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**The Business Challenges Of Entrepreneurship  
In Transition Economies**

**Abstract:**

Increase in globalization and internationalization in markets has created a complex business environment for all size firms in open market and also in transition economies. We see that there are more obstacles for entrepreneurs in transition. The purpose of this research is to examine the leading business constraints of entrepreneurship such as institutional environment and market (taxation and regulations, financing, policy instability, inflation, corruption, infrastructure, anti-competitive practice, marketing and managerial practices and bureaucracy) in transition economies. This study aims to integrate theoretical field with the empirical statistical data. The theoretical and empirical data were collected from literature and institutions based on statistical data, indexes and indicators to examine the business challenges. Therefore we use the global competitiveness index which is measuring nine pillars of competitiveness (institutions, infrastructure, macroeconomy, health and primary education, higher education and training, market efficiency, technological readiness, business sophistication and innovation). We also use governance indicator. We define governance broadly as the traditions and institutions by which authority in a country is exercised. This includes the process by which governments are selected, monitored and replaced; the capacity of the government to effectively formulate and implement sound policies; and the respect of citizens and the state for the institutions that govern economic and social interactions among them. The six dimensions of governance corresponding to this definition that we measure are: 1. *Voice and Accountability (VA)* – measuring perceptions of the extent to which a country's citizens are able to participate in selecting their government, as well as freedom of expression, freedom of association, and a free media. 2. *Political Stability and Absence of Violence*

(PV) – measuring perceptions of the likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including politically-motivated violence and terrorism. 3. *Government Effectiveness (GE)* – measuring perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies. 4. *Regulatory Quality (RQ)* – measuring perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development. 5. *Rule of Law (RL)* – measuring perceptions of the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence. 6. *Control of Corruption (CC)* – measuring perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capture" of the state by elites and private interests. BEEPS (Business Environment and Enterprise Performance Survey), CPI (Corruption Perception Index) and WBES (World Business Environmental Survey) will be used to examine challenges. The WBES team sought to accomplish the following objectives: To provide feed back from enterprises on the state of the private sector; To measure the quality of governance and public services including the extent of corruption; To provide better information on constraints to private sector growth, from the enterprise perspective; To sensitize client governments to the importance of listening to firms and using this information to critically assess policies; To establish the basis for internationally comparable indicators which can track changes in the business environment over time, thus allowing an assessment of the impact of market oriented reforms on private enterprises; To stimulate systematic public-private dialogue on business perceptions and the agenda for reform. By the help of those data we will determine the institutional environment, markets and organizational strategies for entrepreneurs in transition economies. As a conclusion we will make proposals for the entrepreneurs in the process of European integration.

**Keywords:** Entrepreneurship, Business Challenges, Transition Economies, Global Indicators

## 1.Introduction

As globalisation reshapes the international economic landscape and technological change creates greater uncertainty in the world economy, the dynamism of entrepreneurship is believed to be able to help to meet the new economic, social and

environmental challenges. Governments increasingly consider entrepreneurship and innovation to be the cornerstones of a competitive national economy, and in most countries entrepreneurship policies are in fact closely connected to innovation policies, with which they share many characteristics and challenges. Entrepreneurship is increasingly recognised as an important driver of economic growth, productivity, innovation and employment, and it is widely accepted as a key aspect of economic dynamism (Ahmad and Seymour, 2008). The purpose of this research is to examine the leading business constraints of entrepreneurship such as institutional environment and market (taxation and regulations, financing, policy instability, inflation, corruption, infrastructure, anti-competitive practice, marketing and managerial practices and bureaucracy) in transition economies. This study analysis *Transition Economies; CEE plus CIS. Central and Eastern (CEE):* Albania, Armenia, Bosnia and Herzegovina, Bulgaria, Croatia, Czech Republic, Hungary, Poland, Romania, Slovak Republic, Slovenia, and Turkey. *Commonwealth of Independent States (CIS):* Azerbaijan, Belarus, Estonia, Georgia, Kazakhstan, Kyrgyz Republic, Lithuania, Moldova, Russia, Ukraine, and Uzbekistan. To determine the business challenges of entrepreneurship in Transition Economies we use the global competitiveness index (GCI), governance indicators (GI), Business Environment and Enterprise Performance Survey (BEEPS), Corruption Perception Index (CPI) and World Business Environmental Survey (WBES). After examining obstacles we will develop suggestions to entrepreneurs in Transition Economies.

## 2.The Importance and Dynamics of Entrepreneurship

Why is entrepreneurship important? First, *entrepreneurship contributes to job creation and growth*; it is increasingly new and small firms, rather than large ones, that are the major providers of new jobs. Second, *entrepreneurship is crucial to competitiveness*; new entrepreneurial initiatives, either starting a new firm or reorienting an existing one (e.g. after the transfer of a business to a new owner), boost productivity. They increase competitive pressure, forcing other firms to react by improving efficiency or introducing innovation. Increased efficiency and innovation within firms, whether in organisation, processes, products, services or markets, enhances the competitive strength of an economy as a whole. This process offers consumers benefits through greater choice and lower prices. Third, *entrepreneurship unlocks personal potential*; an occupation is not just a way to earn money. People have other criteria in their career choices, such as security, level of independence, variety of tasks and interest in their work. Higher income levels may prompt people to fulfil 'higher needs', such as self-realisation and independence, through entrepreneurship. Fourth, *entrepreneurship and societal interests*; entrepreneurs are

the drivers of the market economy and their achievements provide societies with wealth, jobs and diversity of choice for consumers (Brussels, 2003).

Some authors state that entrepreneurship is about identifying and acting upon (*enterprising human activity*) opportunities that *create value* (be that economic, cultural or social). Typically, entrepreneurial activities require the leveraging of resources and capabilities through *innovation*, but the opportunities themselves always relate to the identification of either new products, processes or markets. This point to the following definitions of the entrepreneur, entrepreneurship, and entrepreneurial activity; *entrepreneurs* are those persons (business owners) who seek to generate value, through the creation or expansion of economic activity, by identifying and exploiting new products, processes or markets. *Entrepreneurial activity* is the enterprising human action in pursuit of the generation of value, through the creation or expansion of economic activity, by identifying and exploiting new products, processes or markets. *Entrepreneurship* is the phenomena associated with entrepreneurial activity. The definitions suggest that any indicator should include reference to the value created by entrepreneurial activity, the changes in resources, capabilities and opportunities confronting an entrepreneur, and the business and wider environments that will impact activity. The definitions are proposed to guide the collection and interrogation of data sets (Ahmad and Seymour, 2008).

According to other definition entrepreneurship is about people, their choices and actions in starting, taking over or running a business, or their involvement in a firm's strategic decision-making. Entrepreneurs are a heterogeneous group and come from all walks of life. In Table 1 a number of themes emerge including the risk-taking role of entrepreneurs (Aidis, 2003); the role of innovation or the creation of something new (whether that be a process, product, market or firm); the arbitrage role of the entrepreneur; and the process of change, emergence, and creation (Aidis, 2003; Bruyat & Julian, 2000; Hartmann, 1959; Schumpeter, 1934; Weber, 1947), with activity differentiated from the relatively 'static' management (*Leitung*) (Hartmann, 1959).

**Table 1:** A Superficial Review of Extant Definitions

<i>Essence of definition</i>	<i>Publication</i>
Entrepreneurs buy at certain prices in the present and sell at uncertain prices in the future. The entrepreneur is a bearer of uncertainty.	(Cantillon, 1755/1931)

Entrepreneurs are 'pro-jectors'.	(Defoe, 1887/2001)
Entrepreneurs attempt to predict and act upon change within markets. The entrepreneur bears the uncertainty of market dynamics.	(Knight, 1921, 1942)
The entrepreneur is the person who maintains immunity from control of rational bureaucratic knowledge.	(Weber, 1947)
The entrepreneur is the innovator who implements change within markets through the carrying out of new combinations. These can take several forms:	
<ul style="list-style-type: none"> <li>· the introduction of a new good or quality thereof,</li> <li>· the introduction of a new method of production,</li> <li>· the opening of a new market,</li> <li>· the conquest of a new source of supply of new materials or parts, and</li> <li>· the carrying out of the new organisation of any industry.</li> </ul>	(Schumpeter, 1934)
The entrepreneur is always a speculator. He deals with the uncertain conditions of the future. His success or failure depends on the correctness of his anticipation of uncertain events. If he fails in his understanding of things to come he is doomed...	(von Mises, 1949/1996)
The entrepreneur is co-ordinator and arbitrageur.	(Walras, 1954)
Entrepreneurial activity involves identifying opportunities within the economic system.	(Penrose, 1959/1980)
The entrepreneur recognises and acts upon profit opportunities, essentially an arbitrageur.	(Kirzner, 1973)
Entrepreneurship is the act of innovation involving endowing existing resources with new wealth-producing capacity.	(Drucker, 1985)

The essential act of entrepreneurship is new entry. New entry can be accomplished by entering new or established markets with new or existing goods or services. New entry is the act of launching a new venture, either by a start-up firm, through an existing firm, or via 'internal corporate venturing'. (Lumpkin & Dess, 1996)

The field of entrepreneurship involves the study of sources of opportunities; the processes of discovery, evaluation, and exploitation of opportunities; and the set of individuals who discover, evaluate, and exploit them. (Shane & Venkataraman, 2000)

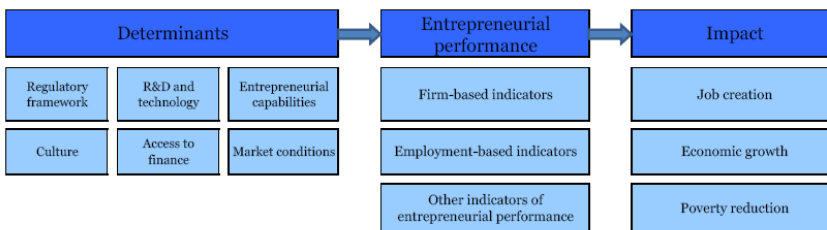
Entrepreneurship is a context dependent social process through which individuals and teams create wealth by bringing together unique packages of resources to exploit marketplace opportunities. (Ireland, Hitt, & Sirmon, 2003)

Entrepreneurship is the mindset and process to create and develop economic activity by blending risk-taking, creativity and/or innovation with sound management, within a new or an existing organisation. (Commission of the European Communities, 2003)

**Source:** Aidis, R. (2003), "Entrepreneurship and Transition Economies", TI 2003-015/2, Tinbergen Institute Discussion Paper, 1-31.

### 3. Categories for Entrepreneurship Indicators

An enterprise is a legal entity possessing the right to conduct business on its own. The OECD's Entrepreneurship Indicators Project has built a framework for addressing and measuring entrepreneurship was seen in Figure 1 (Ahmad and Hoffman, 2007).



**Figure 1:**

Topic categories for entrepreneurship indicators

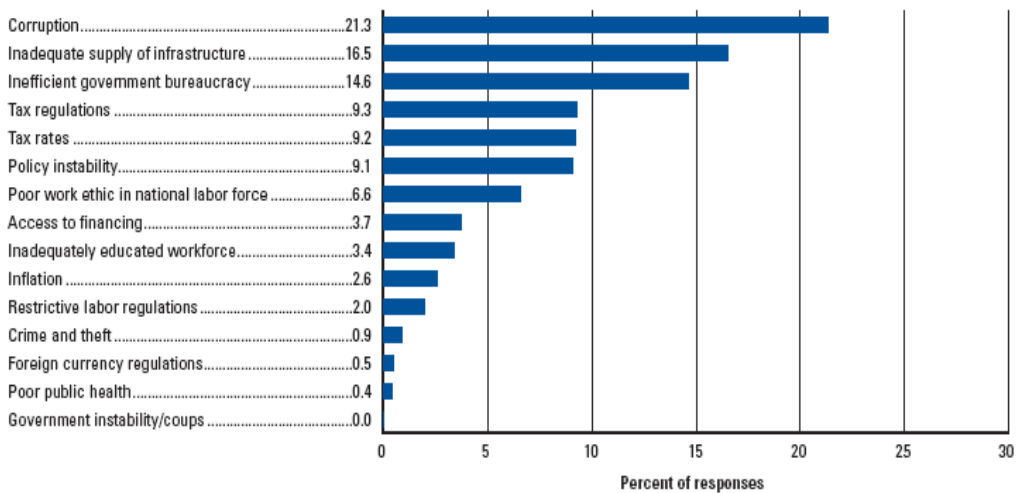
**Source:** Ahmad, N. and A. Hoffman (2007), *A Framework for Addressing and Measuring Entrepreneurship*. Paris: OECD Entrepreneurship Indicators Steering Group. OECD's project describes and presents a framework that reflects both the determinants, outputs and most importantly manifestations (performance indicators) of entrepreneurship. (Ahmad and Seymour, 2008). In our study we use indicators and indexes which cover *institutional environment and market* (taxation and regulations, financing, policy instability, inflation, corruption, infrastructure, anti-competitive practice, marketing and managerial practices and bureaucracy) in transition economies. Those indicators and indexes are Corruption Perception Index (CPI), Global Competitiveness Indicators (GCI), Governance Indicator (GI), Business Environment and Enterprise Performance Survey (BEEPS) and World Business Environmental Survey (WBES).

#### 4. Transition Economies

In our study we will examine CEE and CIS countries as a Transition Economies. *Central and Eastern (CEE)*: Albania, Armenia, Bosnia and Herzegovina, Bulgaria, Croatia, Czech Republic, Hungary, Poland, Romania, Slovak Republic, Slovenia, and Turkey. *Commonwealth of Independent States (CIS)*: Azerbaijan, Belarus, Estonia, Georgia, Kazakhstan, Kyrgyz Republic, Lithuania, Moldova, Russia, Ukraine, and Uzbekistan. *Transition Economies* = CEE plus CIS (Batra, Kaufmann and Stone, 2003).

#### 5. The Business Challenges For Entrepreneurs in Transition Economies

The performance of the transition economies has fallen short of expectations for several reasons: Advanced western economies did unusually well in the 1990s, which raised the bar for perceptions of economic success; the economic problems associated with the transition were widely underestimated; and policymakers made a number of questionable choices (Svejnar, 2001:2). In figure 2 we see the most problematic factors for doing business in Transition Economies. These factors are corruption, infrastructure, bureaucracy, tax regulations and rates, policy instability, poor work ethic, financing, inadequately educated workforce, inflation etc (Kaufman, 2005).



Note: From a list of 15 factors, respondents were asked to select the five most problematic for doing business in their country and to rank them between 1 (most problematic) and 5. The bars in the figure show the responses weighted according to their rankings.

**Figure 2:** The most problematic factors for doing business in Transition Economies (The Case of Albania)

**Source:** Kaufmann Daniel (2005), *Myths and Realities of Governance and Corruption*, World Bank 2005

The most important challenges are corruption, infrastructure, bureaucracy, taxation and financing. The other types of barriers for entrepreneurs (especially SME's) are: Learning foreign environment, Doing market analysis abroad, Purchasing legal consulting services, Translation of documents, Adaptation of products to foreign markets, Travel expenses, Higher business and financial risk, Higher business and financial risk, Establishing foreign distribution and marketing networks, Accessing information other markets, Lack of information, Knowledge and experience in international markets, Understanding overseas markets, Identifying foreign business opportunities, Inability to contact potential overseas customers, Distance of foreign markets, Transmitting information across geographic space, Regulatory requirements on product standards, Intellectual property rights protection, National competition policies, Legislative and regulatory frameworks, Telecommunications infrastructure, Research and education policies, Entrepreneurship abilities, Managerial abilities (Kaufmann, 2005).

SMEs types of entrepreneurship in transitional economies have had limited experience in international trade. During the central planning period large enterprises were favoured over SMEs. There were restrictions to private SMEs and their



international trading activities. Therefore, SMEs were not much exposed to foreign competition or exporting activities before making the transition to market economies. In addition, SMEs in transitional economies face higher transaction costs and have more limited access to credit and other inputs. As a result, they have greater difficulty penetrating export markets (Kaufmann, 2005). The barriers encountered by SME at different stages are then classified into formal, informal, environmental and other categories (based on institutional theory). The authors find that as the transition stage moves into the advanced stage, SME owners become increasingly more concerned with human resource (labour) and skill development (training) than at the initial stages seen in Table 2 (Aidis, 2003:31).

**Table 2:** The SME Barriers at Different Transition Stages

STAGE 1	STAGE 2	← Stages 2 & 3 →	STAGE 3
<b>FORMAL:</b> Taxes, Policy instability/uncertainty, Legal regulations			
<ul style="list-style-type: none"> <li>• Customs and trade regulations</li> </ul>	<ul style="list-style-type: none"> <li>• Frequent changes to laws and government</li> <li>• Business registration business</li> </ul>	<ul style="list-style-type: none"> <li>• Gov't non-transparency</li> <li>• Commercial law</li> <li>• Social security payments</li> </ul>	<ul style="list-style-type: none"> <li>• Too many licenses</li> <li>• Accounting standards</li> <li>• Information</li> <li>• Need for specific consulting advice (marketing, financial, psychological)</li> <li>• Lack of state support</li> </ul>
<b>INFORMAL:</b>			
<ul style="list-style-type: none"> <li>• Macroeconomic stability</li> <li>• Inflation</li> </ul>	<ul style="list-style-type: none"> <li>• Gov't Attitude</li> <li>• Organised crime and mafia</li> <li>• Anti – corruption measures</li> <li>• Business security</li> <li>• Lack of positive attitude</li> </ul>	<ul style="list-style-type: none"> <li>• Corruption</li> <li>• Bureaucracy</li> <li>• Payment behaviour of clients</li> </ul>	<ul style="list-style-type: none"> <li>• Too many tax inspections</li> <li>• Implementation of regulations</li> <li>• Motivation / quality ethics of the workforce</li> </ul>
<ul style="list-style-type: none"> <li>• Macroeconomic stability</li> <li>• Inflation</li> </ul>	<ul style="list-style-type: none"> <li>• Physical infrastructure</li> <li>• Low product demand</li> <li>• High input prices</li> <li>• Suppliers</li> <li>• High interest rates</li> </ul>	<ul style="list-style-type: none"> <li>• Infrastructure</li> <li>• Unfair competition</li> <li>• Premises rental costs</li> <li>• Wage costs</li> <li>• Business training</li> </ul>	<ul style="list-style-type: none"> <li>• Shortage of qualified workers</li> <li>• Strong competition</li> <li>• Lack of investment/finance</li> </ul>
<b>OTHER</b>			
<ul style="list-style-type: none"> <li>• Business growth into new markets</li> </ul>			

**Source:** Aidis, R. (2003), *“Entrepreneurship and Transition Economies”*, TI 2003-015/2, Tinbergen Institute Discussion Paper, 1-31.

There is an increased need to develop internal business capabilities to deal with increasing competition as well as business growth such as specific consulting and business training programmes. Three formal constraints: *taxes, policy instability and legal regulations* form a barrier for business development throughout the transition stages. *Access to finance* also continues to be a barrier to businesses throughout the three transition stages but it seems that the types of financing needed is affected by transition stage. In the primary or secondary stages the emphasis lies on the need for micro-credit and short and long term bank loans, the more advanced stages necessitate more sophisticated financing such as venture capital and stock listings (Aidis. 2003). As Pissarides (2004) has indicated, it is important for financing opportunities to adapt to the requirements of SME owners as transition progresses, allowing for more complex forms of financing including venture capitalists in more advanced stages. However, there are different viewpoints as to the sequence of funding and institutional building needed for SME development (Aidis, 2003:16). *Insufficient knowledge about Internet applications* is an important barrier to the adoption of e-business practices among SMEs For Slovenia, Poland, Romania and Cyprus. Research indicates that many SME managers consider the Internet is useful but mostly for the operations of big companies. As a result, they do not see compelling reasons for e-business adoption in SMEs (Damaskopoulos and Evergiou, 2003:138). Ukrainian business environment is not favorable for the innovations. High taxes and corruption create non-favorable conditions for innovations in SMEs. Many companies reported taxation and legislation among the main barriers to innovations (Egorov and Voytovich, 2001:1455).

The business barriers classified into five part. These are institutional barriers: Bureaucracy, Too many licences, Accounting standards. Political instability, Frequent changes in laws and regulations, Frequent changes in government, Non-transparency of laws/regulations, Operation of commercial law, Operation of the financial system, Inadequate measures against corruption. Internal barriers: Large severance pay, High labour costs, High dismissal costs. External barriers: Late payment, High social security payments, High profits tax. Financial barriers: Cost of credit, High collateral requirements, Bank charges. Insufficient finance for expansion, High burden of taxes/contributions, Insufficient demand. Social barriers: Lack of state support, Lack of support from LA, Lack of support from Chamber (Barlett and Bucklic, 2001:193-195). Under the light of surveys conducted by EBRD and World Bank; taxes, financing and policy instability can be observed in the top four obstacles in the transitional countries (Estrin et al,2005).

The survey asked respondents to rate how problematic were a set of general constraints for the growth and operation of their firm. Table 3 presents the ranking of responses for the world, by regional groups and by individual region to the following

question: "Please judge on a four-point scale how problematic are the following factors for the operation and growth of your firm." Four constraints stand out (based on a simple average for the overall world sample): taxes and regulations, financing, policy uncertainty/instability and inflation. Indeed, if we were to focus on a simple average for the overall world sample, the following constraints stand out: taxes and regulations, financing, policy uncertainty/instability, and inflation (Batra et al., 2003).

**Table 3: Leading Constraints**

	Leading Constraint	Second constraint	Third constraint	Fourth Constraint
World	Taxes and Regulations	Financing	Policy Instability	Inflation
OECD & Newly Industrialized East Asia (including China)	Taxes and Regulations	Financing	Policy Instability	Inflation
Transition Europe	Taxes and Regulations	Financing	Inflation	Policy Instability
Developing countries (Africa, MENA, East Asia Developing, South Asia, Latin America)	Corruption	Inflation	Financing	Policy Instability/ Infrastructure (tie)
Africa	Financing	Corruption	Infrastructure	Inflation
MENA	Policy Instability	Corruption	Inflation	Exchange Rate
East Asia NIC/China	Financing	Inflation	Anti-competitive practices	Policy Instability
East Asia Developing	Street Crime	Corruption	Inflation/Exchange Rate/Organized Crime (tie)	Infrastructure
South Asia	Corruption/Policy Instability (tie)		Inflation	Infrastructure
Latin America	Taxes and Regulations	Policy Instability	Street Crime	Financing
OECD	Taxes and Regulations	Financing	Policy Instability	Inflation
CIS	Taxes and Regulations	Financing	Policy Instability	Inflation
CEE	Taxes and Regulations/Inflation (tie)		Financing	Policy Instability

**Source:** Batra, Geeta, Daniel Kaufmann and Andrew H. W. Stone (2003), *The Firms Speak: What the World Business Environment Survey Tells Us about Constraints on Private Sector Development*, World Bank October, 2003, p.5

Yet such worldwide average results mask crucial differences across regions, and particularly between industrialized and developing countries. For OECD, newly industrialized East Asian countries, and transition economies, the leading obstacles identified by the firms where indeed taxes and regulations, financing, policy instability, and inflation. However, for developing regions as a group (Africa; Latin America and the Caribbean, LAC; Middle East/North Africa, MENA; South Asia; and East Asia) the leading constraint is corruption, followed by inflation, financing, policy instability, and infrastructure. Surprisingly, in Transition Europe (CIS and CEE), although corruption is quite prevalent in the region and an important problem for about half the firms, it is not among the top four constraints (Batra et al., 2003).

The second leading general constraint (Table 4) for the global sample is financing firms in Central and Eastern Europe are most likely to identify it as seriously

constraining, followed by those in CIS countries, and then those in Africa, South Asia and Latin America. Globally, while financing is identified as the second leading constraint by small and medium enterprises, it ranks as fourth for large enterprises (Batra et al., 2003). Svetlicic et al (2007) has supported this findings. Their study examined differences in outward foreign direct investment (FDI) activity between small and medium-size enterprises (SMEs) and large enterprises in five Central European economies (CEEs). In conclusion they have found that the access to financial resources is more difficult for SME's than large firms.

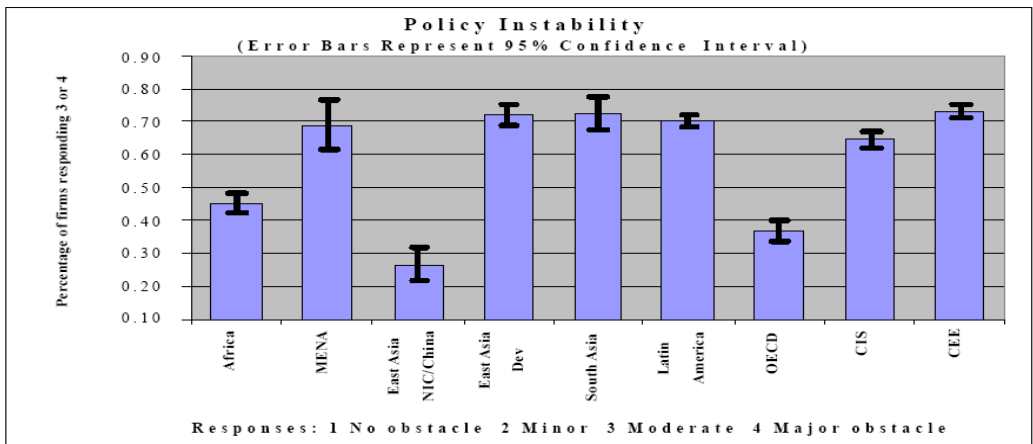
**Table 4:** Financing Constraints (percent of firms rating constraint “major” or “moderate”)

Financing Constraints	Africa	MENA	East Africa NIC/China	East Asia Developing	South Asia	Latin America	OECD	CIS	CEE
High interest rates	83.5	67.4	40.3	72.5	83.9	87.6	47.8	80.6	79.5
Lack access to long term loan	n.a.	n.a.	31.2	52.0	65.1	63.1	20.0	58.7	67.0
Collateral requirements	51.9	45.2	30.1	43.6	58.5	65.1	35.7	49.7	52.2
Bank paperwork	47.1	51.6	29.9	34.6	56.6	63.0	38.9	52.9	48.3
Inadequate credit info on clients	51.7	46.3	27.0	48.4	46.7	46.1	23.5	40.1	41.6
Special connections	38.2	33.3	26.3	39.6	44.5	46.5	26.5	35.1	43.1
Banks lack money to lend	28.4	33.0	20.6	52.2	35.1	39.1	14.3	37.4	46.8
Access to specialized export finance	44.9	39.8	15.1	33.7	36.4	34.7	16.5	35.5	38.8
Access to non-bank equity	43.1	36.2	13.0	32.6	34.9	35.6	18.1	38.3	42.0
Access to lease finance	38.2	29.3	13.1	34.9	32.9	34.1	19.3	32.7	48.9
Access to foreign banks	43.6	29.3	11.7	41.5	33.9	35.0	11.1	35.3	40.4
Corruption of bank officials	23.5	27.4	19.0	45.1	28.9	18.6	5.7	24.3	29.3

**Source:** Batra, Geeta, Daniel Kaufmann and Andrew H. W. Stone (2003), *The Firms Speak: What the World Business Environment Survey Tells Us about Constraints on Private Sector Development*, World Bank October, 2003, p.5

The fourth leading constraint is policy uncertainty and instability (Batra et al., 2003). Meyer et al (2005) argued that according to the foreign investors; instability and uncertainty are major obstacles related to new rules and regulation. Firms' views of this constraint vary widely by region (Figure 3). At one extreme, more than 70 percent of firms in South Asia, Central and Eastern Europe and Developing East Asia report policy instability as seriously constraining, with firms in Latin America, MENA, and CIS close behind. By contrast, only 26 percent of firms in East Asia NIC and China identified this constraint as “major” or “moderate”, and also only 37 percent of firms in OECD countries did so (Batra et al., 2003).

Firms differ by region in the particular dimension of policy instability that troubles them. Over 70 percent of firms in CEE, over 60 percent of firms in CIS countries and Developing East Asia, and about half of firms in LAC find *economic and financial policies* unpredictable. In CEE and Africa, nearly three quarters of firms rated *changes in rules, laws and regulations* affecting them as being unpredictable, while two-thirds of firms did so in CIS. With regard to *advance notification of changes in laws and policies* affecting them, 68 percent of firms in CEE, 60 percent of CIS firms, and 57 percent Latin American firms responding reported that they were “seldom” or “never” notified in advance of changes affecting them. Finally, there is a question of whether *government considers businesses’ views* in the formulation of legal and policy changes. In Transition Europe, MENA and Latin America the majority of firms suggest that this is relatively rare (Batra et al., 2003).



**Figure 3:** Policy Instability by Region (percent of firms responding 3 or 4 seriously constraining)

**Source:** Batra, Geeta, Daniel Kaufmann and Andrew H. W. Stone (2003), *The Firms Speak: What the World Business Environment Survey Tells Us about Constraints on Private Sector Development*, World Bank October, 2003.

Corruption is identified as a serious constraint by over 70 percent of firms in South Asia and nearly as many in Developing East Asia and MENA (Figure 4). Sixty-four percent of firms in Africa, almost 60 percent of those in Latin America and about half in the CIS and Central and Eastern Europe report it a serious impediment. This contrasts with the much lower share (about 20 percent) of firms in NIC East Asia/China<sup>5</sup> and in OECD countries that rate it as a “major” or “moderate” obstacle.

Further, in many of the developing countries, the majority of firms reported that it was common “in their line of business to have to pay some irregular ‘additional payments’ to get things done”. The data on firms’ reported percentage of total revenue paid every year in bribes clearly and positively correlate with the data on the degree to which firms find corruption constraining.

<i>Region</i>	<i>Irregular additional payments Made to government officials "to get things done"</i>	<i>Advance knowledge of amount of additional payment</i>	<i>Service delivered as agreed if additional payment made<sup>5</sup></i>	<i>If payment made to one official, another govt official will request payment for same service</i>	<i>If government official acts against rules, can go to superior and get correct treatment without recourse to unofficial payment</i>
South Asia	65	50	83	46	32
East Asia Developing	62	60	76	60	26
Africa	52	not asked	33	not asked	not asked
MENA	36	not asked	53	not asked	not asked
CEE	33	48	73	28	36
CIS	29	46	75	35	38
Latin America	28	70	32	70	69
OECD	12	26	62	17	45
East Asia NIC/China	11	22	42	10	25
Total	13	53	59	45	45

**Figure 4:** Indicators of Corruption by Region (percent of firms that responded “always,” “mostly,” or “frequently,” as opposed to “sometimes,” “seldom,” or “never”)

**Source:** Batra, Geeta, Daniel Kaufmann and Andrew H. W. Stone (2003), *The Firms Speak: What the World Business Environment Survey Tells Us about Constraints on Private Sector Development*, World Bank October, 2003.

An important manifestation of weak governance is the extent to which registered firms operate unofficially. Related to this is the degree to which firms comply with tax laws. While there are variations from region to region, about half the firms in the global sample indicated that they report no more than 80 percent of their revenues (Batra et al., 2003).

## 6. The Impact of EU Accession

Eight transition countries became members of the EU in May 2004 (Estonia, Latvia, Lithuania, Hungary, Czech R., Slovak R., Poland and Slovenia). A number of authors argue that EU accession will be a win-win situation for both the existing member countries as well as the new accession countries (Mayhew 1999; EIU 2003; Knaack and Jager 2003). To be sure, EU market integration will increase overall business possibilities. Depending on the size of business, EU accession effect closely

entrepreneurship operations. In table 5, we summarize a number of opportunities and threats corresponding to EU membership for SMEs type of entrepreneurship.

**Table 5:** EU Membership Opportunities and Threats for SME Development

Issue	Opportunities	Threats
Exports	New export opportunities*	Competition increased in domestic markets**
Economies of scale	Cost reduction and efficient production	Price wars and crowding out of small suppliers*
Opening borders and market integration	Removal of barriers and restriction in the movement of goods, services, labour and capital*	Costs: Harmonisation of technical standards and compliance costs*
	Improve cross-border trade*	Enforcement: Having the laws in place means little if they are not effectively enforced* Need new skills in specialized management*
Further removal of physical barriers for trade and movement i.e. customs procedures	Reduction of transaction costs for businesses*	SMEs incur highest adjustment costs and will have to accumulate additional investment
Increased mobility for EU citizens	Liberalisation of airlines increases access for tourism*	Decrease in labour pool due to 'brain drain' to higher wage EU countries*
Harmonisation of regulations	Improved overall business environment*	Greater burden: environmental protection; workplace health; May inflate operating costs rather than reduce them*
Higher living standards	Increased consumption*	Higher costs of production* Labour-cost advantage quickly eroded

**Source:** Aidis, R. (2003), *“Entrepreneurship and Transition Economies”*, TI 2003-015/2, Tinbergen Institute Discussion Paper, 1-31.

EU accession lead to opening border, market integration and new export opportunities which bring in turn unexpected competitive pressures in domestic markets. Local SMEs are likely to be promoted less than large sized enterprises and multinationals by EU market changes. Therefore SMEs will need new management skills and new technical standards which will increase their costs, investment in higher product and process standards. Adoption of new laws may seem attractive however corrupt behaviors could affect the uneven implementation and enforcement of these laws (Aidis, R., 2003). Trade, investment patterns and infrastructure developments provide better opportunities for connection between Southeast Europe with the EU. Although Southeast Europa has poor rail and road transport infrastructure due to history of political disintegration, most of Balkan countries transportation connection to the EU is much better than other countries in the region. Therefore infrastructure

investments will be beneficial to ensure crossborder co-operation and nurture conditions for increased economic growth and political integration (IBEU, 2004).

Subject to the integration to EU, higher living standards will reduce the new member country's low labour cost advantage and increased mobility within the member countries will encourage qualified workers to work in old EU members where the wages are higher. For example Lithuania encounter a shortage of qualified workers for the construction and service sectors. In general, without government intervention, the winners in EU integration will be large enterprises and the losers will disproportionately be SMEs. However, internal firm-level development also plays a decisive role. As Smallbone and Rogut comment (Aidis, R., 2003):

*... firms that are already proactively managed, and with an existing presence in foreign markets, are in the best position to take advantage of any new foreign market opportunities. In comparison, firms that are focused on regional or domestic markets niches, and in which managers are complacent or dismissive about any market integration effects impacting on their businesses, may be in for a shock.*

## 7. Examining Entrepreneurship in Transition Economies: Indicators and Indexes

### The Business Environment and Enterprise Performance Survey (BEEPS)

The Business Environment and Enterprise Performance Survey (BEEPS) is based on the firm level data which measure the corruption experience of firms. BEEPS was designed to unbundle corruption so different types of corruption transactions are determined which have dissimilar causes and results. A comparison is made on the both the extent and type of corruption experienced by foreign versus domestic firms, as well as among different types of foreign firms by means of BEEPS. Two types of corruption; state capture and public procurement kickbacks are focused by the researchers of survey. **State capture:** defined as the extent to which firms make illicit private payments to public officials in order to influence the formation of laws, rules, regulations or decrees by state institutions, and **Public procurement kickbacks:** defined as illicit private payments to public officials to secure public procurement contracts (Hellman, Jones and Kaufmann, 2002).

The BEEPS survey provides the first empirical measures of state capture. Firms were asked to disaggregate the types of bribery in which "firms like yours" have been engaged. Those that report having made private payments to public officials for the purpose of influencing the



content of laws, decrees or regulations are designated as *captor firms*. Similarly, firms were asked if they had made private payments to public officials to obtain public procurement contracts, though this question was only asked of the subset of firms that already identified themselves as having trade with the state. Thus, a group of *kickback firms* can be identified from the larger sample. Table 6 presents the data on the share of captor firms and kickback firms in each country.

**Table 6:** Measuring the Types and Level of Corruption in Transition Economies

Country	Share of Captor Firms <sup>2</sup>	Share of Kickback Firms <sup>3</sup>	Average Share of Annual Firm Revenues Paid in Bribes <sup>1</sup>
Albania	11	51	4.0
Armenia	7	26	4.6
Azerbaijan	24	52	5.7
Belarus	2	5	1.3
Bulgaria	11	13	2.1
Croatia	10	26	1.1
Czech Republic	7	43	2.5
Estonia	5	28	1.6
Georgia	8	18	4.3
Hungary	4	15	1.7
Kazakhstan	6	21	3.1
Kyrgyzstan	7	19	5.3
Latvia	14	22	1.4
Lithuania	14	15	2.8
Moldova	12	9	4.0
Poland	9	32	1.6
Romania	13	39	3.2
Russia	9	22	2.8
Slovakia	12	35	2.5
Slovenia	10	27	1.4
Ukraine	12	33	4.4
Uzbekistan	2	24	4.4
Overall	9.5	26	3.0

**Source:** Hellman Joel S., Geraint Jones and Daniel Kaufmann (2002), *Far From Home: Do Foreign Investors Import Higher Standards of Governance in Transition Economies?* [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=386900](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=386900)

The data in table 6 allow us to see that the highest share of captor firms is in Azerbaijan; on the other hand, the lowest share takes place in Uzbekistan; the highest share of kickback firms is in Albania; on the other side, Belarus has the lowest level. In addition, table 6 provides a measure of the average share of bribe payments by firms as a share of their annual revenue. Once again Azerbaijan firms come first in average share of annual firm revenues paid bribes.

## 7.2. The World Business Environment Survey (WBES)

The World Bank's World Business Environment Survey (WBES) suggests what is required to develop the business environment, based on what businesses themselves say about conditions they need to grow and the obstacles they struggle. A standard core enterprise survey was applied in a roughly parallel way in all 80 countries throughout the world, (at least 100 firms were surveyed in each country) plus the West Bank and Gaza to evaluate business conditions in a large, crossregional set of member countries, by the World Bank Group and partner institutions. It uses a uniform methodology and parallel parameters for sample structure. The conditions WBES sought to assess include: *the conditions for private enterprise growth, focusing on local economic policy, governance, regulatory, infrastructure and financial barriers, and services to businesses*. The survey represents an important step toward standardizing evaluations of the conditions for private investment in developing and transition countries around the world. The survey enables to make *regional comparisons of investment climate and business environment conditions*. The WBES explores how a variety of firm characteristics, such as size and type of ownership, affect their experience and perceptions of constraints. Using a multivariate regression approach gives us insights into the influence of firm characteristics on their response to key potential obstacles to business operation and growth, to control for country effects (Batra, Kaufmann and Stone, 2003).

WBES prevents universal generalizations. It suggests enormous variance different kinds of constraints. Even though two countries may have important regulatory or governance restrictions, the elements may be rather different in each country; hence, generalization should be avoided.

**Table 7: Effect of Firm Characteristics on Obstacle Severity: Results of Least Square Estimates**

Dependent variable	Explanatory variables							
	Small Size Firm	Medium Size Firm	Firms with foreign ownership	Firms with government control	Firms that export	Located in Large city	Located in Small city	N
Finance <sup>a</sup>	0.222* (0.034)	0.159* (0.031)	-0.329* (0.030)	0.105* (0.036)	0.065* (0.025)	0.021 (0.029)	0.055 (0.034)	9211
Taxes and regulations	0.071* (0.026)	0.080* (0.026)	-0.096* (0.025)	-0.169* (0.029)	0.005 (0.021)	0.002 (0.025)	0.018 (0.028)	9384
Inflation <sup>a</sup>	0.173* (0.030)	0.096* (0.027)	-0.084* (0.027)	-0.076* (0.032)	-0.053** (0.022)	-0.032 (0.027)	0.011 (0.030)	9111
Exchange rate <sup>a</sup>	0.089* (0.033)	0.031 (0.030)	0.058** (0.028)	-0.108* (0.036)	0.116* (0.025)	0.021 (0.029)	0.089* (0.034)	8990
Corruption <sup>a</sup>	0.205* (0.034)	0.112* (0.031)	-0.054 (0.031)	-0.165* (0.037)	0.003 (0.025)	0.016 (0.031)	0.029 (0.036)	8359
Tax Administration <sup>b</sup>	0.053 (0.032)	0.063** (0.029)	-0.057** (0.028)	-0.175* (0.034)	0.012 (0.023)	0.011 (0.028)	0.071** (0.032)	9479
Infrastructure <sup>b, c</sup>	-0.082 (0.032)	-0.022 (0.029)	0.007 (0.028)	-0.128* (0.033)	-0.018 (0.023)	0.019 (0.027)	0.047 (0.032)	9119
Policy instability	0.041 (0.032)	0.035 (0.029)	-0.018 (0.029)	-0.113* (0.034)	0.012 (0.023)	-0.033 (0.028)	-0.004 (0.032)	9016
High Taxes <sup>b</sup>	0.074* (0.027)	0.085* (0.029)	-0.093* (0.026)	-0.238* (0.031)	-0.004 (0.021)	0.017 (0.026)	0.028 (0.029)	9695
Street Crime	0.188* (0.033)	0.074* (0.030)	-0.077* (0.029)	-0.109* (0.035)	-0.077* (0.024)	-0.003 (0.029)	-0.016 (0.034)	8801
Bribes as % of sales <sup>a</sup>	0.254* (0.059)	0.159* (0.055)	-0.077 (0.050)	-0.257* (0.072)	-0.075 (0.042)	0.014 (0.048)	0.055 (0.056)	5234

\* significant at 1% level; \*\* significant at 5% level; \*\*\* significant at 10% level.

**Source:** Batra, Geeta, Daniel Kaufmann and Andrew H. W. Stone (2003), *The Firms Speak: What the World Business Environment Survey Tells Us about Constraints on Private Sector Development*, World Bank October, 2003

This survey also discourages universal generalizations. Rather, it's value lies precisely in shedding light on the enormous *variance* in the nature and severity of different types of constraints *across countries and regions*, as well as *between firms of different characteristics*.

This variance implies that the global generalizations regarding the severity of a particular constraint are of limited value. It also suggests the importance of "unbundling" generic clusters of constraints. Although two countries may have severe regulatory or governance constraints, for example, the components may be quite different in each country. The detail afforded by the survey also suggests that

generalizations about firm size and formality may benefit from a nuanced analysis of actual conditions (Batra, Kaufmann and Stone, 2003).

### 7.3. Governance Indicator

Governance Indicators (GI) have been developed to define in depth and measure governance. Covering more than 200 countries, these GI are based on more than 350 variables and obtained from dozens of institutions worldwide, including the survey. The Governance Indicators capture six key dimensions of institutional quality or governance, and measure, through two indicators each, the political, economic, and institutional dimensions of governance described above. The following six dimensions are (Kaufmann, 2005): *Voice and accountability*—measuring political, civil and human rights. *Political instability and violence*—measuring the likelihood of violent threats to, or changes in, government, including terrorism. *Government effectiveness*—measuring the competence of the bureaucracy and the quality of public service delivery. *Regulatory burden*—measuring the incidence of market-unfriendly policies. *Rule of law*—measuring the quality of contract enforcement, the police, and the courts, as well as the likelihood of crime and violence. *Control of corruption*—measuring the exercise of public power for private gain, including both petty and grand corruption, and state capture. These indicators have been available since 1996, and we released the last installment for 209 countries, with data up to the end of 2004.

**Table 8:** Significant Changes in Governance Worldwide in Short-term, 1998–2004

Selected countries based on aggregate indicators for 209 countries	
<b>Voice and accountability</b>	
Significantly worsened.....	Central African Republic, Nepal, Ivory Coast, Haiti, Zimbabwe, Russia, Kyrgyz Republic, Eritrea, Pakistan, Belarus, Solomon Islands, Venezuela, Kazakhstan, Bangladesh, Ecuador, Iran, Gabon
Significantly improved .....	Chile, Kenya, Bahrain, Gambia, Algeria, Mexico, Senegal, Peru, Turkey, Slovak Republic, Nigeria, Indonesia, Ghana, Croatia, Bosnia and Herzegovina, Sierra Leone, Serbia
<b>Regulatory quality</b>	
Significantly worsened.....	Zimbabwe, Venezuela, Ivory Coast, Ethiopia, Bangladesh, Pakistan, Philippines, Lebanon, Egypt, Zambia, Myanmar, Guinea, Eritrea, Bolivia, Peru, Tunisia, Honduras, Guatemala, Ecuador, Kazakhstan, Cameroon, Cuba
Significantly improved .....	Cape Verde, Armenia, Tajikistan, Azerbaijan, Bosnia and Herzegovina, Serbia, Estonia, Zaire DRC, Equatorial Guinea, Iceland, Lithuania, Slovak Republic, Iraq
<b>Rule of law</b>	
Significantly worsened.....	Zimbabwe, Argentina, Ivory Coast, Ethiopia, Moldova, Cuba, Venezuela, Nepal, Haiti, Lebanon, Papua New Guinea, Dominican Republic, Myanmar, Eritrea
Significantly improved .....	Mozambique, Slovak Republic, Estonia, Latvia, Lithuania, Madagascar
<b>Control of corruption</b>	
Significantly worsened.....	Zimbabwe, Bangladesh, Eritrea, Ivory Coast, Swaziland, Ethiopia, Equatorial Guinea, Central African Republic, Sudan, Moldova
Significantly improved .....	Tanzania, Madagascar, Croatia, Serbia, Colombia, Bulgaria, Estonia, Latvia, Slovak Republic

**Source:** Kaufmann Daniel (2005), *Myths and Realities of Governance and Corruption*, World Bank 2005.

#### 7.4. The Global Competitiveness Indexes

After several years of rapid and almost unhampered growth, the global economic landscape is changing. Rising food and energy prices, a major international financial crisis, and the related slowdown in the world's leading economies are confronting policymakers with new economic management challenges. Today's volatility underscores the importance of a competitiveness supporting economic environment that can help national economies to weather these types of shocks in order to ensure solid economic performance going into the future. A nation's level of competitiveness reflects the extent to which it is able to provide rising prosperity to its citizens. Since 1979, the World Economic Forum's annual *Global Competitiveness Reports* have examined the many factors enabling national economies to achieve sustained economic growth and long-term prosperity. Their goal over the years has been to provide benchmarking tools for business leaders and policymakers to identify obstacles to improved competitiveness, stimulating discussion on strategies to overcome them. For the past several years, the World Economic Forum has based its competitiveness analysis on the Global Competitiveness Index (GCI), a highly comprehensive index for measuring national competitiveness, which captures the microeconomic and macroeconomic foundations of national competitiveness (Schwab and Porter, 2008).

Schwab and Porter (2008) define *competitiveness* as *the set of institutions, policies, and factors that determine the level of productivity of a country*. The level of productivity, in turn, sets the sustainable level of prosperity that can be earned by an economy. In other words, more competitive economies tend to be able to produce higher levels of income for their citizens. The productivity level also determines the rates of return obtained by investments in an economy. Because the rates of return are the fundamental drivers of the growth rates of the economy, a more competitive economy is one that is likely to grow faster over the medium to long run. The concept of competitiveness thus involves static and dynamic components: although the productivity of a country clearly determines its ability to sustain a high *level* of income, it is also one of the central determinants of the returns to investment, which is one of the key factors explaining an economy's *growth potential*.

The determinants of competitiveness are many and complex. For hundreds of years, economists have tried to understand what determines the wealth of nations. This

attempt has ranged from Adam Smith's focus on specialization and the division of labor to neoclassical economists' emphasis on investment in physical capital and infrastructure, and, more recently, to interest in other mechanisms such as education and training, technological progress (whether created within the country or adopted from abroad), macroeconomic stability, good governance, the rule of law, transparent and well-functioning institutions, firm sophistication, demand conditions, market size, and many others. Schwab and Porter (2008) group all these components into *12 pillars of economic competitiveness*: These are **Basic requirements** (Institutions, Infrastructure, Macroeconomic stability, Health and primary education), **Efficiency enhancers** (Higher education and training, Goods market efficiency, Labor market efficiency, Financial market sophistication, Technological readiness, Market size), **Innovation and sophistication factors** (Business sophistication, Innovation). In table 9 we see global competitiveness index rankings and 2007-2008 comparisons.

**Table 9: Global Competitiveness Index rankings and 2007–2008 comparisons**

Country/Economy	GCI 2008–2009		GCI 2008–2009 rank (among 2007 countries)*	GCI 2007–2008 rank	Country/Economy	GCI 2008–2009		GCI 2008–2009 rank (among 2007 countries)*	GCI 2007–2008 rank
	Rank	Score				Rank	Score		
United States	1	5.74	1	1	Azerbaijan	69	4.10	68	66
Switzerland	2	5.61	2	2	Vietnam	70	4.10	69	68
Denmark	3	5.58	3	3	Philippines	71	4.09	70	71
Sweden	4	5.53	4	4	Ukraine	72	4.09	71	73
Singapore	5	5.53	5	7	Morocco	73	4.08	72	64
Finland	6	5.50	6	6	Colombia	74	4.05	73	69
Germany	7	5.46	7	5	Uruguay	75	4.04	74	75
Netherlands	8	5.41	8	10	Bulgaria	76	4.03	75	79
Japan	9	5.38	9	8	Sri Lanka	77	4.02	76	70
Canada	10	5.37	10	13	Syria	78	3.99	77	80
Hong Kong SAR	11	5.33	11	12	El Salvador	79	3.99	78	67
United Kingdom	12	5.30	12	9	Namibia	80	3.99	79	89
Korea, Rep.	13	5.28	13	11	Egypt	81	3.98	80	77
Austria	14	5.23	14	15	Honduras	82	3.98	81	83
Norway	15	5.22	15	16	Paru	83	3.95	82	86
France	16	5.22	16	18	Guatemala	84	3.94	83	87
Taiwan, China	17	5.22	17	14	Serbia	85	3.90	84	91
Australia	18	5.20	18	19	Jamaica	86	3.89	85	78
Belgium	19	5.14	19	20	Gambia, The	87	3.88	86	102
Iceland	20	5.05	20	23	Argentina	88	3.87	87	85
Malaysia	21	5.04	21	21	Macedonia, FYR	89	3.87	88	94
Ireland	22	4.99	22	22	Georgia	90	3.86	89	90
Israel	23	4.97	23	17	Libya	91	3.85	90	88
New Zealand	24	4.93	24	24	Trinidad and Tobago	92	3.85	91	84
Luxembourg	25	4.85	25	25	Kenya	93	3.84	92	99
Qatar	26	4.83	26	31	Nigeria	94	3.81	93	95
Saudi Arabia	27	4.72	27	35	Moldova	95	3.75	94	97
Chile	28	4.72	28	26	Senegal	96	3.73	95	100
Spain	29	4.72	29	29	Armenia	97	3.73	96	93
China	30	4.70	30	34	Dominican Republic	98	3.72	97	96
United Arab Emirates	31	4.68	31	37	Algeria	99	3.71	98	81
Estonia	32	4.67	32	27	Mongolia	100	3.65	99	101
Czech Republic	33	4.62	33	33	Pakistan	101	3.65	100	92
Thailand	34	4.60	34	28	Ghana	102	3.62	n/a	n/a
Kuwait	35	4.58	35	30	Suriname	103	3.58	101	113
Tunisia	36	4.58	36	32	Ecuador	104	3.58	102	103
Bahrain	37	4.57	37	43	Venezuela	105	3.56	103	98
Oman	38	4.55	38	42	Benin	106	3.56	104	108
Brunei Darussalam	39	4.54	n/a	n/a	Bosnia and Herzegovina	107	3.56	105	106
Cyprus	40	4.53	39	55	Albania	108	3.55	106	109
Puerto Rico	41	4.51	40	36	Cambodia	109	3.53	107	110
Slovenia	42	4.50	41	39	Côte d'Ivoire	110	3.51	n/a	n/a
Portugal	43	4.47	42	40	Bangladesh	111	3.51	108	107
Lithuania	44	4.45	43	38	Zambia	112	3.49	109	122
South Africa	45	4.41	44	44	Tanzania	113	3.49	110	104
Slovak Republic	46	4.40	45	41	Cameroon	114	3.48	111	116
Barbados	47	4.40	46	50	Guyana	115	3.47	112	126
Jordan	48	4.37	47	49	Tajikistan	116	3.46	113	117
Italy	49	4.35	48	46	Mali	117	3.43	114	115
India	50	4.33	49	48	Bolivia	118	3.42	115	105
Russian Federation	51	4.31	50	58	Malawi	119	3.42	n/a	n/a
Malta	52	4.31	51	56	Nicaragua	120	3.41	116	111
Poland	53	4.28	52	51	Ethiopia	121	3.41	117	123
Latvia	54	4.26	53	45	Kyrgyz Republic	122	3.40	118	119
Indonesia	55	4.25	54	54	Lesotho	123	3.40	119	124
Botswana	56	4.25	55	76	Paraguay	124	3.40	120	121
Mauritius	57	4.25	56	60	Madagascar	125	3.38	121	118
Panama	58	4.24	57	59	Nepal	126	3.37	122	114
Costa Rica	59	4.23	58	63	Burkina Faso	127	3.36	123	112
Mexico	60	4.23	59	52	Uganda	128	3.35	124	120
Croatia	61	4.22	60	57	Timor-Leste	129	3.15	125	127
Hungary	62	4.22	61	47	Mozambique	130	3.15	126	128
Turkey	63	4.15	62	53	Mauritania	131	3.14	127	125
Brazil	64	4.13	63	72	Burundi	132	2.98	128	130
Montenegro	65	4.11	64	82	Zimbabwe	133	2.88	129	129
Kazakhstan	66	4.11	65	61	Chad	134	2.85	130	131
Greece	67	4.11	66	65					
Romania	68	4.10	67	74					

\* One country that was included last year is not shown because of the lack of Survey data (Uzbekistan). This explains why the lowest rank in this column

**Source:** Schwab, Klaus and Michael E. Porter (2008) *The Global Competitiveness Report The Global Competitiveness Report* (2008 World Economic Forum)

## 7.5. Corruption Perceptions Index (CPI)

A country or territory's *CPI Score* indicates the degree of public sector corruption as perceived by business people and country analysts, and ranges between 10 (highly clean) and 0 (highly corrupt). In table 10 we see Corruption Perception Index of Transition Economies.

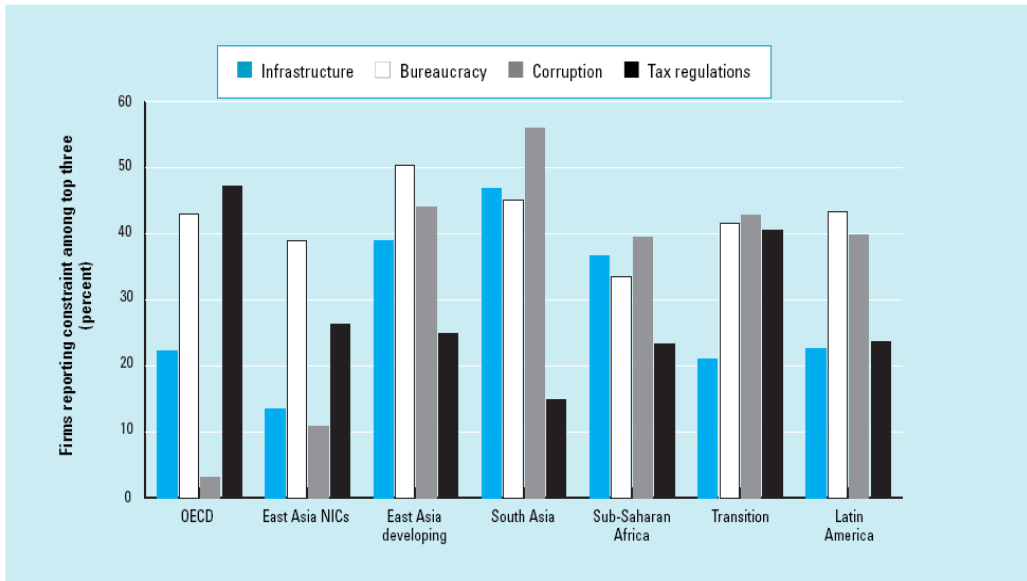
**Table 10:** 2008 Corruption Perceptions Index of Transition Economies (out of 180)

Country Rank	Country /Territory CPI	CPI Score 2008	Standard Deviation	Confidence Intervals*	Surveys Used**
26	Slovenia	<b>6.7</b>	0.5	6.5 – 7.0	8
27	Estonia	<b>6.6</b>	0.7	6.2 – 6.9	8
45	Czech Republic	<b>5.2</b>	1.4	.8 - 5.9	8
47	Hungary	<b>5.1</b>	0.6	4.8 - 5.4	8
52	Slovakia	<b>5.0</b>	0.7	4.5 - 5.3	8
58	Turkey	<b>4.6</b>	0.9	4.1 - 5.1	7
58	Lithuania	<b>4.6</b>	1	4.1 - 5.2	8
58	Poland	<b>4.6</b>	1	4.0 - 5.2	8
62	Croatia	<b>4.4</b>	0.7	4.0 - 4.8	8
67	Georgia	<b>3.9</b>	1.2	3.2 - 4.6	7
70	Romania	<b>3.8</b>	0.8	3.4 - 4.2	8
72	Bulgaria	<b>3.6</b>	1.1	3.0 - 4.3	8
72	Macedonia	<b>3.6</b>	1.1	2.9 - 4.3	6
85	Montenegro	<b>3.4</b>	1	2.5 - 4.0	5
85	Albania	<b>3.4</b>	0.1	3.3 - 3.4	5
92	Bosnia and Herzegovina	<b>3.2</b>	0.6	2.9 - 3.5	7
109	Armenia	<b>2.9</b>	0.4	2.6 - 3.1	7
109	Moldova	<b>2.9</b>	1.1	2.4 - 3.7	7
134	Ukraine	<b>2.5</b>	0.5	2.2 - 2.8	8
145	Kazakhstan	<b>2.2</b>	0.7	1.8 - 2.7	6
147	Russia	<b>2.1</b>	0.6	1.9 - 2.5	8
151	Belarus	<b>2.0</b>	0.7	1.6 - 2.5	5
158	Azerbaijan	<b>1.9</b>	0.4	1.7 - 2.1	8
166	Uzbekistan	<b>1.8</b>	0.7	1.5 - 2.2	8
166	Kyrgyzstan	<b>1.8</b>	0.2	1.7 - 1.9	7

**Source:** Lambsdorff, 2008 ([transparency.org/surveys/#cpi](http://transparency.org/surveys/#cpi) or [www.icgg.org](http://www.icgg.org))



Slovenia, Estonia, Czech Republic, Hungary and Slovakia' CPI score are above 5.0. Azerbaijan, Uzbekistan and Kyrgyzstan' CPI score are below 2.0. We can say that corruption is an important constraint for entrepreneurs in transition economies. In figure 6 we see some key constraints to business, by region.



**Figure 6:** Some key constraints to business, by region: Responses from firms in Survey 2005

**Source:** Kaufmann Daniel (2005), *Myths and Realities of Governance and Corruption*, World Bank 2005

According to figure 6 *Corruption* is the most important constraint in transition. The other important constraints are *bureaucracy and tax regulation and then infrastructure*.

## Conclusion

Institutional environment and market conditions are important for entrepreneurs all over the world. In our study we try to determine the most important constraints for entrepreneurs in Transition Economies by using indicators and indexes. We see that bureaucracy, tax regulation, financing, infrastructure and corruption is the most important constraints in transition. Our researches show that all size of entrepreneurship (SMEs, Multinational, National Enterprise etc.) is important to

growth of the transition economies. Beside this business owner characteristics is important as well as environment and the role of the state for entrepreneurs in transition.

The role of government will be of crucial importance in the transition economies. Government will be required to put in place the necessary market oriented structures and institutions that will facilitate the establishment, nurturing and growth of SMEs. Bureaucratic regulations and corruption need to be tackled as a matter of urgency. Government and its agencies will be increasingly required to play a facilitatory rather than production role within the economy, one that embraces the market, private ownership and entrepreneurialism. Increased participation of SMEs in the global economy will also be essential and in this regard policy should aim at: encouraging the upgrading of skills and technology; providing information on market opportunities; facilitating access to small business finance; facilitating networking amongst SMEs and, where appropriate with large domestically owned enterprises as well as TNCs. The obstacles facing SMEs in the transition economies are immense, but the process of globalization will require their improved competitiveness and product quality if they are to survive let alone fully participate and benefit from it (Kaufman, 2005).

It is expected that the harmonisation of regulations will improve the overall business environment but it can also result in additional compliance costs. SMEs tend to have lower absorption capacity, therefore increased regulatory costs result in increased prices for consumers thus reducing overall competitiveness. Some EU regulations will have less impact on SMEs such as environmental protection which will primarily impact large-scale manufacturers especially those producing chemicals, metals, machinery and equipment. However, increased workplace health standards will have a broader impact on all enterprises regardless of size.

There is an increased need to develop internal business capabilities to deal with increasing competition as well as business growth such as specific consulting and business training programmes. The obvious policy conclusion is that governments wanting to promote the outward internationalization of SMEs should: Deregulate economic infrastructure and simplify administrative procedures for doing business abroad; Provide information on conditions for doing business abroad on a regular basis, offering online platforms for small businesses in foreign countries and institutions; Improve SMEs' access to financial resources and adjust internationalization support programs to SMEs' needs; Simplify accounting systems and create financial and fiscal frameworks that alleviate the difficulties faced by SMEs and encourage innovative activities; Improve cooperation between business and research and educational institutions to stimulate spillovers and a more adaptive education system; Introduce educational methods and programs that enhance

innovation and entrepreneurship and develop holistic internationalization training programs; Initiate R&D support instruments, such as tax rebates, research grants, and the provision of infrastructure; Promote technology transfer by launching networks between large companies, SMEs, and research organizations; Facilitate an adoption of e-commerce and e-government; Provide assistance, training, and consultant services to managers and smallbusiness owners. (Svetlicic, Jaklic and Burger, 2007: 54-55). SMEs need to develop their creativity, adaptability and their orientation to capitalising on market opportunities, meeting customer satisfaction, taking advantage of the weaknesses of rivals, and developing supplier-oriented relationships. Flexibility, innovativeness, and continuous performance improvement within a cluster are factors that are becoming the elements of a new strategic approach to building a competitive advantage and developing SMEs.

Managerial responses also important in EU integration for Transition. Partly from normative standpoint but also based on actual behavior the following managerial responses do address: Be innovative, open to new concepts, accept a risk; React quickly to the market need for western and western-like product; Apply frugal marketing, don't commit resources without assessing the expected outcome of one's activities; Keep prices moderate-the affluent segment in TE is limited in scope. Don't allow prices to fluctuate excessively; Consider market niches-especially for smaller companies looking for improved margins; Diversify sources of supply to enhance the selection in terms of quality and quantity and build a wider base of providers. Purchasing is also a part of marketing; Build image, develop an active brand policy. Stay close to your customer base; Maintain consistency with respect product/service quality, nature of operations, marketing style; Develop exporting and implement marketing adaptations it requires; Use consultant to save time and resources (Sternquist and Paliwoda, 1996).

In general, without government intervention, the winners in EU integration will be large enterprises and the losers will disproportionately be SMEs.

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