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**Entrepreneurship and  
Proprietorship in Transition:**

**Policy Implications for the Small-  
and Medium-Size Enterprise Sector**

Richard Scase

**Working Papers No. 193**

**August 2000**

UNU World Institute for  
Development Economics Research  
(UNU/WIDER)

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# **Entrepreneurship and Proprietorship in Transition**

Policy Implications for the Small- and Medium-Size  
Enterprise Sector

**Richard Scase**

August 2000

This study has been prepared within the UNU/WIDER project on Small and Medium Enterprises in Transition: How Does Entrepreneurship Develop in Post-Socialist States (Transition from Below: The Role of the New Private Sector), which is directed by Professor Robert J. McIntyre, UNDP Regional Bureau for Europe and the CIS, Bratislava, Slovak Republic.

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Camera-ready typescript prepared by Janis Vehmaan-Kreula at UNU/WIDER  
Printed at Pikapaino Paatelainen Oy, Helsinki

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ISSN 0782-8233  
ISBN 952-455-001-6 (printed publication)  
ISBN 952-455-002-4 (internet publication)



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## ABSTRACT

In this paper, the role of small and medium size enterprises in the economic transformation of the countries of Central Europe is assessed. It argues that although these fulfil an important role, they are less significant as agents of macroeconomic transformation than the re-structuring of large-scale corporations, often acting as joint ventures with foreign companies. The paper begins by making a distinction between entrepreneurship and business proprietorship. Drawing upon the ideas of the German philosopher Max Weber, it defines the former in terms of the capitalist's commitment to sustained accumulation such that personal consumption is sacrificed. With proprietorship, on the other hand, the ownership of assets is used for trading purposes to generate revenues which are then used primarily for personal consumption. Within the context of present economic uncertainties in Central Europe, together with the personal experiences encountered under the former state socialist regimes, motives of proprietorship rather than those of entrepreneurship are more likely to prevail. Despite this, the role of small businesses is important since it sustains an ideology of the free market, one in which there are opportunities for personal business proprietorship. It also sustains free market ideals in that consumer choice is extended through the generation of a thriving small business sector. Even so, the structural features of the economies of the former state socialist regimes are being shaped to a greater extent by the strategies and actions of large corporations. As part of this discussion, the personal biographical experiences likely to encourage agents to set up their own small businesses are identified.

## 1. THE SOCIO-ECONOMIC CONTEXT

It is now ten years since the fall of the Berlin wall that was followed by the collapse of the state socialist regimes of Central Europe. From the relatively uniform socio-economic structures of these, diversities have emerged both *within* and *between* these different countries. These are reflected in all spheres of social, economic and political activity. These range from the role of political parties, pressure groups and local and national government administrative structures to economic production and patterns of trading. Many of these differences between countries reflect variations in the ideologies of governing regimes, the stability of elected governments and the continuing impact of the earlier state socialist regimes. Other contrasts are the function of diversities in levels of economic development and of patterns of industrialization and how these have shaped the formation of occupational structures, institutional orders and cultural systems. But among these, one of the major factors that has shaped differences has been the role of the state; particularly in terms of its involvement in, and governance of, economic activity. There are a number of cross-national contrasts (Vickerstaff *et al.* 1998).

As noted in other contributions to this project<sup>1</sup> the approaches taken to privatization have been varied in speed, impact and the extent to which foreign actors have been involved. In the Czech Republic, for example, it has been more extensive and rapid than in Bulgaria or Slovakia. By the mid 1990s large sectors of manufacturing were privatized in Hungary and the Czech Republic but such programmes were not fully implemented or 'speeded up' until later in Poland, Russia, Bulgaria and Romania.

Associated with this, there has been the adoption of different privatization methodologies in the different countries. The issue of vouchers to the public has been a common pattern, but in some countries approaches have been adopted which allow extensive intervention of foreign corporations and even 'take over' of state owned economic enterprises (SOE) or co-operation in joint-ventures. The outcome of these different patterns has been reflected in the strategic and operational activities of companies. Post-socialist enterprises with high levels of foreign intervention, either through direct ownership or through collaborative ventures have been at the

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<sup>1</sup> Papers presented at the UNU/WIDER Project on Small and Medium Enterprises in Transition: How Does Entrepreneurship Develop in Post-Socialist States, held in Helsinki, Finland on 18-19 June 1999.

forefront of organizational re-structuring, shedding large amounts of 'surplus' labour, affecting local and national employment levels (Vickerstaff *et al.* 1998). They have had a greater capability to invest in new technologies and to develop new product portfolios for re-focused market opportunities. For instance, Volkswagen's purchase of a state-owned car manufacturing facility in Bratislava in Slovakia has led to a process of total enterprise re-structuring. Virtually the whole of the pre-1989 labour force has been replaced by younger employees with no experience of 'socialist' work practices, the technology has been completely revamped and the operating plant fully integrated into Volkswagen's global operations (Vickerstaff *et al.* 1998).

On the other hand, when companies have been privatized through employee share ownership participation schemes (ESOPS), there has been less organizational and technological re-structuring. Equally, in these enterprises, traditional 'socialist' management cultures have often persisted as well as 'socialist' working practices. This is particularly the case in many of the larger 'privatized' enterprises of Russia, Slovakia, Bulgaria and Romania. The vested interests of the earlier socialist regimes have been able to continue as the principal stakeholders and as the prime beneficiaries of economic activity. Behind a rhetoric of 'free enterprise', 'the market' and Harvard Business School – inspired 'best management practices', enterprise directors have so far, been able to 'hang on to the past'. This has also served the interests of other employees in these enterprises since they have often avoided redundancy, the loss of their housing benefits and other work-related privileges. It is only during the past few years that the impact of market forces is compelling management in these indigenously-owned enterprises to re-structure their operations, often forcing them to invite foreign ownership participation or to seek the advice of foreign-based consultants.

Organizational re-structuring, associated with processes of privatization, has also varied both within and between countries. In some, there has been the rapid shedding of non-economic activities such as the provision of pre-school facilities for employees' children, housing and other welfare functions, while in others, these have been retained. In Russia, the continuing role of enterprises in providing catering, medical and social facilities has allowed for the continuing non-payment of wages more acceptable and probably reduced the potential for more widespread social unrest. But further than this, there have been differences in how companies have embarked upon re-structuring their core economic activities. This has had ramifications for the formation and growth of small firms. In some,



there has been the outsourcing of various functions with a shift towards creating 'leaner' and 'flatter' structures. In line with this, have been the attempts to de-centralize structures through the setting-up of strategic business units, devolved budget and cost centres and other 'fashionable' organizational forms much emphasized by western-based management consultants.

The outcome for economic efficiencies of these management modernization efforts has often been less than expected because of the inadequate strategic skills and the cultures of management that prevailed under the former state socialist regimes. Only now, ten years after macro-economic and political reforms have been implemented, are enterprise managers acquiring the appropriate skills to manage effectively in new market-driven circumstances. Again, there are striking differences between countries with Hungary, the Czech Republic and sectors of the Polish economy at the forefront. Large parts of manufacturing industry in Russia, Bulgaria, Romania and Slovakia continue to adhere to organizational forms characterized by centralized, bureaucratic structures. It is in the foreign-owned subsidiaries and in the joint ventures with western companies that organizational re-structuring has been most pronounced, with the majority imitating the 'best-practices' of German and United States companies (Whitley *et al.* 1996).

These contrasting business environments provide the context for understanding the role of small firms in the former state socialist economies of Russia and Central Europe. In some of these, small firms have emerged 'independently' and operated in parallel with larger enterprises while in others they are the direct outcome of the internal re-structuring programmes of large enterprises. It is the outsourcing of what were previously 'in-house' functions that have offered opportunities for business start-up. Yet in other conditions, where institutional or regulatory orders have lapsed or even broken down, there has been the emergence of widespread 'illegal' entrepreneurship, based upon cash trading and organized crime. The Mafia in Russia is the best known example of this. Despite its illegitimacy, it fulfils a key role in trading relations meeting personal 'basic' consumption needs that may otherwise be conducive to social disorder among some sectors of the population.

## 2. THE UNRELIABILITY OF DATA

Our understanding of the role of small firms in the former socialist economies of Russia and Central Europe is less than satisfactory because of a range of factors. Under the old regimes, small-scale trading was extensive, particularly in economies such as those of Poland, Hungary, Yugoslavia and the Central Asian Republics.

But there are no reliable data since, although this was recognized as an important mechanism for sustaining economic activity – often in small towns and rural areas – it was considered to be 'illegal' and often according to party activists' interpretations of Marx, a legacy of an earlier pre-socialist era. The official orthodoxy was that such economic activity would evaporate as these societies evolved into a 'higher level' and more mature condition of socialism. However, there are no reliable data as to how widespread and important these patterns of trading were within these state socialist countries.

Equally, the introduction of macroeconomic and political reforms in the 1990s, intended to generate favourable conditions for the growth of 'liberal' market economies has led to the emergence of both 'informal' as well as 'formal' patterns of trading and exchange relationships. The patterns are not visibly measurable since they often constitute a key component of the subterranean, non-declared, 'non-taxable' economy (Acs and Audretsch 1993). Anecdotal evidence would suggest, however, that it has pronounced significance in large sectors of these emerging market economies in not only 'low-skill', traditional spheres but even in the provision of professional and technical services. Those with expert skills of one kind or another combine their full-time employment as enterprise directors or state officials with the sale of their professional services to clients, often trading from their place of 'formal' employment. Indeed, it often goes further than this with these employees using the tangible assets of their employing organizations for trading purposes and hence, personal gain. A more indirect method is for such employees to encourage family members to set-up 'independent' businesses through which corporate and institutional cash flows can be diverted. Some examples of these could be travel agencies or catering firms to which employees in senior institutional or enterprise positions will direct 'profitable' business. Such tactics, of course, are also very common in many developing countries.

The unreliability of data is confounded by the fact that commitment to the introduction of market reforms, together with the rejection of state socialist

ideologies can lead to an *overstatement* as to the scope and extent of entrepreneurship. Even those who continue to be employed as state officials are likely to claim that they are associated with entrepreneurial ventures when closer enquiry suggest that this is not the case. In order to demonstrate their commitment to post-socialist values and their rejection of past socialist ideals they will refer to their involvement in 'start-up', spare-time entrepreneurial ventures. Combining this with various illegal and informal forms of entrepreneurship means that any estimates of the *real* significance of entrepreneurship and small business ownership are likely to be extremely unreliable (Vickerstaff *et al.* 1998).

### 3. ENTREPRENEURSHIP AND PROPRIETORSHIP

In any analysis of the role of small firms in Russia and the post-socialist countries of Central Europe, it is necessary to make a distinction between *entrepreneurship* and *proprietorship*. This is important from not only a conceptual point-of-view but also because it has important implications for policies aiming at encouraging both business start-ups as well as for those directed to stimulating the growth of existing small business. Each refers to *contrasting psychologies of founder-owners*, their *attitudes towards trading* and their *orientation to capital accumulation*. Essentially, entrepreneurship refers to a person's commitment to wealth creation, capital accumulation and to business *growth*. The classical entrepreneur, therefore, invests his or her money (M) into a productive activity which, whatever the product or service, realizes a higher end value (M + 1) than the initial capital invested. This is then re-invested (M1 → M2 → M3) to sustain a dynamic of capital accumulation (Marx 1976).

It is in the pursuit of this aim of capital accumulation and long-term growth that the entrepreneur foregoes personal consumption and who regularly if not constantly searches out market opportunities in which the dynamic of capital accumulation can be implemented. This inevitably entails taking risks and coping with uncertainty but underpinning this need for *calculative decision-making* is the motive for sustaining business growth since without this there will be no capital accumulation. Needless to say, the forms that this may take can be varied ranging from the setting-up of distinct business ventures within different market niches (in order to reduce dependency upon trading fluctuations), to organic growth, to 'squeezing' as much profit as possible from an ongoing venture. But in one way or another, the motive

of entrepreneurship is 'rational' decision-making in relation to changing market opportunities (Scase and Goffee 1982).

With proprietorship on the other hand, the motives are quite different. Essentially, this refers simply to the ownership of property and other assets. These may be used for personal enjoyment, consumption or trading. If the latter, they are exploited to realize profit and personal gain but what distinguishes proprietorship from entrepreneurship is that the ownership of these capital assets, whether property, technology or even human skills, are not utilized for the purposes of long-term capital accumulation. Instead, *any economic surpluses generated from trading are likely to be consumed and utilized to sustain a specified standard of living and style of life rather than re-invested in the business*. In other words, capital accumulation through business growth is *not* the prime motive of business proprietorship. Consequently, the formulation of policies to encourage business growth among proprietors is likely to have limited success since this is not a key personal motive (Scase and Goffee 1982).

Within the emerging markets of Russia and the economies of Central Europe, it is *proprietorship* rather than *entrepreneurship* that best describes the greater proportion of small business traders. Indeed, in many economic sectors entrepreneurship is undoubtedly the exception. It is for this reason that the small business owners do not constitute a viable force for rejuvenating the growth of these economies. Although they are real features of these systems they are relatively unimportant in providing the capabilities for sustained macro-economic growth. They may offer jobs and provide earnings (legal or otherwise) that are numerically significant in, for example, the service and retail sectors. In this sense they fulfil a key function which may be very important in sustaining social stability. But the emerging strata of small business *proprietors* in these economies appear, so far, to be incapable of constituting an *indigenous* force for macro-economic development. What appears to be emerging in these economies, are strata of proprietors who carve out niches for themselves, in relation to which they are able to sustain levels of trading which allow them to *survive* rather than to *grow* in the manner of ideal-type entrepreneurs who are committed to profit, re-investment and capital accumulation (Scase 1997).

These motives for business proprietorship are often rooted in personal past experiences of state socialism; that is, the quest for personal autonomy. The carving out of market niches is in order to allow this to occur. Under state socialism, there was limited capacity for personal autonomy except for small circles of artists and other cultural workers. There were extensive

bureaucratic controls that regulated all spheres of life, ranging from employment to housing accommodation and personal recreation and leisure patterns. These were often reinforced by tight networks of inter-personal relations that cut across institutional orders, incorporating employment and housing opportunities. In these circumstances, those in authority could exercise control over others who had little capability or recourse for redress.

In the post-socialist conditions of the 1990s, business proprietorship offers for those who were subject to these control mechanisms the capacity to carve out personal autonomy so that they are economically and socially 'free' from the control of others. Indeed, even under state socialism, informal patterns of trading were not only the mechanisms for acquiring additional economic resources, of which a prized element was foreign currency, but also the means according to which individuals could express a certain degree of psychological independence and personal autonomy.

Hence, in any analysis of small businesses in Central Europe it is important to recognize the conceptual and empirical distinctions between entrepreneurial activity on the one hand and small-scale business proprietorship on the other. It would appear to be the latter that are expanding rapidly as increasing numbers of individuals seek to protect themselves from the risks and uncertainties of the newly-emerging market economies (Acs and Audretsch 1993). Proprietorship is perceived to offer a vehicle for cash flow and a hedge against the risks of lay-off and unemployment brought about by enterprise re-structuring driven, as is often the case, by the injection of foreign capital through take-overs and joint ventures, or by the requirements of the IMF and other international agencies for structural reforms. It is for this reason that the growth of the small business sector in post state-socialist countries offers little potential for providing a springboard for entrepreneurial ventures that will create sufficient new jobs and develop innovative products and services which, in turn, can have a significant and substantial effect for generating indigenous, self-sustaining national economic growth (Arzeni 1996). Rather, the growth of the small business sector in these economies is generating strata of proprietors which do, indeed, create some jobs but generally which are established for the purposes of creating cash flow that can be used for sustaining living standards and personal patterns of consumption. The likely outcome is that small businesses will, at best, constitute sectors within market economies that will be *dominated* by large-scale corporations and increasingly *dependent* upon the global investment

strategies of multi-national corporations and the policies of international investment institutions (Whitley 1992).

#### 4. ENTREPRENEURSHIP AND BOOTY CAPITALISM

If these factors account for the motives underlying a greater proportion of small business start-up in Central Europe, it is evident that even those who are committed to entrepreneurship are likely to be motivated by the desire for short-term financial gain rather than longer term, capital accumulation. They represent a form of what Max Weber describes as 'booty capitalism', meaning economic activities that are pursued in a 'haphazard' and often non-rational way for the purposes of personal gain (Weber 1947). He makes a clear distinction between those driven by these motives and those who are dedicated to savings, investment and capital growth in a systematic, sustainable and pre-meditated fashion. Weber draws a further distinction between profit acquired through *trading* (where the rewards of which are consumed) and the profit obtained as a consequence of *investment* in production (where the rewards of which are re-invested for further accumulation). For Weber, the entrepreneur is first and foremost a miser since personal consumption is sacrificed for the longer term goal of expanding the scale of the entrepreneur's activities (Weber 1976).

The limited evidence on small-scale business start-up in Russia and Central Europe suggests that few business owners have a serious commitment to long term capital accumulation. Equally, there appears little to support the Weberian view that entrepreneurship (not proprietorship) is related to the sacrifice of personal consumption. Instead, any processes that may be identified as entrepreneurship appears to have close similarities with what Weber describes as 'booty capitalism'. Many of these ventures are associated with their owners' attachments to large organizations through their jobs or personal networks through family members or spouses. Trading activities between the employing organization and its customers or suppliers or 'diverted' or channelled through such enterprises. Indeed, this is often the motive for 'start-up'. Businesses of this type are nothing more than 'buying and selling' agencies whereby the proprietors are able to 'siphon' a percentage of their employers' sales or revenues.

In their most extreme form, of course, these businesses can be illegal in their nature and are incorporated within broader 'illicit' networks of trading.

The outcome is 'Mafia' – based businesses, established upon complex patterns of reciprocity, the enforcement of which are maintained by a variety of illegal sanctions. In many ways, these business ventures reflect a legacy of the 'network' trading patterns that operated within the former state-socialist regimes. Accordingly, some of these present-day market-based networks are functional for the distribution of goods and services in economic sectors where structural reforms have created shortages or breakdowns in supply chains (Struthers *et al.* 1996).

In all of the economies of Central Europe in the early 1990s, there were widespread attempts by managers – directly or through intermediaries – to set up trading links with foreign partners in order to obtain hard currency. This was then used to purchase personal consumer products so that the 'good life' of western societies could be enjoyed. If, then, there were personal motives underpinning the setting-up of small business ventures these were more related to *trading* than *production* and for the purposes of acquiring resources that could be *consumed* rather than re-invested in *productive* business growth (Aris 1998).

To the extent that these observations have any systematic empirical substance, the new entrepreneurs of Russia and Central Europe would seem incapable of bringing about a fundamental change in the ideological and the economic structures of these countries. As such, it would be optimistic to regard them as a force of *indigenous* economic transformation. This must surely be the starting point for any systematic analysis of these emerging market economies particularly since *entrepreneurs* probably constitute only a very low proportion of small business *proprietors*. Instead, it is highly likely that this sector has little commitment to setting up enterprises for longer-term capital accumulation rather than short-term personal gain. Who, then, are these proprietors?

## **5. WHO ARE THE SMALL BUSINESS PROPRIETORS?**

There are a number of factors that will attract individuals to small business proprietorship. There will be both 'push' and 'pull' factors; for example, the threat or experience of unemployment and the identification, perhaps on a day-to-day basis, of opportunities for setting up a trading venture to generate cash flow. There will also be a range of biographical and structural forces that will be significant. Among the former, may be family

traditions (in the pre-socialist era) while the latter may include trading opportunities generated by macro-economic and political reforms.

An obvious category of potential proprietors are those who, because of their work situation, handle cash within the context of face-to-face relations with customers. These are likely to be those working in service occupations in the hotel, catering and retail sectors. Under the old regimes, workers engaged in these spheres often acquired business skills that they are now able to exploit in a more explicit and legitimate manner. Bar tenders, waiters, hotel porters, taxi drivers, cleaners, shop assistants and others were able to acquire foreign currency and often other material resources which they could use as 'exchange' for the purchase of various consumer products. There are countless anecdotal examples of how much resources could be obtained. A frequently cited case is that of bar tenders who would 'thicken' the line that denoted the 'measure' on a spirit glass. By serving to the bottom of the line with each customer order, enough spirits could be saved over a period of time that could then be used for illegal exchange purposes. Many of those engaged in such occupations were able to accumulate sufficient financial reserves so that they could buy or lease their own bars, small restaurants and shops during the 'first waves' of mass privatization in the early 1990s.

For them, the setting up of business ventures was fairly easy since they needed to obtain little in the form of financing and they already possessed the necessary human, social and technical capital for trading with customers. Even so, these pre-transition asset accumulations have not protected large numbers of them from the threat of insolvency; except in cases where their trading has been 'underwritten' by state subventions, contracts with large enterprises or their incorporation within reciprocal trading networks. Many of them encounter difficulties in managing competition – the dynamics of which they do not completely understand – while others encounter problems with managing cash flow in order to sustain satisfactory profit margins. In common with their counterparts in more mature market economies, they often find it easier to trade with their personal skills than to generate profitable returns from the utilization of fixed and variable assets, of which their own human capital is but a single factor.

Others experience problems because of the need to raise loans for buying their trading outlets from their previous state owners. These debts have to be serviced and often the financial returns are low. In some cases, the opportunities for personal gain were greater under the old regimes when



they were trading either informally or illicitly. Then, no taxes needed to be paid and trading activities were not subject to regulation and various state-imposed changes such as social insurance cover for any employees.

Even so, the appearance of these strata of small traders in the service sectors of the different economies of Central Europe does have an important *symbolic* impact. The *appearance* of shops, restaurants and bars under various forms of private ownership, displaying an increased variety of goods and services is material evidence of the transformations of previously highly centralized state-owned economies. Hence, they fulfil a key *ideological function* in the transition process. They demonstrate the 'freedom', the 'opportunity' and the 'choices' available in post-socialist, market-based economies. The appearance of large numbers of small businesses highlights the transition to a market economy and with this, the opportunity for citizens to be not only consumers but *customers* who are able to *choose* from a *variety* of outlets for their purchase of personal goods and services. In this sense, small trading firms may be regarded as *ideologically* or *symbolically* more important than the privatization of large enterprises. They represent a legitimization of the market economy, linked to the fact that much of the widespread dissatisfaction towards the former state socialist regimes was directed towards the process of the *distribution* of goods and services rather than to the work regimes according to which these were *produced*. It was weaknesses in the processes of distribution and consumption and with this, the lack of variety and diversity of goods and services that were major sources of widespread popular protest (Blackburn 1991).

A further category of business proprietors are those former state bureaucrats who occupied positions that enabled them to develop extensive personal networks both at home and abroad. After the collapse of the old regimes they were able to utilize these for trading purposes, especially for the import and export of various goods and services. The former state socialist planning processes consisted of ministries for different sectors of the economies which set output targets for enterprises or groupings of enterprises (combines, *kombinate* or *obyedinenyia*).

In order for these production targets to be met, a complex and elaborate *informal system of 'plan bargaining' and negotiation emerged* and played a large role in both the plan formulation and plan execution stages. To achieve their plan targets it was often necessary for senior and middle managers to barter for various components, pieces of equipment and other necessary resources. Without these supplementary resources officially

determined plans could not be achieved. The immediate income (salary and performance-based bonus) as well as career reputation and promotion prospects were determined by success in this undertaking. In extreme cases they might even lose their managerial positions.

These enterprise directors have been able to take advantage of privatization programmes and to exploit their extensive personal networks for realizing personal gain through emerging market opportunities. They have often played a key role in the 'break-up' of state-owned enterprises, often purchasing segments of cash flow at relatively cheap prices for the purposes of starting up their own business ventures. Further, they have often been able to do this through their access to financial resources because of their personal contacts with various branches of the state banking system (Thirkell *et al.* 1997).

There are others who are setting up their own businesses because, despite a long period of state socialism, entrepreneurial and proprietorial traditions persist within their families. There are urban and rural populations in Eastern Europe who, to a greater extent than in Russia, have always subscribed to proprietorial values. Many of these were the small-scale traders who had their assets expropriated in the late 1940s. Equally, there are members of peasant families where entrepreneurial and proprietorial values have continued to be highly significant in shaping attitudes and behaviour. In Poland, this tradition was accepted by the former state regime by allowing a peasant-based co-operative movement to survive. Indeed, it was the younger, educated children of peasant families who emigrated to the United States, some of who have become wealthy entrepreneurs and subsequently returned to Eastern Europe to be significant investors in business ventures.

There are also those who have acquired skills through trading within the 'informal' economies of the earlier state socialist regimes, so that they possess the necessary resources for business start-up. Under some of the old regimes there were large numbers of state employees who had 'second-jobs' according to which they were able to supplement their earnings as for example, in Hungary (Burawoy and Lukacs 1992). The activities undertaken within these gave them the necessary competencies – such as, for example, negotiation skills and the ability to obtain financial resources for business start-up. These informal economies, consisting of people pursuing various 'illicit' trading practices of one kind or another, were a source of social stability under the conditions of state socialism and continued to play that same role in the emerging market economies of the

1990s. They provide opportunities for personal gain for those who would otherwise be economically and socially marginalized.

While the informal economy constitutes an important sphere for small business start-ups, so, too, does the restructuring of large-scale state enterprises and the more formalized mechanisms of privatization associated with the introduction of market reforms. Many large enterprises have restructured through divesting themselves of a whole range of 'in-house' activities. Traditionally, the enterprise under state socialism provided social, welfare, educational and recreational facilities. With economic restructuring many of these functions have been sold off through management and employee buy-outs. These have enabled individuals to set-up businesses, established on the basis of going concerns to sell back various services to their previous employers. Often, as in Russia and Poland, this has occurred within the context of leasing arrangements, whereby employees lease facilities and resources from large enterprises and then sell back products to these same enterprises. It is in these processes of so-called 'outsourcing' that the valuation of state assets for the purpose of selling them to enterprise managers and other employees has often been subject to considerable dispute (Thirkell *et al.* 1997).

## **6. THE ROLE OF SMALL FIRMS**

The discussion above outlines the main factors that account for the widespread growth of small businesses in Eastern Europe. But what is their role in the newly emerging market conditions of the 1990s? First, as stated earlier, they offer *variety* in the provision of consumer goods and services. Second, they offer job opportunities for both proprietors and their staff who might otherwise be unemployed. Third, the persistence of an informal economy consisting of small-scale petty traders enables those who would otherwise be economically marginalized to obtain a more satisfactory level of earnings (Scase and Goffee 1987). Accordingly, the small business sector in Eastern Europe has many of the material and ideological functions of its counterpart in any western economy. Entrepreneurship and business proprietorship, therefore, offers vehicles whereby those who are economically disadvantaged are able to overcome or to compensate for this through small scale trading. Fourth, small businesses in Eastern Europe – in a similar manner as in mature market economies – are functional to the needs of larger scale enterprises.

Through processes of outsourcing, many small businesses in Eastern Europe offer services to larger companies that enable the latter to have lower operating costs and therefore, to remain competitive in national and international markets. But, as subcontractors to larger enterprises they are highly vulnerable to shifts in the economic fortunes of these larger businesses and, as such, they often lack the trading independence necessary for longer-term growth. Indeed, the role of small businesses in Central Europe is vital but nevertheless vicarious within the overall processes of national economic renewal. In general, it consists of a stratum of entrepreneurs, small-scale traders and business proprietors who have carved out niches for themselves within emerging market relations so that they are able to obtain 'satisfactory' levels of living. As such, they do fulfil important ideological functions since their existence reaffirms 'the openness' of market relations and the *promise* of personal success through trading in societies that, under state socialism, had generally abolished such opportunities. In this sense, the growth of small businesses illustrates the 'freedom' of the market as opposed to the 'totalitarianism' of the previous regimes.

## 7. THE NEED FOR RESEARCH

There is clearly a need to document the processes of small business start-up and growth in the various countries of Central Europe. Undoubtedly there is a need for comparative research both within and between countries. It would be surprising, for example, if there were not important differences between Romania, Hungary and Poland, bearing in mind the sharp contrasts in the 'forms' of state socialism they experienced (Acs and Audretsch 1993). Equally, the dynamics of business start-up are likely to differ between economic sectors. The processes of setting up trading ventures in the creative industries (advertising, public relations, marketing and sales) are different to those in small-scale engineering and agriculture-associated activities. Similarly, those starting-up high-tech or biotechnology businesses need to trade in very different market environments than those who are operating trading ventures in domestic-orientated, low-skill product and service markets. Funding requirements are often different and very contrasting management styles and leadership skills are needed. These demands raise questions about nurturing employee commitment, upon which the success of any small-scale business is dependent.

How are mechanisms of employee commitment established and how is employer legitimacy enforced? Issues of managerial control, in whatever economic sector, are of considerable importance in employment conditions where traditional forms of authority associated with state ownership and control have been either drastically curtailed or abandoned (Ruzicka 1996). It is a major policy challenge to cultivate a new culture of 'trust relations' within small firms. If the culture of organizations under the old regimes encouraged employee compliance and rule adherence, such patterns of behaviour are often detrimental to the trading success of small businesses under the new conditions. New psychological contracts between employers and employees have to be negotiated so that innovation and creativity are encouraged rather than played down. This, of course, is not simply a post-socialist challenge; it is inherent in all forms of economic organization. But it is only through the systematic and detailed analysis of small firms that the dynamics associated with these processes can be documented and understood. It requires the use of case studies rather than of sample surveys. Whereas the latter can generate 'superficial' data, the validity of which is highly questionable, especially under conditions in which both policy and institutions are changing rapidly. Under these, case studies are much more satisfactory since they enable actual internal organizational processes to be observed. Unfortunately, there are acute problems of obtaining access to appropriate research situations and when this is granted, there are issues of representativeness and generalization. But certainly there needs to be a shift away from quantitative to qualitative modes of analysis if our understanding of small firm formation and growth in Central Europe is to be enhanced. Further, such studies, grounded in empirical observations, are likely to challenge many of the sweeping generalizations and assumptions of economic theories in terms of how business growth and market mechanisms operate (Sachs and Woo 1994).

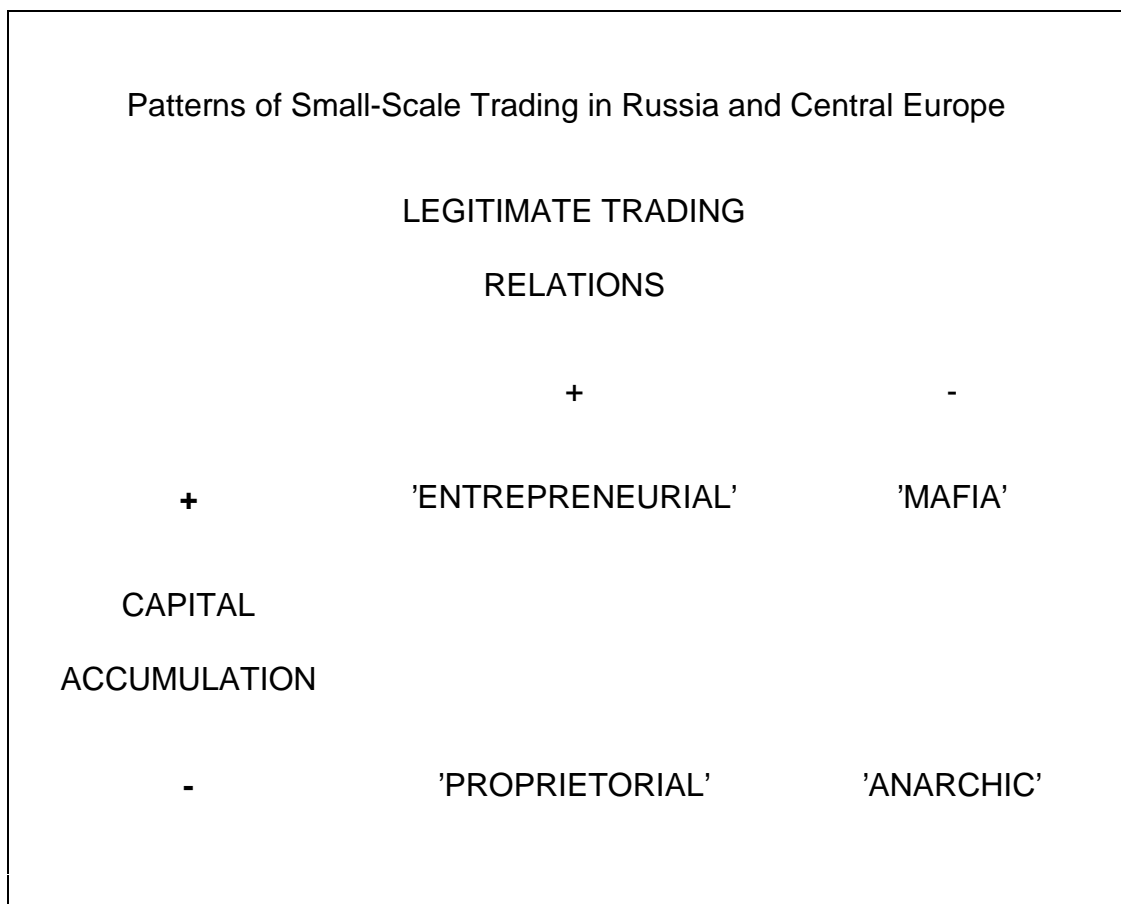
## **8. POLICY IMPLICATIONS**

From the preceding discussion it is evident that there are a series of policy implications for those developing business start-up programmes in Russia and the countries of Central Europe. It is clear that resources devoted to encouraging business growth among *proprietors* are probably misplaced. Available energies and resources need to be directed to those who are geared to *entrepreneurship* and therefore, personal long-term capital accumulation. But how are these two categories to be differentiated in

different empirical settings, particularly in view of the fact that it can be possible for there to be *personal* transitions between proprietorship and entrepreneurship? This is probably the most challenging issue for those responsible for encouraging 'grass roots' economic development in these emergent market economies.

At a conceptual level, it is possible to establish a suggestive, if imperfect typology of contrasting patterns of trading, based upon two differentiating axis. The first, represents the extent to which the motives for business trading are orientated to capital accumulation and the second, the extent to which these trading relations are either legitimate or illegitimate. The outcomes may be summarized as follows:

DIAGRAM 5.1



Entrepreneurial and proprietorial forms of business ownership have already been discussed. They are both legitimate forms of trading but they differ in their orientations to capital accumulation. With 'Mafia' businesses there is, indeed, a commitment to longer-term capital accumulation (largely through booty capitalism, opportunism, and adventurism) but it is essentially illegitimate and illegal. It differs from 'anarchic' forms of trading in that it is often highly organized and structured around to networks of rights and obligations. Commodities are exchanged through informal mechanisms of pricing with transactions conducted through bartering, services owed and cash (usually dollars). With 'anarchic' trading, there is little in the form of socio-economic organization beyond the boundaries of the household unit unlike the complex forms the Mafia can take. It is essentially 'individualistic', 'opportunist' and orientated to making, quite literally, 'a quick, fast buck'.

In any empirical situation, it is difficult to differentiate between these conceptual types. From a biographical point-of-view, there can be mobility from one category to another. Proprietors may become entrepreneurs and vice versa. Equally, those engaged in anarchic forms of trading are likely to become incorporated within the Mafia while those who are so connected may become expelled, forced to engage in illicit trading on their own. Even so, it is possible to suggest that there are *structural* forces such as the size and complexity of a political economy that are likely to encourage a preponderance of some forms of trading over others. Hence, the 'anomie' generated by the economic reforms in a geographically dispersed country such as Russia has encouraged 'Mafia' patterns of business whereas in Romania and Slovakia 'anarchic' forms are likely to be the more common illicit trading forms. At the same time, the more routinized and legitimate normative and institutional orders of the Czech Republic, Poland and Bulgaria (at present), are conducive to more legitimate entrepreneurial and proprietorial patterns.

It is clear that while the small business sectors of the economies of Russia and Central Europe do fulfil important material and ideological functions they seem to possess little in the form of *system transforming capacities*. In themselves, they appear to have little potential as vehicles for economic growth and for generating rational, capitalist forms of economic production because they overwhelmingly consist of *proprietors* rather than *entrepreneurs*. Even the latter are primarily orientated to short-term economic gain for personal consumption and support of a particular style of life rather than towards investment for longer term capital accumulation.

This is not to argue that there are no cases of successful entrepreneurial development to be found in the transitional economies. There are some individuals and small groups who already have and will continue to set up entrepreneurial ventures on the basis of the development of innovative products and services. There are, and will be, personal success stories emerging from this strata that will serve to legitimate the 'opportunities' available in the emerging economies of Central Europe. These will serve as role models to be emulated by others. Notwithstanding these 'exceptional' instances, small business proprietorship primarily offers opportunities for personal economic and psychological autonomy of a kind similar to that which characterizes the small business sectors of the mature capitalist economies.

For the longer term economic transformation of the economies of Russia and Central Europe, it is the processes of privatization and organizational restructuring of large-scale enterprises that offer pointers to the future nature and direction of these societies. It is these processes that will crucially determine both their economic and socio-political features. Within these developments, the role of small business sectors is certainly very real but alongside other processes of capital restructuring and institutional transformation, relatively unimportant.



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