

Revisiting entrepreneurship in a transition context

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Abstract: This paper aims to critically review entrepreneurship in a transition context, analyzing its nature today as compared to two decades earlier (i.e., at the start of transition). The methodology used in the current paper is predominantly based on a literature review, but since both authors have been heavily involved in empirical investigation as well as policy-related consulting in transition countries, this experience is drawn upon where appropriate. In this paper, we present preliminary findings of our review. The review can make two contributions to the entrepreneurship field. First, we demonstrate the value of considering entrepreneurship as a societal phenomenon, which draws attention to antecedents and outcomes of entrepreneurial behaviour. Second and related to this, we contribute to the recent debate on the importance of context for entrepreneurship.

Debating points:

- In an approach that emphasises context what is the role for human agency?
- Are studies of entrepreneurship in transition really part of the mainstream?
- James Curran once described transition studies as theoretically bereft and empirically dubious. Do you agree with his description?

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Introduction

Two decades after formerly socialist countries started on their path towards market economies and a decade after Smallbone and Welter (2001) published a much-cited paper on the distinctiveness of entrepreneurship in a transition context, it is time to take stock and look ahead, asking whether and in which ways entrepreneurship in this context is still distinctive and what are the implications for both entrepreneurship research and entrepreneurship policy. In relation to transition contexts, two major events have occurred since 2001 that have important potential implications for entrepreneurship in a transition or post-transition context. The first is the enlargement of the European Union in 2005 and 2007, which resulted in countries such as Poland, Hungary, Czech Republic etc. being drawn into a grouping that was strongly market-oriented. This not only signalled their intentions with regards to on-going market reform but also gave them access to resources (both financial and technical) to contribute to these restructuring processes. The second major event that has taken place during this period is the rapid emergence of China; not that this started in 2001 but the 13 years since then has seen China increasing its activity on world markets, with private sector development at the forefront. However, China has its own version of private enterprise which presents some differences, both with mature market economies but also with transition economies in Central and Eastern Europe (Smallbone and Welter 2012b; Yang 2007).

The result of these two major events is to increase the heterogeneity of experience that exists with regards to entrepreneurship in transition economies. One element in the conceptualisation of entrepreneurship under transition developed in Smallbone and Welter (2001) was the nature of the inheritance from the socialist period; the point being made that, although some forms of entrepreneurship were tolerated in a few Central European countries, by and large the inheritance of the socialist period in this regard took the form of informal activity or a parallel economy, which strictly speaking was illegal. Cooperatives and state-owned enterprises were not averse to making use of products and services generated in the second economy, in their desperate attempts to meet planning targets and, therefore, to avoid sanctions. Hence, we concluded that although entrepreneurship was, in the formal sense, not explicitly practiced, there were sections in society in these countries where enterprising was developing as an idea; so that when the Soviet Union collapsed there were energetic, enterprising people ready to come forward.

The second element in the conceptualisation of entrepreneurship under transition developed in the 2001 paper was that of the different forms of entrepreneurship that emerged once transition started, including self-employment. Self-employment often provided a means of self-help thereby contributing to social inclusion. This was a form of activity that was quite popular amongst workers from former state-owned enterprises that were essentially on administrative leave. Because of labour market rules and regulations they were forced into the informal economy and would be seen as necessity-driven, which most of them were at the outset. The problem with such language is that it tends to imply that once characterised as necessity-driven that characterisation will not change; and that is demonstrably not the case.

A first review of the literature reveals little consideration of conceptualisations of entrepreneurship in a transition context, with the notable exception of a few articles and special issues where editorials focused on more theoretical grounding of entrepreneurship research in emerging economies (Ahlstrom and Bruton 2010; Bruton, Ahlstrom and Li 2010; Bruton, Ahlstrom and Obloj 2008; Smallbone, Welter and Ateljevic 2014). The question arises as to whether entrepreneurship researchers nowadays assume more similarities than differences between a mature market context and a transition context. Therefore, this paper aims to critically review entrepreneurship in a transition context, analyzing its nature today as compared to two decades earlier (i.e., at the start of transition) and asking for the implications for the entrepreneurship field.

Methodology and conceptual framework

A full answer to the question of what is distinctive about entrepreneurship in transition economies requires some differentiation between contexts. It is only recently, that entrepreneurship scholars have started paying more attention to the context in which entrepreneurship takes place. Context is seen to simultaneously providing opportunities and restricting actions of individuals (Welter 2011). It becomes “part of the story” (Zahra and Wright 2011: 72), thus contributing to theory building.

This paper reviews entrepreneurship in a (post-)transition context against the understanding of context as introduced by Welter (2011) who suggested different dimensions of context along a continuum of where entrepreneurship takes place and when this happens. The “where” dimension reflects the manifold locations of entrepreneurship, namely social, spatial and institutional. Social context includes the relations of individuals, be they networks, families, households or friends. The spatial

context covers the physical and geographical environment, the institutional context the regulatory and normative environment. These contexts overlap; for example the social context (networks, family, households) and institutional contexts (laws, norms, regulations) both have a spatial dimension. The “when” dimension refers to historical and temporal contexts, thus capturing changes over time and introducing a dynamic perspective. In our paper, we consider the where and when dimensions of context. Our view of the relationship between contexts and entrepreneurship is dynamic and reciprocal: entrepreneurship is affected by contexts as they exist today and as they have existed before, but entrepreneurship also affects contexts and thus contributes to changing contexts overtime. With this, we aim to contribute to the emerging debate on contextualizing entrepreneurship (research), specifically drawing out the implications of considering context(s) such as the transition context for our entrepreneurship theories and methods.

The methodology used in the current paper is predominantly based on a literature review, but since both authors have been heavily involved in empirical investigation as well as policy-related consulting in transition countries, this experience is drawn upon where appropriate. Our review includes any fresh examinations of some of the established themes reported in the 2001 paper but, more importantly, it also seeks to identify any new themes and new interpretations which have emerged during this time. Since this is work in progress, we present preliminary results, mapped against the context framework outlined above.

Reviewing entrepreneurship in transition economies through a context lens

Historical contexts: Are there entrepreneurial legacies from socialism?

Smallbone and Welter (2001) emphasized the *nature of the inheritance from the socialist period*; the point being made that, although some forms of entrepreneurship were tolerated in a few Central European countries, by and large the inheritance of the socialist period in this regard took the form of informal activity or a parallel economy, which strictly speaking was illegal. Cooperatives and state-owned enterprises were not averse to making use of products and services generated in the second economy, in their desperate attempts to meet planning targets and, therefore, to avoid sanctions. Hence, we concluded that although entrepreneurship was, in the formal sense, not explicitly practiced, there were sections in society in these countries where entrepreneurship was developing as an idea; so that when the Soviet Union collapsed there were energetic, enterprising people ready to come forward.

Since then, several studies have explored the potential of entrepreneurial activities conducted illegally during the Soviet period which provided a foundation for more substantial and productive entrepreneurship post-socialism, thus contributing empirical evidence and a positive stance to the oftentimes negatively understood hypothesis of Soviet legacies. For the Soviet Union, Rehn and Taalas (2004) showed how entrepreneurial behaviour flourished in the daily lives of individuals during the Soviet period, struggling to cope with the material shortages of the Soviet system. As a result, the authors suggested that the former USSR may be seen as a highly entrepreneurial society.

Guariglia and Kim (2006) find that one quarter of newly self-employed entrepreneurs in Russia had been 'moonlighting' in the past. Aidis and van Praag (2007) confirm the existence of positive benefits from illegal entrepreneurial experiences acquired under socialism in supporting entrepreneurship and economic development in the transition period. Moreover, research on shuttle traders or 'trader-tourists' has consistently shown their roots in Soviet times (Bruns, Miggelbrink and Müller 2011; Egbert 2006; Smallbone and Welter 2012a; Wallace, Shmulyar and Bedzir 1999; Yukseker 2007).

Some research suggests a "transgenerational" transmission of entrepreneurship, either through social positions or through role models within family, from socialist to post-socialist times. Social status during Soviet times appeared to have played a role also for post-socialist entrepreneurship as mentioned in our 2001 paper for the example of nomenclature entrepreneurs with a communist party background. Djankov, Miguel, Quian, Roland and Zhuravskaya (2005) showed that parents of current entrepreneurs in Russia were less likely to have been workers during Soviet times. Dombrovsky and Welter (2006), in their study on entrepreneurs in Latvia, showed that a quarter of all respondents reported a relative of theirs as entrepreneur during the Soviet times. This illustrates not only that there were substantial underground profit-seeking activities in the Soviet Union, but also that this affected post-socialist entrepreneurship even in those countries where private entrepreneurship during socialism was forbidden. However, Dombrovsky and Welter (2006) also demonstrated that the effect of having a relative who was an entrepreneur after independence increases the likelihood of being an entrepreneur by more than twice as much as having a relative, who was an entrepreneur in Soviet times. This indicates the greater importance of entrepreneurial role models from the post-socialist period, which may be viewed as encouraging from the point of view of the development of 'productive' entrepreneurship.

Institutional contexts and entrepreneurship

Strong external environmental influences have been a recurring theme in studies of entrepreneurship in emerging market economies. This is reflected in the growing number of studies which have emphasized the institutional contexts for entrepreneurship (Aidis 2005; Aidis, Estrin and Mickiewicz 2008; Bruton and Ahlstrom 2003; Manolova, Eunni and Gyoshev 2008; Manolova and Yan 2002; Meyer, Estrin, Bhaumik and Peng 2009; Peng 2003; Peng and Heath 1996; Peng and Luo 2000; Tan 2002; Welter and Smallbone 2003; Yan and Manolova 1998). Studies have progressed to demonstrating the simultaneously positive and negative influence of the legal environment: Kim and Li (2014) distinguish between regulatory and protective functions of legal institutions, illustrating their divergent impact on entrepreneurship in emerging market economies, together with the role of trust in complementing or substituting for legal loopholes (also see Welter 2012; Welter and Smallbone 2011). Although in *any* context entrepreneurship is influenced by a dynamic interrelationship between individual characteristics and external conditions, in situations where the formal institutional framework is only partially installed and/or has major institutional deficiencies, the institutional context and the interplay between formal and informal institutions can become a critical factor. The specificities of the external environment in emerging economies make it a potentially more dominant influence on entrepreneurship than in a more stable business context.

Where the environment is characterise by a high level of uncertainty, associated with rapidly changing external conditions and major institutional deficiencies (Ahlstrom and Bruton 2010), the role of both formal and informal institutions is often a constraining one. This might encourage illegal or semi-legal activities (Baumol 1990) as reflected in the example of cross-border entrepreneurship in post-socialist countries, where petty traders and small-scale entrepreneurs circumvent customs and excessive border controls (Welter and Smallbone 2009). At the same time, institutional voids can also offer opportunities for entrepreneurs as has been shown for business service firms in the Ukraine in the early 1990s (Smallbone, Welter, Voytovich and Egorov 2010). In this context, entrepreneurs frequently drew on previously learned behaviour, based on culturally embedded informal institutions, such as 'blat' or 'guanxi' (Puffer, McCarthy and Boisot 2010; Smallbone and Welter 2009a), indicating the strong role of the social context for entrepreneurship in transition countries, which we will elaborate in more detail in the next section.

Puffer et al. (2010) suggest that countries such as Russia and China might develop unique balances between formal and informal institutions that better fit their (historical) contexts and situations. This is taken up by Smallbone and Welter (2012b) who compare institutional change and entrepreneurship across three country settings, highlighting the interdependencies between institutional and temporal contexts: new EU member states from Central and Eastern Europe, the Commonwealth of Independent States (CIS) which consists of former Soviet republics and China. The authors highlight distinctive paths of institutional change and entrepreneurship development. In new member states, institutional change resulting from the accession to the European Union fostered entrepreneurship development. In CIS countries, persisting institutional deficiencies have a predominately negative effect on entrepreneurship because of the unsupportive wider political context. The environment for entrepreneurship is typically – still – difficult; government has little interest in promoting and support new and small businesses and/or does not have the technical knowledge and capacity to provide framework conditions to facilitate business ownership (Smallbone and Welter 2009b). In other words: the hostile institutional context restricts the development of entrepreneurship and also its nature.

Clearly a major barrier to entrepreneurship in such countries results from deficiencies in the institutional environment (Aidis, Estrin and Mickiewicz 2008). For example, in Russia the 2012 IFC surveys show that out of 15 areas of the business environment identified, private business owners identified tax rate as the biggest obstacle, followed by access to finance and then corruption. More than 36 percent of respondents recorded tax rates as the biggest obstacle, compared to around 10 percent of those in firms surveyed in other countries. In this regard, the pattern has not changed radically since the 1990s as reported in the 2001 paper. As the 2001 paper showed, corruption is a major issue in countries such as Russia, i.e., in early stages of transition. It is almost endemic within these societies and is allegedly going to the top of the country not just affecting petty officials. Bribes and corruption when applied to hard-pressed small firm owners is undoubtedly a constraint on business development. What it means is that resources are forcibly being allocated to activities that are non-productive in terms of the company. Corruption is not a new problem, having been identified in the 2001 study, although it is probably true to say that we know rather more about the causes of informality and the context in which it occurs than we did 13 or 14 years ago. It was a characteristic inherited from Soviet times and exacerbated by high levels of taxation and, in the early years, continual changes in tax rates under the tax regime, which made compliance relatively expensive (Estrin and Prevezer 2010). It can be argued that a

combination of these factors forced more small firms into the informal sector than would otherwise have occurred (Bruns, Miggelbrink and Müller 2011; Polese and Rodgers 2011). A point to stress is that in such institutional contexts there is no clear black and white distinction between formal and informal. What this also demonstrates is the linked nature of many of these constraints. In this case it is between corruption and informal activity, which when facing firms that are fully legally compliant may cause unfair competition as a result of the informal enterprises operating with lower costs.

In China, on the other hand, neither the state nor entrepreneurs show much interest in institutional change, instead they prefer to explore what they can do within the context of the (ambiguous) institutions that exist (Smallbone and Welter 2012b). This results in 'double entrepreneurship' (Yang, 2007) which incorporates an economic and a socio-political dimension, because entrepreneurs in China need to be able to both make a profit and to obtain socio-political security.

The interface of social, spatial and institutional contexts

One theme which explains part of the distinctiveness of entrepreneurship in post-socialist economies concerns the interface of social, spatial and institutional contexts, which results in distinctive enterprise characteristics and entrepreneurial strategies (Smallbone and Welter 2001; Welter and Smallbone 2011) such as multiple ownership, serial entrepreneurship, unrelated diversification and a heavy use of networking.

The emphasis on the importance of networks and networking has been a consistent feature of studies on entrepreneurship in a transition context. This particularly refers to the more informal and personal relations, which can provide a mechanism for personal trust-based relations replacing what are, in practice, very low levels of institutional trust (Welter and Smallbone 2006). This is a feature that still is highlighted in empirically-based studies (Batjargal 2003, 2006, 2010; Ledeneva 1998, 2008; Lovell, Ledeneva and Rogachevskii 2000; McCarthy, Puffer, Dunlap and Jaeger 2012; Polese and Rodgers 2011; Puffer, McCarthy and Boisot 2010; Rasanayagam 2011; Rehn and Taalas 2004). However, networking, in the form of blat, apparently has changed its nature. Onoshchenko and Williams (2013), for example, based on 200 face-to-face interviews from a Ukrainian city, illustrate how blat which was friendly help during the socialist era, has become a commodity bought and sold for illicit monetary payments.

Another legacy from the Soviet period, namely the 'legacy of non-compliance', together with institutional voids fostered the emergence of a vibrant informal economy in most

post-Soviet economies, although this lost (some) momentum in the years preceding Accession in those countries which joined the European Union from 2004 onwards. Such informal activities include a wide variety of activities on a 'cash-in-hand-basis', which may be viewed as specific features of the post-Soviet period, including shuttle trading and the widespread use of informal employment. In this regard, several studies focus on informal entrepreneurship and its contribution to development in a transition context (De Castro, Khavul and Bruton 2014; Lee and Hung 2014; Morris 2011; O'Brien 2012; Williams Colin and Nadin 2013; Xheneti, Smallbone and Welter 2013; Yukseker 2007). Williams (2005) finds informal activities to be a widespread phenomenon with just two thirds of households in post-Soviet economies relying on incomes earned in the formal sector. Williams et al. (2007) illustrated that 51% of all Ukrainian households reliant on informal strategies to earn income are multiple-earner households; only 6% are no-earner households (i.e., with no employment possibilities outside the informal sector), whilst nearly two thirds of self-employed entrepreneurs were operating without a licence, that is informally and illegally.

Recently and in line with a general move towards considering the wider socio-spatial context for entrepreneurship such as families, households, communities, research also has studied households and enterprising families in a transition context (Welter and Xheneti 2013; Xheneti, Smallbone and Welter 2013). For example, related studies show households in a transition context partaking in 'multiple economies' (Pavlovskaya 2004; Smith 2002; Smith and Stenning 2006). Pavlovskaya (2004), in her study of Moscow households emphasises the 'multiple economies' existing during the transition period, including formal and informal, private and state as well as monetised and non-monetised spheres. The author points out that these 'sub-economies' should not be seen as dichotomies, but rather complementary to one another; with boundaries that are permeable and fuzzy. This co-existence of legal and illegal / grey activities has been illustrated in several empirical studies which have shown that most new and small firms involved in productive and rent seeking activities at the same time (Rehn and Taalas 2004; Smallbone and Welter 2009b).

This has consequences for our understanding of entrepreneurial activities in transition environments, suggesting that informal activities can be a seedbed for more substantial entrepreneurial ventures, as argued by several authors (Guariglia and Kim 2006; Smallbone and Welter 2006). Bennett and Estrin (2007), for example, show how informal activities allow entrepreneurs to explore the profitability of a venture idea by using them as a stepping stone, allowing them to experiment cheaply in an uncertain

environment. Recent research undertaken by the authors on petty trading activity in EU border regions has distinguished between, on the one hand, those driven by proprietorship-type motivation (Scase 2003), where individuals lack the interest and ability towards entrepreneurship and, on the other, more entrepreneurial individuals whose motivation, drive and resourcefulness makes them nascent entrepreneurs (Welter and Smallbone 2009). In this regard, it is important to recognise the heterogeneity of informal entrepreneurial activity that exists, only some of which is likely to have real potential as a development route into more formal forms of entrepreneurship. This has potentially interesting implications for theorising and empirically analysing entrepreneurship in a (post-)transition context.

The temporal dimension

Smallbone and Welter (2001) included an extensive discussion of concepts of necessity-driven and opportunity-driven entrepreneurship, supported by Scase's distinction between entrepreneurship and proprietorship (Scase 1997, 2000). The main point we emphasised in 2001 is the danger of becoming too deterministic, because starting up a new business or expanding an existing business is a process that may be influenced by changes in individuals associated with learning, but also with the fact that transition conditions, particularly in the early stages are often very volatile. The external environment could also be a change element in circumstances where changes took place. Some entrepreneurs that were necessity-driven at start-up became more opportunity-oriented subsequently. This is a debate that is ongoing and which indicates the importance of looking at entrepreneurship in a transition context from a dynamic perspective (Block and Koellinger 2009; Smallbone and Welter 2003; Tipu 2012; Vershinina and Rodionova 2011; Welter and Smallbone 2008, 2009; Williams Colin 2010; Williams Colin and Nadin 2013).

For example in Estonia regular surveys have described the change over time in the barriers to business development reported by entrepreneurs. Decreasing emphasis has been placed on regulatory and administrative barriers and greater emphasis over time has been placed on barriers such as competition from other small firms and competition with imports. Both may be seen as indicators of the emergence of the market-based economy.

Welter and Smallbone (2010) look at institutional change in relation to women entrepreneurs in Central and Eastern Europe and Central Asia. While institutional change such as the introduction of private property rights created opportunity fields for

entrepreneurial men and women alike, it typically had a negative impact on women, because of the effect of a change in family policies on the subsidies for state enterprise kindergartens, which led to a lack of public childcare facilities. The authors also illustrate the diversity of behavioural responses by women to deal with the post-Soviet traditional gender role, including some who openly defied post-Soviet gender roles, while others accepted them, at least on the surface. In a post-Soviet context, business is typically considered a predominantly male territory, requiring so-called male qualities, such as strength and assertiveness. In such circumstances, women entrepreneurs break out of norms ascribing them specific roles and behaviours.

In relation to the context framework set out above, all this emphasizes change as an important factor for explaining entrepreneurship and its distinctiveness in a transition context. Overall, this temporal dimension of entrepreneurship requires further study.

Outlook: The evolution of the field – a move towards the mainstream?

Not surprisingly perhaps, one of the characteristics of studies that have been undertaken since 2001 is that they tend to be more specialised. Earlier studies in the mid-1990s studied the “basics” of entrepreneurship emergence and SME development, such survival and growth of SMEs, for example. They contrast with studies undertaken ten years and later on more sophisticated and current topics such as trust (Welter and Smallbone 2006). Furthermore, instead of narrowly focusing on transition countries alone, transition economies were drawn into larger projects that were designed to incorporate a variety of different operating environments. The effect was to widen the net of researchers that have undertaken research or became interested in entrepreneurship in these transition environments. This contrasted with the early 1990s when, although a track might be included in a conference, the number of participants in entrepreneurship and transition tracks was typically less than in other topics. One might suggest that the transition context has become mainstreamed, with more researchers from outside the transition environment gaining experience of entrepreneurship in these conditions. At the same time, centres of research on the transition countries have emerged, which in itself has contributed significantly to the number of people interested in this subject. Also, research methods have changed, partly because overtime the quantity and quality of secondary databases has improved, but also time has enabled an accumulation of research evidence which is now several times greater than it was in 2001. One of the opportunities that this has presented is to examine changes over time, thus allowing us to study the temporal context, together with, e.g., changes in the

institutional context. Moreover, as one would expect, the post-2001 period has seen a growing number of papers critically assessing earlier work such as for example, the critique of what is now seen as oversimplified surveys of barriers facing firms (Doern 2009; Doern and Goss 2012).

Our preliminary findings demonstrate that entrepreneurship in transition economies has many distinctive features, which are associated with the historical legacy from the socialist period as well as the specific institutional, social and spatial contexts. This distinctiveness of entrepreneurship in the transition context can now be considered part of the main stream within the field of entrepreneurship as the role of context is increasingly realised. At the same time, there is no single “transition” context. Since 2001 when the first article was published there has been increased differentiation between the former Soviet bloc and those post-socialist countries which now are member states of the European Union. In addition, China has emerged on the world stage with an emphasis on entrepreneurship. Thus, it is important to recognise the role of context in shaping the pace of entrepreneurship, both in emerging and mature market economies.

At the same time, it is important to emphasise that the study of entrepreneurship in transition environments should not be viewed as some kind of eccentric or marginal activity, since the findings reviewed have important implication for mainstream theory. At the heart of the distinctiveness of entrepreneurship in transition economies is the specific interplay between individual entrepreneur/firm behaviour and the external environment, which changes as the process of transition unfolds. Mainstream entrepreneurship theories need to be able to incorporate a wide range of external environmental conditions, including those where market conditions are only partially established, and the interplay of individual behaviour with contexts.

Thus, our review can make two contributions to the entrepreneurship field. First, we demonstrate the value of considering entrepreneurship as a societal phenomenon, which draws attention to antecedents and outcomes of entrepreneurial behaviour (Davidsson 2003). The societal context contributes to explaining why some entrepreneurs see opportunities and others don't, why opportunities vary over time and why the outcomes of entrepreneurial activities as well as entrepreneurial behaviour might vary in a post-socialist context and change over time as transition proceeds.

Second and related to this, we contribute to the recent debate on the importance of context for entrepreneurship. In 2001, the argument from transition economy focused

researchers was a need for concepts and theories in entrepreneurship to be robust enough to accommodate transition conditions alongside those of mature market economies, which tended to be either explicitly stated or implicitly assumed. In the last years, there has been a growing body of publications which emphasise the wider importance of social economic and institutional context (Spedale and Watson 2013; Ucbasaran, Westhead and Wright 2001; Watson 2013; Welter 2011; Welter and Xheneti 2013; Zahra 2007; Zahra and Wright 2011; Zahra, Wright and Abdelgawad 2014). Clearly, this has implications for the study on entrepreneurship in transition economies, which, at first glance, would appear to be less of a minority interest. But also it provides a route for transition economy research to be fed into the mainstream: our idea with developing this review further is to show how research on entrepreneurship in a transition context (or in the context of emerging market economies, as they have come to be called) can question our conceptual and theoretical frameworks, pushing us towards extending them to include a wide range of different contexts.

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