

EXPLORING Entrepreneurship *SME Development in a Post-Soviet Context*

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Exploring Entrepreneurship and SME Development in a Post Soviet Context

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Foreword

This is the fifth of the TeliaSonera Institute Discussion Paper series. The Institute, which is located at the Stockholm School of Economics in Riga and is generously supported by TeliaSonera, aims to promote applied economic research in areas such as entrepreneurship, regulation, and many other aspects of market economies. This Discussion Paper, on Exploring Entrepreneurship and SME Development in a Post Soviet Context by the holder of the TeliaSonera Professorship at SSE Riga, Friederike Welter, and is an extended version of her Inaugural Lecture given on March 17, 2005.

The first four Discussions Papers were entitled: Venture Capital in Latvia, Entrepreneurship in Latvia, the New EU Regulatory Framework in Electronic Communications, and Women and Entrepreneurship in Latvia, respectively. Copies of the Discussion Papers can be ordered from the SSE Riga library.

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1. Introduction

This discussion paper is concerned with entrepreneurship and the development of small and medium-sized enterprises (SME) in Central and Eastern European (CEE) countries, where the transition from a socialist command economy towards a market-based system opened up enormous possibilities for private entrepreneurs. Since the early 1990s, private entrepreneurship gained ground, and the same applies to research on new and small enterprises [e.g., Aidis (2003, 2006), Aidis et al. (2007), Djankov et al. (2005), Dombrovsky and Uebele (2005), Lageman (1995), McIntyre and Dallago (2003), OECD (1996), Pfirmann and Walter (2002), Sauka and Welter (2007), Smallbone (1997), Smallbone and Welter (2001a, 2001b, 2003, 2006a, 2006b), Welter (1996, 1997, 2005), Welter and Smallbone (2003), Welter et al. (2004, 2006)], although some authors consider entrepreneurship research in CEE still to be a very young field [Meyer and Peng (2005)²]. In this paper I will discuss some facets of entrepreneurship in a post Soviet (or transition) context, outline important factors influencing entrepreneurship and small business development and review some of the policy issues involved in fostering entrepreneurship development. The paper draws on the results of several research projects I have undertaken in CEEs together with David Smallbone from Kingston University in the UK and colleagues from various countries.

2. Facets of Entrepreneurship in a Post Soviet Context

Is entrepreneurship different in a post Soviet context? While the basic principles governing entrepreneurship can be assumed to be the same regardless of country, there may be differences in the nature of and forms of entrepreneurship. Some research has tended to label entrepreneurship and small business in a post Soviet context as being more unproductive and consisting mainly of proprietors, who enter entrepreneurship because of necessity [e.g., Scase (1997, 2003)]. The picture emerging here is one where entrepreneurship is an activity which does not create and add value to an economy and society, thus often viewed by governments and public with suspicion. The following sections will explore facets of entrepreneurship in a post Soviet context in more detail.

There are some typical patterns of entrepreneurial behaviour to be observed in a transition context. This includes a mixture of typical strategically behaviour of new and young entrepreneurs (such as self-financing), but also patterns which are distinctive in a transition context: serial and portfolio entrepreneurship, where entrepreneurs either open one business after the other or own several ventures, a strategy of broad, but often unrelated diversification, networking and avoidance behaviour [Smallbone and Welter (2006a)]. In the following two sections, I am investigating the possible dilemmas that two of these strategies, namely networking and rule-avoiding behaviour, may pose for entrepreneurship development in a post Soviet context. I explore the question whether these behavioural patterns, which show enormous adaptive capabilities of entrepreneurs in dealing with environment, are to be assessed as positive or negative for long-term entrepreneurship development.

2.1 Is Entrepreneurship Unproductive?

Often, new and young firms in transition countries rely on specific strategic responses in order to finance more capital intensive businesses or to exploit opportunities. Networking is one of the patterns commonly used to enter markets, to find customers and to develop markets, to get access to scarce resources, to recruit employees, or to cope with the bureaucratic requirements of a highly unstable environment [cf. Smallbone and Welter (2001a), Welter and Smallbone (2003) for more examples], as the following cases illustrate. Konstantin, owner of a personnel recruitment agency in Moscow, uses networking contacts for personnel recruitment. He states that “*This is a typical Russian way*”, meaning that entrepreneurs recruit a person rather than someone to fulfil a specific function.

Party membership often proved helpful in establishing contacts which assisted entrepreneurs during the transition period in setting up their business. One such example was reported in Welter and Smallbone (2003): THW is a private company, which commenced trading in 1992. Its core activities involve selling welding equipment and related services, particularly instructing/training customers in the use of equipment, which is sold as part of the purchase package. The owner originally worked in a welding institute. He was also a leader in the Young Communist League and then an instructor. He was able to use his political connections with former YCL colleagues to get the business started, because one of his former colleagues was a leader of a bank, thus allowing the entrepreneur relatively easy access to credits. Moreover, his connection with the welding institute means that his company was able to obtain materials at slightly lower than the market price.

Networking often is coupled with gifts, where it involves people outside the kinship group. Consider this case from Uzbekistan, where a female entrepreneur opened a detergent company in 1995 [cf. Welter (2005)]. She needed to register with the Standards Office, acquire a license and have permits from local government, the local environmental health office and the fire office. In order to speed up the process, the entrepreneur paid bribes in form of presents, e.g., flowers and candy for woman, brandy for man. She accepts these ‘shadow expenditures’ as part of doing business. Being an Uzbek woman, it was not openly suggested how much she should pay but she chose to offer presents to ‘oil the wheels’ of the process. She thinks male officials are more open about the amount of bribes required from male entrepreneurs.

This kind of networking behaviour is both a source of resources as well as of practical skills in “keeping personal contacts, fixing things, knowing ways of settling problems” [Ledeneva (1998: 184)]. In this regard, several authors have described how in a fragile environment where institutional trust is lacking and norms are unstable or unfamiliar individuals use social contacts and individual networks dominated by mutual trust in order to pursue business [e.g. Manolova and Yan (2002), Peng (2000), Smallbone and Welter (2001a, 2006a), Welter and Smallbone (2003), Welter et al. (2004), Yan and Manolova (1998)]. These reciprocal contacts assist in solving diverse business problems. Entrepreneurs draw on persons and contacts they know and they trust. However, in the long run such behaviour might restrict business development and growth, as entrepreneurs limit themselves to doing business within a known circle. Peng (2003: 279) emphasises that “Especially when the informal enforcement regime is weak, trust can be easily exploited and abused”.

² The authors reviewed several journals prominent in international business studies, concluding that “Only recently have scholars begun to analyse the determinants of new firm establishment (Puffer and McCarthy 2001, Batjargal 2003) and their survival (Lyles et al. 2004).” [Meyer and Peng (2005: 602)]. However, this assessment is mainly a result of that they only included peer-reviewed journals in international business studies, neglecting small business and entrepreneurship journals and other publication outlets, where research on transition economies in Central and Eastern Europe has been prominent since the mid-1990s.

2.2 An Ethical Dilemma

Deficits in the regulative environment encourage entrepreneurial reactions, which are non-productive from a macro economic point of view because they do not contribute to overall economic development, but ensure enterprise survival, thus they are rational from the entrepreneur's point of view [Peng (2000), Smallbone and Welter (2001a)]. Entrepreneurs recur to ruleavoiding behaviour in order to cope with unforeseen pressures in a dynamic and unstable environment. 'Typical' avoidance behaviour includes, e.g., tax avoidance through setting up a second business and transferring payments between businesses, or to splitting payments to employees into a minimum wage part, which is paid officially, and bonus payments 'under the table' [Welter and Smallbone (2003)]. All this is done in order to preserve the financial resource base of the enterprise in a business environment where new and small firms experience major difficulties in accessing external finance.

However, ruleavoiding behaviour poses an ethical dilemma to entrepreneurs (and societies) which few, if none transition research studies so far have discussed. The conflict is between the type of behaviour, which the formal institutional environment requires and the behaviour, which is necessary to survive as entrepreneur. This is illustrated in several case studies collected by the author and David Smallbone during joint research projects since the mid1990s [cf. Smallbone et al. (2001), Smallbone and Welter (2001a, 2006a), Welter and Smallbone (2003), Welter et al. (2004, 2006)], indicating that the prevailing social norms in a transition context do not trigger enforcement of the 'officially' prescribed formal behaviour.

The following quotes from cases illustrate this dilemma in more detail. On the one hand, take Natalja, owning a small, successful travel agency. She has never paid taxes, because her balance sheets have not shown any profits. The price for 'noninterference' of the local tax inspectorate is *"four fully paid tourist vouchers per year for a particular tax inspector who is the firm's protector."*

On the other hand, entrepreneurs are aware of the dilemma connected with their bribing and acceptance of violating norms. For example, Olga, the owner of a small advertising and information firm, refers to the Russian labour legislation as outdated, which forces her from time to time to violate its regulations: *"But I have no choice: if I comply with all of its articles, I will be unable to develop as fast as is required by the market."* Viktor, publishing entrepreneur, takes a poor view of unofficial payments which however, according to him, are normal business conventions in his trade: *"In Moscow, the entire book world is pervaded with crime; the entire book trade is performed by 'nonregistered' down payments."* He also mentioned the need to know people, including criminals, in the trade in order to survive and grow. Nicolai, who owns a construction firm in Russia, explains that *"(..) in Russia, it's just impossible to do fair business here. No tax reduction will help. Entrepreneurs in Russia have the brains of thieves. It will take generations before civilized businessmen emerge in Russia."*

Interestingly, Ain, managing director of a wholesale company in Estonia, who uses business and social networks (Rotary Club) for his business, concedes a public influence on his networking behaviour: *"Top managers in Estonia need to be politically correct at all times since their behaviour is noticed (e.g. by press) and they are always representatives of their companies so their public image reflects on their firms."*

What is the conclusion to be taken from these examples? Obviously, in some transition contexts bribes and presents are accepted as 'usual' business norms; and entrepreneurs recur to defiance strategies in (openly) ignoring marketbased norms and values [Oliver 1991]. If in hostile environments businesses want to thrive and grow, they apparently have to rely on illegal and unethical behaviour, which benefits this single firm but is detrimental to overall economic development in the long run. The problem here is breaking the vicious circle, where initially, many firms survive and grow by using a networkbased strategy based on personal trust and informal agreements among managers and officials in order to overcome institutional uncertainties [Peng and Heath (1996)]. This only will happen if transition economies move from a relationshipbased, personalized transaction structure to a rulebased, impersonal exchange regime where "unfamiliar parties, who would have been deterred from transacting before" [Johnson et al. (2000)] can rely on third party enforcement rules and thus enter business relations with each other.

2.3 Proprietors or Entrepreneurs? The Development Potential of Entrepreneurship

Scase (1997, 2003) classified most small businesses in Central and Eastern Europe as proprietorship and not entrepreneurship. He argues that these activities, although offering employment and providing income to the owner and employees, in case there are any, these proprietors cannot contribute to economic development, as they use business income mainly for personal use instead of reinvesting it. In this regard, proprietors might be seen as noninnovative entrepreneurs owning nongrowthoriented businesses, while genuine entrepreneurs would be the ones being creative and growthoriented. Distinctions such as entrepreneurs out of economic need or because of a desire to be independent [Bögenhold (1987)] or the necessity versus opportunitybased entrepreneurship categories of the Global Entrepreneurship Monitor (GEM), based on the motives given for setting up a business, use motives to identify the growth and development potential of entrepreneurs. However, Smallbone and Welter (2003, 2006a) have questioned the applicability and usefulness of such distinctions in a transition context.

Consider this small business owner, who opened up a knitwear factory in Chisinau, Moldova, which borders Romania and Ukraine, and which is one of the poorest countries in Europe (Smallbone and Welter 2003). This entrepreneur previously worked in a stateowned company as engineer. When the transition process started, he was put on administrative leave. In order to earn an income for his family, he decided to open a knitwear business, as this had been his parttime activity for some time. Moreover, such a business did not need many resources. In terms of the concepts outlined above, this entrepreneur would certainly be seen as a proprietor and a necessitybased entrepreneur. However, his initial survival orientation quickly was replaced by growth aims. He used a diversification strategy, where he bought shirts in Poland and Belarus as shuttle trader, to overcome periods of low demands for his knitwear. When we interviewed him in 1999, he clearly expressed several ideas of how to develop his business further, but also pointed out the restrictions to business development in a Moldovan environment. Although starting his venture out of necessity, his later story clearly illustrates the development towards a more opportunitybased firm.

Regarding the proprietorentrepreneurship distinction, Smallbone and Welter (2006a) note that such a distinction is not unique for a transition country, but rather a common characteristic of many small firm owners in market economies, explaining the low growth rate in small firms. They suggest to see this issue as part of a wider discussion around the role of entrepreneurship and small business in economic development, rather than being viewed as a specifically transition issue. The authors also argue against other classification attempts such as the categories introduced by GEM. Although such approaches attempt to understand entrepreneurs according to the motives for entering entrepreneurship, as these are purported to indicate later growth prospects and business development paths, empirical evidence here is not conclusive: While some studies confirming a relation between initial business motives and later business development [e.g., Wiklund (2001)], others concluding that initial startup reasons are not a reliable predictor of later business growth [e.g., Dahlquist and Davidsson (2000), Solymossy (1997, 2005)].

This lead Smallbone and Welter (2006a) to question the applicability of such concepts in a transition context, the more as such dichotomies neglect the specifics of the context for entrepreneurship, which results in highly qualified people entering entrepreneurship because they lost their jobs: “As a result, many entrepreneurs in transition environments are well equipped to identify and exploit opportunities as they emerge over time, even if the initial reasons for becoming an entrepreneur in the first place can reasonably be described as ‘necessity.’” Moreover, the authors emphasise that entrepreneurship also is influenced by the learning experiences of individuals. Learning can result in changing motivations and business aims, it can contribute to growth intentions even in cases where entrepreneurs initially were only interested in survival and earning incomes for families; it can result in entrepreneurs identifying new opportunities and becoming more confident and also more innovative as they develop their own entrepreneurial capabilities alongside the business. To sum up, entrepreneurship in a post Soviet context is neither proprietorship nor simply necessitydriven, but the reality is more complex, showing a diverse picture of people setting up businesses for a variety of reasons, which include ‘push’ as well as ‘pull’ factors.

3. The Embeddedness of Entrepreneurship in a Post Soviet Context

Entrepreneurship is influenced by a variety of factors. We can distinguish between factors of influence on the macro level (e.g. the political, juridical and economic framework, cultural norms and religious traditions), on the meso level (e.g. business associations, industryspecific practices and codes of conduct, standardization and trade unions) and on the micro level such as personal beliefs and values, educational background and professional experiences and network support (potential) entrepreneurs can draw on. Most entrepreneurship research tends to focus on individual and micro level influences. Only recently there has been a shift towards linking entrepreneurship to the overall institutional framework. For example, Solymossy (2005) argues for a shift away from considering personal influences such as motivations towards other, environmental factors and a need to analyse how they influence the process of entrepreneurship: “This approach parallels current progress in the entrepreneurship field; there has been a movement away from focusing only on the entrepreneurial individual and increasing focus on other factors

affecting entrepreneurial activity and success.” Such external influences on entrepreneurship gain particular importance in fragile and dynamic environments such as new sectors or during the transformation period in Central and Eastern Europe. In this context, institutional forces influence the nature and pace of entrepreneurship. This takes on special importance, when comparing entrepreneurial behaviour in different contexts. In the following sections, I briefly will outline and discuss some important conditions for entrepreneurship in a post Soviet context, in order to illustrate its embeddedness.

3.1 The Historical Context for Contemporary Entrepreneurship Development

Three main factors are important in explaining today’s level of entrepreneurship and the starting conditions in the early 1990s: the state of presocialist entrepreneurship development in connection with the personal background in entrepreneurship and entrepreneurship developments during Soviet times [cf. Mugler (2000), Smallbone and Welter (2001a), Welter (1996)].

For example, in countries such as Poland, Czechoslovakia and Hungary, a strong prewar tradition in private entrepreneurship existed. Russia on the other hand always was dominated by state and bureaucratic entrepreneurship. Prewar industrialisation traditions helped in upholding entrepreneurial traditions. For Central European countries, various studies have estimated that the offspring of presocialist entrepreneurs accounted for between 25 and 40% of all private entrepreneurship during early transition [Lageman (1995: 114)] whilst in a 1997 survey in Ukraine, Belarus and Moldova, ‘family background’ was only mentioned by a handful of respondents [Smallbone and Welter (2001a)]. In Hungary, prewar entrepreneurs and their offspring had either been (partly) selfemployed in the second economy, or they had often occupied leading positions in state enterprises during the socialist period [Szelenyi (1988)]. This appears to confirm a thesis modelled on Max Weber’s research stating that cultural entrepreneurial traditions could be transported via highlevel professional positions, where individuals ‘parked’ their entrepreneurial skills, but they were also able to practise insofar as they were allowed to practise autonomous decisionmaking involving limited risktaking [Szelenyi (1988)].

As regards the context during Soviet times, Poland and Hungary started early on reforms, allowing for both some private ownership of firms and various forms of private entrepreneurial activities and managerial freedom within state enterprises [e.g., Welter (1996), OECD (1996)]. For example, Poland (re)introduced private craft enterprises in 1972, some years later the government allowed for so-called Polonia enterprises, i.e., joint ventures of Polish emigrants; and at the beginning of the 1980s it legally guaranteed the existence of private enterprises. Hungary experimented with various forms of private ownership, mostly within the framework of state enterprises, where employees were allowed to use machines and resources to manufacture for their own use, although most of these forms did not work out in the way the government intended to.

On the other hand, in countries such as Czechoslovakia, the Baltic Soviet Republics and the other Soviet republics no form of entrepreneurship was allowed; and respective reforms only began with Gorbachev in the mid1980s. Here as well as in early reform countries, where the legal private sector had to fight political modes restricting, e.g., the number of employed persons within a private firm, socialism

contributed to the emergence of the so-called second economy [Dallago (1990)]. 'Entrepreneurial' behaviour in such environments was mainly restricted to illegal activities such as moonlighting, the unofficial use of state machinery for private aims and tolerated theft at the working place [Dallago (1990), Smallbone and Welter (2001a)], although some functions in state firms such as the *tolkach* who was responsible for securing resources [Kerblay (1977), Harter (1997)], had entrepreneurial elements because they allowed for limited decisionmaking.

Interestingly, there appears to be an influence of illegal entrepreneurial activities on today's entrepreneurs. A paper by Dombrovsky and Welter (2006) shows for Latvia that 25 percent of all respondents reported that some relative of theirs was an entrepreneur during the Soviet times. While this is understandably lower than the percentage of respondents reporting a relative being an entrepreneur after independence (37%), the implications, nevertheless, are remarkable. This implies that there were substantial underground profitseeking activities in the Soviet Union, which underlines the proposition put forward by Rehn and Taalas (2004) namely that Soviet entrepreneurship is a complex phenomenon and has to be interpreted in its everyday context. It also underlines in the light of an ongoing discussion of the antecedents of entrepreneurship in a transition context, a need to take the 'historical' dimension into account and to look at entrepreneurship in its social and historical context.

3.2 A Soviet Legacy?

In this section I will turn to discuss possible cultural influences on entrepreneurship development in a post Soviet context, asking whether there is a Soviet legacy influencing contemporary patterns of entrepreneurship. Some see a Soviet legacy in the 'homo sovieticus', who is characterised by a lack of initiative, risk propensity and a weak responsibility for his/her actions, all of which appear to contradict characteristics of an idealtypic entrepreneur. There has been a controversial debate around the extent to which Soviet society fostered this 'homo sovieticus' and how this might have affected entrepreneurship in the transition process. It very much resembles the 'nature' versus 'nurture' debate of entrepreneurship teaching. Soviets themselves recognised this phenomenon [cf. the manifold descriptions in the novel written by Sinovjev (1987)]. During the transition period, most researchers saw individual behaviour as resulting mainly from situational influences compared to attitudinal ones [e.g., Shiller et al. (1992)], thus rejecting the influence of 'mentalities'.

Another discussion centres on the potential of entrepreneurial activities as carried out during the socialist period to 'breed capitalism' [Kornai (1992)]. Even though the transformation process changed the rules for entrepreneurs, some forms of entrepreneurship and entrepreneurial activities survived, contributing a distinctive experience of entrepreneurship into the transition period. In this context, some studies illustrate the influence of illegal entrepreneurial experience on today's entrepreneurship. For example, Earle and Sakova (1999) find that owning a sidebusiness in the pretransition year of 1988 increased the probability of private business ownership in transition context in six countries, namely Bulgaria, Czech Republic, Hungary, Poland, Russia and Slovakia. Given that entrepreneurship was forbidden in four of them, namely Bulgaria, the Czech and Slovak Republics and Russia, this appears to confirm the seedbed hypothesis.

Nevertheless, some researchers are highly critical, regarding the potential of a Soviettype system to produce entrepreneurship at all [e.g., Dallago 1997, Scase (2003)], whilst others [e.g., Rehn and Taalas (2004)] emphasize the entrepreneurial nature of everyday life in a Soviet context, which lead them to understand bargaining and bartering in order to cope with shortages as Soviet entrepreneurial activities. Others suggest a more differentiated approach by assessing the potential of different categories of activities [e.g., Welter (1996)].

At a first glance there appears to be but few development potential in rentseeking and mainly shortterm oriented illegal activities as dominated the entrepreneurial spectrum in countries such as Czechoslovakia and the Baltic states, where entrepreneurship was forbidden. Similarly, parttime entrepreneurial activities, which mainly were aimed at providing additional incomes such as the Hungarian innerfirm economic brigades, might be expected to vanish in a marketbased economy. Scase explains this in terms of the proprietorship nature of such activities, where the motives for taking up and continuing such activities were often rooted in past experiences of state socialism, namely a quest for personal autonomy. Proprietorship offered personal autonomy [Scase [2003: 69]]: "Even under state socialism, informal patterns of trading were not only the mechanisms for acquiring additional economic resources, but also the means according to which individuals could express a certain degree of psychological independence and personal autonomy."

Aidis and van Praag (in press) analyse whether illegal entrepreneurship experience can be a predictor for the level of business performance and motivations of private 'legal' business owners in a transition context, expecting a positive relationship. Illegal entrepreneurship is considered a means to obtain tacit knowledge and contacts which would help entrepreneurs in the transition period to overcome institutional deficits. Their results indicate for Lithuania that illegal entrepreneurship cannot be associated with business performance in general. However, as there is strong evidence for a positive relationship between any illegal experiences and intentions to continue and grow a business, they conclude that illegal entrepreneurial experiences can be understood as a signal for a source of motivation.

Independent entrepreneurial activities, such as the legal craft firms in Poland or private economic cooperatives in Hungary, might have shown more potential to develop into marketbased entrepreneurial ventures. However, their owners often had problems in adapting to market conditions, in particular because during socialist time, they often held monopolies on their respective markets [cf. Smallbone and Welter (2006a)]. Nevertheless, this is less a signal for a specific Soviet mentality as more an indicator for a lack of management knowledge.

Entrepreneurial activities within state organisations as well as party membership or membership in communist youth organisations fostered the development of the so-called nomenclature businesses during the transition period [Smallbone and Welter 2001a], which mainly is based on their links and connections within the socialist system. During the first years of transition, all over Eastern Europe both government officials and party members were quick to privatise state enterprises, often in order to keep their influence, but also to realise opportunities [e.g., for Hungary Voszka (1991, 1994)].

Overall, only few studies have been conducted in order to analyse Soviet legacies. The examples of ruleavoiding behaviour as illustrated above would let us assume there is a Soviet legacy, which sometimes is referred to as the 'legacy of noncompliance' [Feige (1997: 28)]. Several studies on transition economies [e.g., Gustafson (1999), Smallbone and Welter (2001a)] indicate that an inadequate formal institutional framework during the transition period often reenforced existing norms of behaviour. However, most researchers would accept that there is a legacy in learned behaviours, which might result in entrepreneurs being used to working around the rules. One such example concerns the parallel circuits [Kerblay (1977)] of the Soviet period, which were network relations set up by the so-called *tolkach* between state enterprises in order to shift and obtain such resources as were required to fulfil plan goals. Of course, such activities were illegal in the Soviet system; but the state tolerated them – as it tolerated some of the illegal entrepreneurial activities, which later on often became the 'seedbed' for entrepreneurship development.

4. Challenges for Entrepreneurship and Small Business Development in a Post Soviet Environment³

Given the strong impact the context and environment have on entrepreneurship development, I finally turn to review some of the challenges in developing entrepreneurship and small business in a post Soviet environment. Most would agree on that entrepreneurship has a potentially important role to play in the transition process [Smallbone and Welter (2001b)], as it can contribute to the wider social change and democratisation of society; it can create employment possibilities and absorb some of the surplus labour from privatized ventures; it can create new business fields and contribute to the development of service and knowledgebased industries as well as to innovation. In this context, governments set the rules for entrepreneurship, as Solymossy (2005: 516) notes: "Regardless of whether initiated by push or pull motivation, an opportunity is required to establish entrepreneurship. The opportunity must convey the hope of an economic profit....The ability to capitalize on opportunities is enhanced or retarded by governmental policies and resource availability."

In general, support for entrepreneurs and SMEs draws on different philosophies [cf. Welter (1997)]: either governments tend to follow a more direct approach or they prefer an indirect one. The latter concept is oriented towards improving the overall environment and framework for entrepreneurship while a direct approach is aimed at solving internal and external constraints at firm level. For example, with respect to financing problems of SMEs and new entrepreneurs an indirect approach would try to improve the financing system as a whole by strengthening the banking system and orienting it towards entrepreneurs in small and new firms as a target group while a direct approach would try to solve the individual firm's financial problems by introducing special credit lines.

The arguments used to justify entrepreneurship policies and SME support, play an important role in determining the respective approach. Sizerelated disadvantages and market failures are the standard – traditional – arguments in Western countries resulting in firmlevel pro-grammes in

different fields of support. In a transition context, such a direct approach would be necessary in the early years of the transition because of system failures, e.g., in the financing system. Besides, direct approaches are the easiest to design and implement at least in a superficially way. An indirect policy and support strategy would be more important in the long run because of the need to adjust the institutional framework as a whole. Most transition countries therefore understandably opted for the direct approach as an evidence of the immediate needs of new entrepreneurs in the first stage of transition. To a certain extent however this emphasis on direct support also appears to be a result of multilateral and bilateral aid offered to countries in transition [Bateman (2000a, 2000b)].

Therefore during the transition process in CEE we can observe different time patterns in SME support and entrepreneurship policies. Initially, most transition economies introduced support measures aimed at individual entrepreneurs and their ventures, in order to level the playing field for new and small ventures. Increasing political awareness of the importance of entrepreneurship characterises a second phase, which resulted in overall national programmes or strategies being drafted and a shift towards the general conditions relevant for economic development. Governments then should (ideally) concentrate on designing an integrated strategy of indirect and direct support aimed at developing entrepreneurship and SMEs.

Today, we can observe different policy agendas in CEEs depending on the respective state of transition [Smallbone and Welter (2001b, 2006b)]. In so-called 'early stage transition countries', examples of which include Belarus, Ukraine, Moldova, most of the Central Asian republics and parts of Russia, entrepreneurs' main problems arise from an inadequate legal frame and overall lacking institutional infrastructure for entrepreneurship and small business development. Empirical results show that entrepreneurs in such countries often complain about high tax burdens, frequent changes in the legal system and very bureaucratic entry and reporting rules [Smallbone et al. (2001)]. Overall, governments in such environments play a low value on entrepreneurship, often seeing entrepreneurs as 'cash cows'. For entrepreneurship to flourish in the long run, governments will have to recognise the value entrepreneurs will add to their economies and societies, while entrepreneurs will have to learn to 'behave' accordingly to market rules.

CEEs in a later stage of transition, for example the new member states of the European Union, face different challenges. Besides their preaccession preparations, which included raising the knowledge level of private businesses concerning the implications of EUaccession, this refers to creating regional and local policies for fostering entrepreneurship and improving the effectiveness of existing business support networks.

Overall, entrepreneurship development needs willing and capable entrepreneurs and an enabling environment. In this context, an important challenge governments in CEEs face is the design of appropriate policies and support mechanism. Good or bad models for entrepreneurship and SME support in transition countries are difficult to identify because of the political, economic and cultural environments in different countries influencing the outcome of these programmes: „...there are considerable dangers in transposing institutional and organisational paradigms into different cultures with different ideologies and in different time frames. Western banking practice, for example, embodies several hundred years of incremental development of market economies

³ This section draws on Welter (1997).

through various stages, while the models of local enterprise development offered to Central and Eastern Europe have evolved over two decades or more. Furthermore, many of these models remain unproven; still others cannot yet be said to be fully successful even in the industrial nations. [Gibb (1995)]. One problem which became apparent in many CEEs during the late 1990s resulted from a heavy reliance on donor support for financing business support infrastructures. As soon as the outside assistance stopped, many of these centres failed to achieve financial viability and they consequently had to offer their services to profitable clients, leaving behind their original target groups of new and small firms (Bateman 2000a). This sustainability question often resulted from national governments' limited budgets in spite of their (stated or actual) awareness of SMEs' importance and their willingness to support SMEs. Donors could aggravate this when as a consequence of available donor funds entrepreneurship policies and SME support in transition economies were no longer need-driven but resource-driven [Gibb and Havers (1996: 30)].

The implication to be drawn for fostering entrepreneurship is that there is a need to view entrepreneurship in its social context as well as to design a needs-based and evidence-based policy strategy for supporting entrepreneurs and small businesses.

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