of enterprises in BSEC countries from central plan to market is corruption, fraud and organized crime.

The following statement by a Bulgarian respondent is characteristic:

*One of the main problems is corruption at customs offices. Public servants' salaries are extremely low and therefore try to increase them by creating obstacles (bureaucracy, delays) and then solving them.*

Similarly to the above, Vladimir Shlapentokh (1996) wrote in a recent paper:

*The corrupted character of law enforcement forces is of special importance since it deprives Russian citizens of the hope of finding help from the police and courts in their fights against criminals and corrupt bureaucrats. Yuri Luzhkov, the Moscow Mayor, openly accused his own police of corruption and inefficiency. The privatization of the Russian army has created a virtual norm of behavior among generals, officers and soldiers in the illegal trafficking of weapons and thefts of equipment. This implies that the scope of legal activity conducted by the state machinery has diminished radically, while the number of illegal deeds performed by bureaucrats has increased.*

*...Practically, already by 1995 most active people in the country are linked directly or indirectly either with corrupt officials or with criminal organization or with both. Business in the country is*

*impossible without the support of corrupt bureaucracy and criminal organizations. The activities of these two classes of people are in Russia no less "normal" than the activities of people who do not violate the law.*

The phenomenon of corruption in BSEC countries is a very complex issue and as such has many sides and aspects. Therefore its elucidation requires a great deal of separate research. Obviously, our study can only deal with it unsystematically. Corruption thrives when both public officials and private agents have little to fear, precisely the situation in most transition settings where a power vacuum is being created as old political power structures cease to exist and new ones have not as yet taken over. The low official earnings of public servants make illicit income a sine qua non for their survival. In some countries such an income now represents the main incentive to remain in public service. Therefore, using the term "corruption" in many cases distorts and does not reflect reality in BSEC countries.

Also, recent privatization of state monopolies is being done often without appropriate consideration of ways to create genuine competition in each sector of the economy and therefore it creates instant millionaires and helps organized crime to gain a stranglehold on certain areas of the economy.<sup>23</sup>

Organized crime is closely intertwined with corruption. With unmonitored private business opening new avenues for criminality, current and former public officials often facilitate or participate in organized crime. Russia's Mafia is not a single organization but a collection of perhaps 3,000 to 4,000 groups employing many thousands of people.<sup>24</sup>

According to Krawciw (1996), in Ukraine organized crime and corruption present one of the greatest dangers to national security because they have penetrated, and intermingled with, the state apparatus at all levels. Organized crime in Ukraine has also forged strong links with international crime and is attempting to gain control of the import-export system, as well as diversifying into privatization and banking.

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<sup>23</sup> See Vlachoutsicos and Lawrence (1996)

<sup>24</sup> See World Bank, World Development Report (1996)

## **6. Conclusions and Proposals**

In this paper, we explored and investigated the main barriers to transition of enterprises in BSEC countries from central plan to market. The analysis included individual field interviews of 30 managers from state and post state owned companies and of 30 post communist entrepreneurs in three representative BSEC countries; the largest one: Russia, the smallest one: Albania and a medium one: Bulgaria. The purpose of the interviews was to obtain information about specific instances in which efforts to transformation were successfully carried out and instances where such efforts were unsuccessful or prevented.

Our study revealed that one of the main reasons for the slow progress of the BSEC economies is that reforms at the individual enterprise (micro) level have been neglected. Incentive and training programs must provide the impetus needed for state enterprises to be to restructure themselves into smaller viable market oriented firms, and to help BSEC managers transform themselves from shortage focused managers operating in a planned economy, to profit-focused managers operating in a competitive market economy. Developing such programs is especially difficult, since Western teachers of management and East European managers have a limited base of shared management knowledge and organizational culture.

The example of state enterprises in Russia and in other BSEC countries, with function as collectives, is useful; collectives are deeply rooted traditional forms of social organization in some of the BSEC countries' cultures. Efforts to introduce management techniques suited to a market economy will almost certainly fail, unless the techniques chosen from the arsenal of modern western management methods, complement and build upon local traditional managerial values.

This gap in understanding, which western governments and other organizations providing assistance to BSEC countries in various forms, creates misconceptions, which render the effective transfer of knowledge and know-how as well as business cooperation very hard, if not impossible. The need to deal with this gap becomes increasingly necessary. Attitudes and managerial behavior of local managers and officials, which often appear to western eyes as being uninformed or strange, have as a rule a very strong inner logic. Trying to understand the inner logic of such behavior before passing judgment constitutes a major step for coping with this gap.

Westerners dealing in post-communist countries invariably encounter attitudes and behavior, which appear "strange" and/or "ignorant" and/or "incompetent" and even

against the best interests of the person concerned. Experience indicates that invariably there is a sound “inner” (concealed) logic, which dictates such attitudes and/or behavior.

Instead of succumbing to the natural propensity of feeling frustrated and/or irritated and/or contemptuous when encountering such behavior, Westerners are well advised to perceive same as a useful signal indicating that they do not understand important aspects of the specific puzzling incident or behavior.

Therefore, it is indeed worthwhile to spend time and effort in order to grasp the “inner logic” behind each case, which invariably will enhance their understanding and thus their ability to develop effective working relationships with their local colleagues, clients and partners.

Experience further indicates that the “inner logic” in most cases arises from an amalgam of:

- shortage of means and/or
- “face-saving” mechanisms to hide shortage and/or
- blind fear of loss of status, power or influence.

Therefore, in each instance, the quest to grasp the “inner logic” should start with seeking answers to the following questions:

1. What product or service is lacking?
2. Which aspect of the situation and/or behaviour and/or articulation could be perceived by the individual concerned as shameful or inhibiting?
3. How could the situation be perceived by the individual concerned as a threat to his/her status, power or influence?

A better understanding on the part of the west of the inner logic of the apparently incomprehensible ways BSEC countries often go about addressing the challenges of transformation would undoubtedly assist the joint development of effective programs. Taking into consideration the low credibility of declarations and of oral explanations in these countries, programs involving joint concrete problem solving teams, task forces rather than teaching or lecturing, seem to be the most effective way to transfer managerial knowledge.

Our study revealed that generalizing about the features of local managers and of entrepreneurs of BSEC countries is misleading. A whole new class of local

managers with a stake in the market economy towards which their country is striving has been developing in recent years. While sharing the same traditions and being subjected to the same environment with old managers, an increasing gap in "mentality" and managerial methods being applied has been created. There is already a significant number of younger local managers who "do not carry the baggage" and do not identify with the managerial values and practices of the command economy and understand well the challenges and constraints the market economy places on companies.

We also found that whereas managers of state enterprises being directly confronted with the increasing pressures of the emerging market economy on their enterprises and having to cope with its challenges, increasingly realize the necessity of change in order that their enterprises can survive, workers perceive change primarily as a threat. At the core of workers' resistance to change lies their large pervasive fear of unemployment. Thus, contrary to prevalent thinking, it is not managers but workers who resist to change most. These conclusions apply to all the BSEC countries. Differences from country to country are a matter of degree.

Therefore, in state and in these privatized enterprises which still receive subsidies from the state securing workers consensus is a sine-qua-non of successful change. In fact, managers in state enterprises have neither the institutional authority nor the effective power to implement changes against workers' will. Whether new policies or new ways of doing things will be successful or be carried out at all, has been shown to hinge largely upon whether both managers and workers can be persuaded to agree with the particular change and to cooperate for its successful implementation.

So what are the lessons for foreign managers and investors doing business in BSEC countries? First, they should spend time and effort to understand the values, priorities and fears of the individuals (potential partners, clients, suppliers, employees and public officials) with whom they are dealing; they should be mindful of how deeply certain attitudes may be ingrained; also, they should not overlook experience, skills and managerial behavior that can be built upon; and finally, they should expect to work hard and long at change before it occurs.

## **APPENDIX: Outline of Synthesis of Findings from All Sources of the Study**

*Barriers, factors and actions influencing the process and/or the outcome of changes of managerial practices in BSEC countries<sup>25</sup>.*

The insights listed below are presented in rough unsorted form because authors believe that before they can be fit into an integrated method to understand and deal with the problems of transition in BSEC countries, extensive additional qualitative research needs to be conducted.

- I. Macroeconomic problems and insights for effective transition of economy
  - A. Problems
    1. The collapse of the Soviet empire resulted in the breakdown of traditional external markets (suppliers and customers) and of the financial reliability of local clients
    2. Sluggishness of the process of change had always been one of the main weaknesses of the socialist system
    3. The change-averse role of Trade Unions
    4. Insufficiency, and unsuitability of Soviet era legal framework for market-economy system
    5. No clear legal process for mortgages and/or for bankable guarantees for business and investment transactions
    6. Bureaucratic delays in issuing laws and decisions
    7. No coherent policy of protection of local industry from imports
    8. Monopolistic State Banks
    9. Monopolistic suppliers of goods and services
    10. Stifling taxation systems incompatible with market economy
    11. Essential infrastructure not operative as still functioning as socialist state enterprises (transportation, communications etc.)
    12. Problems created by monumental change aspired to convert macroeconomic system from plan to market and by the social consequences of this change

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<sup>25</sup> Statements made by managers interviewed are placed in quotation marks.

13. Conflict between government officials and managers of enterprises
14. Interference in the management of a state enterprise by superior government authorities
15. " Ministries are still rigid and uncooperative and complicated to deal with "
16. Slow and non-transparent decision making process
17. Lack of experience in privatization at all levels
18. High cost of social factor is confusing aims of change
19. Poor economic situation of customers prevents normal function of market
20. Supervising authorities are still main initiators of whatever changes occur
21. Supervising authority inexperienced and indifferent to implications of transition to the survival of enterprises
22. Perennial shortage of all inputs including liquid capital, cripples the effort transformation of managerial behavior in state enterprises
23. Shortage of convertible currency exacerbates the need for foreign investments
24. Extreme shortage and exorbitant cost of capital
25. High inflation
26. Changes usually cost money which is not available to enterprises
27. Overhang of heavy old end new debts among enterprises exacerbate liquidity crunch

B. Insights for effective transition

1. Holistic, global aspect of the process of change (interdependence of factors)
2. Demand in a competitive market serves as the most effective propeller of change in enterprises
3. Transformation of political and economic environment from central plan to market gradually for the new outlook and a business mentality

4. Importance of realistic “evaluation” methods of local assets for joint venture agreements
5. Application of many alternative forms and methods of privatization
6. Support of changes (incentives, financing, know-how, training, monitoring) requires commitment of the state bureaucracies
7. Study by foreign investors of local macroeconomic conditions, culture, mentality and relevant institutions
8. Monitoring degree and problems of the implementation process of each change

## II. Internal structural enterprise logistic reasons

### A. Problems

1. Failure to change has become reason for management to have to step down
2. Erosion of qualified personnel of state enterprises to better paying private sector
3. Shortage of qualified personnel to implement and to handle change
4. Varying and conflicting interests of workers
5. “Speculating” about the privatization process causes uncertainty and fear of new owners' priorities
6. Top management is too absorbed by daily routine and power struggle problems to have time to address strategic issues
7. Power of top management limited by resistance of middle and lower echelons
8. Difference between private and/or privatized small businesses and state enterprises in ability to change (small companies are change easier)
9. Stubborn inertia of old structures
10. Complicated organizational structures of many hierarchical levels



11. Lack of incentives to stakeholders to change
12. Heavy accumulated debt of enterprises
13. Western capital is very difficult to attract and to absorb effectively
14. Positive changes can also have unforeseen negative side-effects
15. In many cases workers back their managers in maneuvers to avoid change fearing that it will threaten their jobs
16. Low awareness of high quality
17. Favoritism at all levels of hierarchies
18. Lack of feeling of responsibility to get work done quickly and properly
19. Change for the sake of change
20. Reluctance to assume risk of change
21. Lack of up-to-date information and know-how
22. Problems in internal enterprise communication because information still considered as power
23. Ignorance of local structures, cultures and values by western investors
24. Physical strain on managers ill equipped to cope with the distinctive problems of competitive markets

B. Guidelines

1. Clarity of vision and of direction
2. Major incentives for change are:
  - a) Competition as initiator of change
  - b) Recognized need of enterprise for self preservation survival
  - c) Financial interest of management and workers (profitability, rewards)
3. Division of enterprises into smaller financially independent units
4. Consideration of the “holistic aspect”
5. Importance of suitable committed foreign partner
6. Importance of study and correct reading of market
7. Demote people who resist

8. Importance of networking with authorities
9. Before calling for outside experts prepare enterprise: first rally for change and bring outside experts only when the atmosphere is right
10. Get good local and foreign consultants
11. Organize personnel training and establish permanent relations with the technical high schools and colleges.
12. Interdepartmental coordination
13. Turning the workers of an enterprise into owners (stock distribution or options) was originally envisaged as a core way to motivate workers. In some cases workers were pacified, not because this acted as a motive for harder work, but because erroneously they thought that being stockholders, they cannot be dismissed
14. Decrease span of CEO's control
15. Make stakeholders realize there is no way back to the old system
16. Implement the changes required, step by step
17. Substitute gradually the old management/leadership from within, with new qualified management which is supportive of change
18. Lease some production units to foreign companies
19. Focus on profitability
20. Introduce an acceptable process for layoffs
21. Introduce clear uncomplicated, transparent and reasonable process for management buyout
22. Introduce profit sharing as an incentive
23. Introduce performance evaluation
24. Joint ventures help you to enter foreign markets
25. Improve internal communications by " liberating " information

### III. Enterprise Internal Structural Human Aspect Factors

#### A. Problems

1. Attitude of people towards change
  - a) Attitude of top managers

- b) Attitude of middle managers
  - c) Attitude of workers
  - d) Attitude of workers collectives (WRC)
2. The overwhelming majority of companies studied, are judged by researchers to be "change friendly"
  3. WRC's power in privatized enterprises seems smaller than in state enterprises
  4. Psychological problems and aspects (feelings of intimidation, uncertainty)
  5. The social factor
  6. Persistent values of the old system i.e. egalitarianism, collectivism, etc.
  7. Resistance and ability of middle and low management to thwart change
  8. Changes seem as "unnecessary extravaganza"
  9. Fears of workers of losing job and status
  10. Stereotypical thinking
  11. Managers older than 50 years old, usually do not get involved in change
  12. Lack of systematic approach
  13. Lack of identification with the enterprise

#### B. Guidelines

1. Use the expertise of eastern managers
2. Explain and convince workers (address fears and mistrust)
3. Create a *Special Department of Staff* which finds jobs for people dismissed
4. Create a reward system for those with innovative ideas
5. Compromise. Fire and hire reasonably, avoid rigidity in changes
6. Redistribute authority among middle and lower managers
7. The most effective means to achieve change is to involve all people affected by it. Suggested steps:
  - a) Set realistic goals
  - b) Explain need for change

- c) Motivate stakeholders
  - d) Require and evaluate performance
  - e) Train
  - f) Support involvement
  - g) Be patient but persevere as well
8. Harmonize priorities between stakeholders
  9. Establish a new personnel policy and a new wage system with wage categories, where every employee can see and affect his carrier path
  10. Establish own *Training Center*
  11. Replace unsuitable and unwilling personnel including managers
  12. Build a clear vision
  13. Create *Innovation Teams*

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