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Entrepreneurship and Economic Transition

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Abstract

Identification of the entrepreneur's economic function has engaged economists for more than 200 years. In this paper we address the issue of entrepreneurship in two distinct ways: a) as it has historically developed within the field of economics and b) as it develops in the transitional context. In contrast to advanced western economies, productive entrepreneurship cannot be taken for granted in transition countries. Therefore we propose a working definition and model for productive entrepreneurship for transition countries. By means of a literature survey, we further present the main characteristics of entrepreneurship in Central Eastern European and Former Soviet Union countries. Entrepreneurship in Lithuania seems to not fit neatly into these two categories and its specific situation is highlighted.

Keywords: Entrepreneurship, economics, transition economies

JEL classification: M13, P2, P5

1. Introduction

Though both an exciting and important area of study, entrepreneurship research has been characterized by little consistency or concrete theory (Baumol 1968; Herbert & Link 1989; Kirchhoff 1991; Van Praag 1996; Wennekers & Thurik 1999; Verheul et al. 2001). As Wennekers and Thurik comment: *Entrepreneurship is an ill-defined, at best multidimensional concept* (1999: 29). This complicates the development of a theory of entrepreneurship. Kirchhoff further notes: …*the absence of a widely held theory of entrepreneurship constrains not only economics but also all the disciplines that extend their interests into the entrepreneurship arena* (1991:109).

The main characteristic all transition countries share is the transition process i.e. the switch from a centrally planned economic system to a more market-oriented system. Though different in terms of degree of change, all transition countries have experienced dramatic changes to socio-economic and political conditions on the macroeconomic level. Further, in contrast to advanced western economies, productive entrepreneurship cannot be taken for granted in transition countries. This is influenced both by the current institutional weakness in many transition countries, as well as by historical legacies. Therefore, we focus on the development of productive entrepreneurship in transition countries.

In this paper, our aim is to develop a working definition for productive entrepreneurship in transition countries. In the process of developing our definition, we summarize the development of entrepreneurship research within the field of economics and we also present the characteristics of entrepreneurs in transition countries.

This paper begins with a summary of the development of entrepreneurship research within economics. Using aspects of existing definitions as a guideline, we develop a working definition and a model for productive entrepreneurship development in transition countries.

A growing body of literature on entrepreneurship in transition economies seems to indicate that though not all transition economies are the same, general trends in the entrepreneurship characteristics can be identified for Central and Eastern European (CEE) countries and Former Soviet Union (FSU) countries. However, some transition countries do not fit neatly into these two categories. The specific case of Lithuania is highlighted as an example of a transition country that seems to incorporate elements from both CEE countries and FSU countries.

2. Entrepreneurship in Economics

The entrepreneur is at the same time one of the most intriguing and one of the most elusive characters in the cast that constitutes the subject of economic analysis (Baumol 1968:64).

Though there is no consensus as to the definition of entrepreneurship, the identification of the entrepreneur's economic function has engaged economists for more than 200 years.

In this section it is not our purpose to provide extensive coverage to all the theorists and concepts that have been developed but to provide an overview of the most important contributions (table 1).

Table 1: Main contributors to entrepreneurship in economic theory

Year	Economist	Entrepreneurial Role (ER)
Classical Era		
1755	R. Cantillon	Introduced the term: Entrepreneur
		ER as speculator
1800	J.B. Say	ER as coordinator
Early Neoclassical Era		
1890	A. Marshall	ER as coordinator, innovator, arbitrageur
1907	F.B Hawley	ER as owner of output (uncertainty bearer)
1911	J. Schumpeter	ER as innovator
1921	F. Knight	ER as responsible decision maker in an uncertain environment
1925	F. Edgeworth	ER as coordinator
Mature Neoclassical Era		
1925	M.Dobb	ER as innovator
1927	C. Tuttle	ER as responsible owner in an uncertain environment
Modern Neoclassical Era		
1973	I. Kirzner	ER arbitrageur and ‘alert to profitable opportunities’
1982	M. Casson	ER coordination of scarce resources under uncertainty
1993	W. Baumol	ER innovator and manager influenced by existing incentive structure

Richard Cantillon has been credited with the introduction of the term ‘entrepreneur’. In his work ‘*Essai sur la Nature du commerce en General’* published in the mid-eighteenth century, Cantillon defines an entrepreneur as a ‘speculator in an uncertain environment’. Jean Baptiste Say, another French political economist, described the entrepreneurial function as being comprised of coordination, supervision and decision-making.

From the end of the 19th century until the mid- 20th century, Alfred Marshall played a crucial role in shaping neoclassical economic thought. Though Marshall recognized the important role played by the entrepreneur, he never precisely states the function of the entrepreneur. Instead he describes the various roles entrepreneurs play including that of coordinator, innovator, arbitrageur (Barreto 1998:54). In the early 1900’s, Frederick Barnard Hawley identified the role of the entrepreneur as owner of output and the bearer of uncertainty. For Hawley, enterprise was not a productive factor or means; enterprise was a motivational force (Barretto 1998:36).

Perhaps one of the best-known and most important contributions to the theory of the entrepreneur has been made by Joseph Schumpeter. In his book, *The Theory of Economic Development* (1912), Schumpeter identified the entrepreneur as an individual who introduces new combinations i.e. innovation to the economy. In his theory of business cycles, Schumpeter explains that innovations come in swarms i.e. the initial innovator is followed by a bunch of ‘imitators’ which results in an economic boom. Periods of innovation and lack of innovation are the main causes for the business cycle. For Schumpeter, an entrepreneur is not only an innovator but also a leader. Since the main characteristic of an entrepreneur is innovation and leadership, Schumpeter’s entrepreneur does not necessarily start his own business. Furthermore, the Schumpeterian entrepreneurial function does not include risk-taking or individuals engaged in management or decision-making based on established grounds.

In his PhD dissertation *Risk, Uncertainty and Profit* (1921), Frank Knight reintroduced the element of uncertainty to the function of the entrepreneur. According to Knight, entrepreneurs are the bearers of uncertainty in order to make a profit. In their role, entrepreneurs actively shield other individuals who are unwilling to take the same gamble for uncertain rewards.

Francis Edgeworth viewed the entrepreneur as a coordinator (combining factors of production) and arbitrageur or middleman (connecting product and factor markets). However he never fully developed a theory of entrepreneurship. Still as a leading neoclassical economist, Edgeworth's recognition of the special role played by the entrepreneur is noteworthy since unlike other neoclassical economists, he refused to eliminate entrepreneurial considerations from his explanatory scheme.

In the mature neoclassical era, Maurice Dobb identified the entrepreneur as an agent who carries out innovations and as such is the source of economic development and is the driving force behind the capitalist system (Barreto 1998:60). In this context, it is not necessary for the entrepreneur to be a capital owner, manager or the bearer of uncertainty. For Dobb, entrepreneurship is something essentially active and creative (ibid.) and in this sense, Dobb's entrepreneur played a central role in the capitalist market process. In comparison to many other entrepreneurship theorists, Charles Tuttle applied a very strict definition of entrepreneurship. Tuttle viewed the entrepreneur as a responsible owner in an uncertain environment. Though Tuttle does not present an extensive theory on entrepreneurship, the entrepreneur plays an active role in his analysis (ibid.).

As Humberto Barreto writes in his book *The Entrepreneur in Microeconomic Theory: Disappearance and Explanation* (1998), entrepreneurs as a 'function' seem to have vanished from modern microeconomic theory. The modern theory of the firm contains three core assumptions: the production function, the logic of rational choice, and perfect information, which effectively bar the inclusion of the entrepreneurial role in economic analysis. As a result of 'the logic of rational choice' the entrepreneur can no longer be the innovator because the ends and the means are known and given. The role of the entrepreneur as uncertainty-bearer, coordinator and arbitrageur also disappears because of the assumption of 'perfect information' and 'the logic of rational choice'. The entrepreneur's disappearance from microeconomic theory seems to be directly related to consistency requirements. Entrepreneurial functions do not fit neatly within the modern theory of the firm. Only by relaxing the assumptions can the entrepreneurial function be included without compromising the model's consistency.

In essence, 'the entrepreneur has been read out of the model' (Baumol 1968:67). Though the term 'entrepreneur' is still used in modern microeconomic theory, he has become synonymous with manager, owner, and capitalist: *In the orthodox firm, the entrepreneur* *plays an essentially sterile role, choosing the optimum values of the endogenous variables* (Barreto *1998:132).* The formalization of neoclassical economics is another reason why entrepreneurship diminished in significance: ... *as neo-classical economics became more formalized and as the mathematics of equilibrium theory became more important, references to the entrepreneur receded from the micro textbooks* (Wennekers & Thurik 1999:32).

The pivotal work of David Birch (1979) demonstrating the importance of SMEs for job creation, served as a catalyst for renewed economic interest in entrepreneurship and SMEs. More recent studies have found that small firms play an important economic role as agents of change through entrepreneurial and innovative activity (Acs & Audretsch 1990; Audretsch 1995), stimulating industrial evolution (Audretsch 1995), creating an important share of new jobs (Acs 1992 in Wennekers & Thurik 1999:28) and reducing unemployment levels (Audretsch & Thurik 2000). In sum, small firms can be viewed as a 'vehicle in which entrepreneurship thrives' (Wennekers & Thurik 1999:29).

The more recent development of the endogenous growth theory (Romer 1990; Aghion & Howitt 1992) has created new possibilities for including entrepreneurship, innovation and creative destruction into macroeconomic growth models. However within endogenous growth theory, entrepreneurship remains largely implicit and the theory does not provide insight as to the underlying conditions of the entrepreneurial activity needed for (human) capital formation and innovation (Wennekers & Thurik 1999:36).

In the modern neoclassical period, important contributors to entrepreneurship research have included Israel Kirzner, Mark Casson and William Baumol. Following the tradition of the neo-Austrian school, Israel Kirzner defines the entrepreneur as the arbitrageur and someone 'alert to profitable opportunities' in his book, *Competition and Entrepreneurship* (1973). Kirzner's entrepreneur is not the bearer of uncertainty nor does s/he fill the role of coordinator or manager in the production process.

In his book, *The Entrepreneur: An Economic Theory* (1982), Mark Casson defines the entrepreneur as an individual who has different skills which enables her/him to make judgments to co-ordinate scarce resources. According to Casson, the entrepreneur operates within a set of technological conditions and by making difficult judgmental decisions, the entrepreneur is able to enjoy the reward of profit. This allows the entrepreneur to coordinate demand and supply under uncertainty (Deakins 1996:13).

A more expansive definition of the entrepreneur is presented by William Baumol in his book, *Entrepreneurship, Management and the Structure of Payoffs* (1993). Baumol incorporates two functions of the entrepreneur: as a Schumpeterian innovator and as a manager. Baumol maintains that entrepreneurs do not appear and disappear; but the numbers of productive and unproductive entrepreneurs change in terms of the existing incentive structures. For Baumol, productive entrepreneurial activity refers to any activity that contributes directly or indirectly to net output of the economy. Productive entrepreneurship does not need to yield tangible products. However, a productive activity should yield a positive marginal product no matter how indirect the route the activity employed takes in achieving this (ibid: 30). Conversely, an unproductive entrepreneur engages in innovative activity but makes no contribution to the real output of the economy. In some cases the activity can also serve to reduce output or restrain its growth. Finally, a destructive or rent-seeking entrepreneur engages in innovative activity that leads to the misallocation of valuable resources into pursuits that from the viewpoint of the economy are useless and are carried out for the self-serving purposes of the entrepreneur (ibid: 10).

3. Towards a definition of entrepreneurship

The Schumpeterian definition of entrepreneurship as linked to innovation i.e. s/he who carries out new combinations in its broadest sense is essential for defining entrepreneurship. In this sense, innovation is a phenomenon that occurs at a given ‘moment of time’ and entrepreneurship is the manifestation of the 'innovative spirit'. Entrepreneurship is a temporary condition for any person, unless they keep innovating

(Van Praag 1996:22). As a result, entrepreneurs do not form a social class and are not necessarily engaged in new venture creation.

In addition to innovative spirit, risk-taking and Knightian uncertainty are also important for defining entrepreneurship. Even if the innovative activity does not entail new venture creation the entrepreneur is involved in risk-taking. As Casson writes: …*even if the entrepreneur is a salaried employee, however, he is still exposed to risk. His reputation for 'good judgment' on which his future earning power depends is always 'on the line'* (1993: 52).

A more recent defintion proposed by Sander Wennekers and Roy Thurik (1999) blends together the concepts of innovation and uncertainty:

Entrepreneurship is the manifest ability and willingness of individuals, on their own, in teams, within or outside existing organizations to (a) perceive and create new economic opportunities (new products, new production methods, new organizational schemes and new production-market combinations) and to (b) introduce their ideas in the market in the face of uncertainty and other obstacles, by making decisions on location, form and the use of resources and institutions (1999:46-47).

Essentially, entrepreneurship is a behavioral characteristic of a person[1]. A blend of internal (personality and skills) and external factors (social and economic incentives) provide the stimulus for innovative activity i.e. entrepreneurship to manifest itself. Further, entrepreneurship is not restricted to a given 'productive' economic activity. As in Cantillon's definition, an entrepreneur can be a registered business owner, a politician, a hustler, a racketeer, a corrupt tax inspector, or a manager in a large firm. What sets entrepreneurs apart from the rest is their engagement in innovative activities such as new combinations and non-routine activities. The entrepreneur's reward for engaging in innovative activity is a blend of power, prestige and profit (Baumol 1993). The economic and social incentives seems to determine what type of entrepreneurial activity are the most prevalent in a given setting.

4. Productive and unproductive entrepreneurship

William Baumol's main contribution to the theory of entrepreneurship was to expand the range of entrepreneurial activity and to emphasize the important role played by institutions, i.e. the 'rules of the game' (both formal and informal institutions) for providing the incentives for entrepreneurial activity. Like Schumpeter, Baumol defines an entrepreneur through his or her innovative activity. Apart from this core characteristic entrepreneurs can vary in all other respects since it is the environmental incentives or disincentives that further shape the entrepreneurial activity. For example, Baumol observes that wars in the early Middle Ages in Western Europe could be viewed as unproductive entrepreneurship, i.e. expressions of 'violent' yet innovative economic activity primarily engaged in rent-seeking activity. The result of these activities led to the net reduction in social income and wealth but enriched the 'entrepreneurs' (1990). An example of productive entrepreneurship could be a Dutch merchant in 17th century Europe. The incentives and subsequent choice to engage in productive or unproductive entrepreneurial activities seems to depend on the socio-economic context. In the modern context, an innovative productive entrepreneur could be found starting a high-tech business venture in Silicon Valley. An innovative but unproductive entrepreneur could be a governmental official drafting another bureaucratic procedure intended to increase his personal wealth within an authoritarian regime. In sum, an entrepreneur may or may not own their own business, may or may not be engaged in productive activity, but the distinguishing factor is 'innovative behavior'. Exploring the role of the socio-economic context on the development of productive and unproductive entrepreneurship seems especially relevant for the transition countries.

5. Aspects of entrepreneurship in transition countries

Entrepreneurship in transition countries can best be defined using a blend of existing definitions and concepts. Though little analytical work has been done on the specific types, roles and definition for entrepreneurship in transition countries, Richard Scase and Bruno Dallago have made more extensive theoretical contributions.

Richard Scase (2000) introduces a distinction between ‘entrepreneurship’ and ‘proprietorship’ for business activities taking place in the post socialist countries of Central Europe and Russia. The main difference between these two categories are the contrasting psychologies of the founder-owners, their attitudes towards trading, and their orientation to capital accumulation. According to Scase, entrepreneurship refers to a person’s commitment to wealth creation, capital accumulation and to business growth. In the Weberian sense, the entrepreneur is willing to forgo direct consumption in order to expand the scale of the entrepreneurial activities (Weber 1920). On the other hand, proprietorships are likely to consume and utilize economic surpluses in order to maintain specific standard of living or lifestyle rather than re-invest these funds into their business. As a result capital assets are not used by proprietors for the purpose of long-term capital accumulation.

The prime motive of proprietors is not capital accumulation or business growth but direct consumption needs. According to Scase, in the emerging markets of Russia and Central Europe, the greater proportion of small business traders are proprietors rather than entrepreneurs (2000:6). Scase however concedes that these categories are dynamic and not rigidly defined. It is therefore possible for proprietors to turn into entrepreneurs or vice versa. Scase also identifies two types of ‘entrepreneurs’ in transition countries: the legitimate and the illegitimate entrepreneurs. Entrepreneurs and proprietors are examples of legitimate businesses while anarchistic, opportunistic hustlers or Mafia members are examples of illegitimate businesses. This categorization is similar to Baumol’s classification of entrepreneurs into productive and unproductive categories.

Bruno Dallago defines the entrepreneur in a Schumpeterian way as *’any individual or organization who has new ideas and implements them through non-routine activities’* (1997:104). For Dallago, entrepreneurship is not strictly an individual process but a 'collective, societal phenomenon' since 'innovation needs time and the cooperation of many individuals and organizations' (ibid.). Within the Soviet type of economy, Dallago identifies two distinct types of entrepreneurs: *economic* and *systemic entrepreneurs*. *Economic entrepreneurs* transform the structure and working of the system through innovative behavior so as to solve certain problems. Further, economic entrepreneurs may engage in both productive and unproductive innovative activities. *Systemic entrepreneurs* work within the existing system to further specific interests.

Within the centrally planned system, systemic entrepreneurs could be found generating innovative activities in order to serve the Party against society as a whole, to serve a specific social group, to enrich themselves or obtain privileges by taking advantages of shortages. Systemic entrepreneurs formed the elite (nomenclature) within the centrally planned system and are therefore more readily opposed to systemic change which would erode their former 'entrepreneurial opportunities'. Though both economic and systemic entrepreneurs could engage in productive or unproductive activities, systemic entrepreneurs had a greater stake in the former system and are more prone to path dependence and unproductive activities. Systemic entrepreneurs are a product of the transition process while economic entrepreneurs (productive or unproductive) are also fond in western developed economies.

Dallago also identifies four types of economic entrepreneurs in the transitional landscape: elite members, domestic, returning migrants and foreign entrepreneurs. The first type of entrepreneurs are from the 'old' political elite. Many of these elite entrepreneurs were managers of state-owned enterprises. Dallago asserts that most of the elite entrepreneurs were very competitive in the redistribution process but not in production. For the most part, elite entrepreneurs can be classified as unproductive or rent-seeking entrepreneurs. The importance of elite entrepreneurs differs amongst transition countries with significantly higher levels found in Russia and lower levels in Hungary (1997:117). As the name implies, domestic entrepreneurs are indigenous individuals who were not members of elite groups. According to Dallago's definition, domestic entrepreneurs were already engaged in entrepreneurial activities before 1989. Though one would expect this group to make up an influential portion of all entrepreneurs, Dallago finds that they make up an small share of new entrepreneurs.

The third type of entrepreneur classified as returning migrants is comprised of former citizens who emigrated prior to 1989. The transition process opened up the possibilities for their return and active engagement in the economic process. Returning migrants may have a positive role in transition because they bring valuable capital resources: both financial and human (1997:117). Though some returning migrants have positively influenced the development of productive entrepreneurship, their role has not been quantitatively important (ibid.). The fourth type of entrepreneurship are foreign entrepreneurs. Their role has, in general, been a positive one by introducing a healthy competitive atmosphere, innovative spirit and by contributing to foreign direct invesment.

Dallago agrees with Baumol's concept that the 'rules of the game' are the main determinants of entrepreneurship in transition countries (1993). In this sense, it is not the supply of entrepreneurs that is of concern, but the rules that shape their behaviors. As Dallago writes, *…it is more the set of 'rules of the game' than the supply of entrepreneurs that determines the performance of an economy and the efficiency of an economic system via the allocation of entrepreneurship to productive or unproductive uses* (1997:106).

6. A working definition for entrepreneurship in transition countries

Given the context of transition where traditionally entrepreneurial activities were not productive and often rent seeking and economically destructive, our working definition for entrepreneurship should emphasize the difference between productive and unproductive forms of entrepreneurship. Baumol argues that entrepreneurs will seek wealth, power and prestige with their innovative activities and that positive environmental incentives can channel innovative, entrepreneurial behavior in a productive way (1993). Though entrepreneurial activity is not limited to business formation, given our interest in productive business development, we focus our definition on business creation. In order to make our definition appropriate for the transition context, it should also take into account the effect of the 'rules of the game' on the development of unproductive as well as productive entrepreneurship (inspired by Baumol and further discussed by Dallago). Further in our definition we focus on productive entrepreneurship and in doing so divert the focus from the distinction between entrepreneurs and proprietors (Scase 2000) or systemic and economic entrepreneurs (Dallago 1997).

In addition, though solo self-employment (self-employed with no employees) may not always be viewed as a form of entrepreneurship in advanced western economies, it can be argued that solo self-employment in transition countries is a form of entrepreneurship (Chilosi 2001). Given the utter 'newness' and lack of private business ownership in transition countries, solo self-employment demands a relatively high level of innovative behavior and risk-taking in the transition context.

Therefore, our defintion should capture that notion that manifestations of entrepreneurship (i.e. innovative, risk-taking, market-oriented behavior) in the form of viable businesses, are influenced by both the existing and historically determined incentive structures (social and economic) within a given context. These incentive structures have a direct influence on the development of productive or unproductive entrepreneurship. In essence, we argue that productive entrepreneurship is a manifestation of the innovative spirit that occurs when the individual, social, legal, political and economic conditions are sufficient.

Thus our working definition, based on Wennekers and Thurik (1999) for **productive entrepreneurship in transition countries** focuses on innovative activity under uncertainty resulting in an economically productive business:

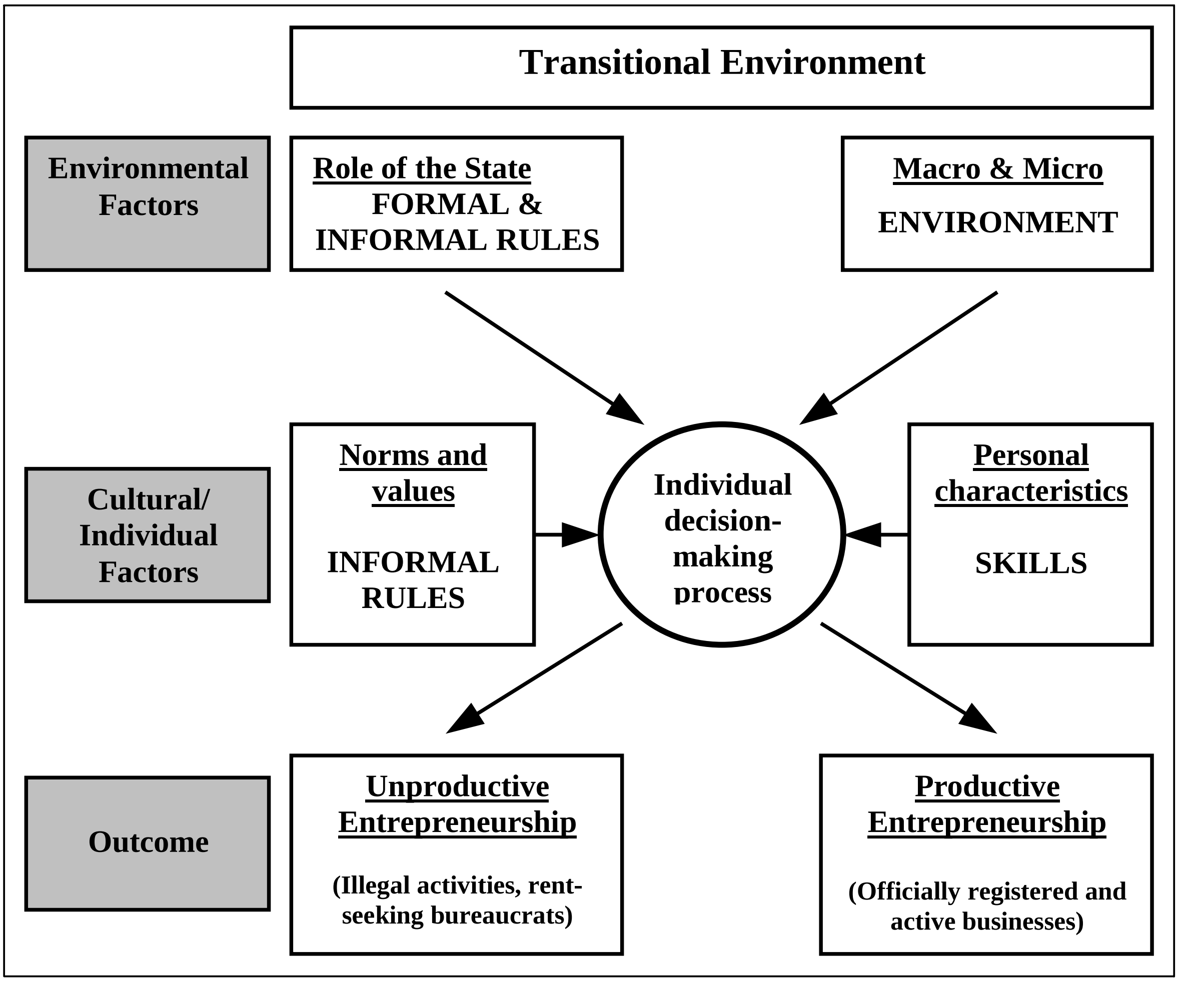
Productive entrepreneurship is … *the manifest ability and willingness of individuals to (a) perceive and create new economic opportunities through innovative activity (new products, new production methods, new organizational schemes and new production-market combinations) and to (b) introduce their ideas in the market in the face of uncertainty and other obstacles; and (c) their efforts result in a viable business that contributes to national economic growth*[2] *and personal livelihood.*

7. A model for entrepreneurship in transition countries

In transition economies productive entrepreneurship cannot be taken for granted. Therefore, in making a model for entrepreneurship development (figure 1) we clearly indicate that the entrepreneurial outcome can be either productive or unproductive entrepreneurship. Our model distinguishes between two main levels of influence: environmental factors (such as macro- and microenvironment and the role of the state) and cultural and personal factors (such as norms and values, personal characteristics and skills). All these factors combined influence the individual's decision-making to pursue either productive or unproductive entrepreneurship in the form of a viable business. It can be argued that some influencing factors are easier to change than others but all areas are open to some degree of change.

Government policy and programs can play an instrumental role in all four of the core factors influencing the development of either productive (legitimate) or unproductive (illegitimate) entrepreneurship. In this sense, our model highlights the important role governmental policy and programs can play in shaping the entrepreneurial outcome as either productive or unproductive. Personal characteristics are the least likely to change and most personal characteristics such as age, sex and ethnicity cannot be changed. However, carefully designed training programs and changes to cultural norms and values may have a positive influence on personal beliefs and values.

Figure 1: Entrepreneurial development in Transition Countries



8. Entrepreneurs in the transition setting

Though transition countries differ in many ways, a number of similarities exist that influence entrepreneurial development. For example, studies of transition economies emphasize the existence of both productive (legitimate) and unproductive (illegitimate) forms of entrepreneurial business activities (Arendarski et al. 1994; Smallbone & Piasecki 1995; Dallago 1997; Frye & Shleifer 1997; Roberts & Zhou 2000; Scase 2000; Chilosi 2001). Unproductive entrepreneurship is often seen as influenced by both path dependence (Dallago 1997) or the currently over-regulated and corrupt legal business climate (Arendarski et al. 1994; Chilosi 2001).

Based on a literature review, a summary of the main entrepreneurial characteristics in terms of factors such as the environment, the role of the state and business owner characteristics found in transition countries are presented in chart 1 and a comparison of the specific characteristics of entrepreneurs in CEE and the FSU countries are presented in chart 2[3]. Some transition countries do not fit neatly within these two categories. The specific case of Lithuania is highlighted in chart 3. Though a number of the characteristics outlined below may also be applicable to SMEs in western developed countries (such as 'lack of external financing'), the distinguishing difference is one of degree. In transition countries some barriers may be similar to those experienced by SMEs in western developed countries however they tend to affect business more severely (Smallbone & Welter 2001).

Chart 1: Entrepreneurship in transition countries: General characteristics

Factor	General characteristics
Environment	Macro: Dramatic changes to socio- economic and political conditions
	Micro: The reorganization of work
	Lack of recent 'productive' entrepreneurial tradition
	Hostile economic environment
	Initial explosion of business activity followed by declining SME start up rates
	Absence of business infrastructure and support services
	Lack of external financing
The role of the state	Neo-liberal governmental stance; hesitant to intervene in market processes
	No previous experience with business tax system or legislation
	Negative attitude towards entrepreneurs
	Over-regulation, interference, corruption
Business owner characteristics	New Business, new career
	Diverse social origins
	Primitive business methods
	Dependence on assistance through private networks
	Government skepticism
	Passive, bureaucratic attitude
	No previous experience with business tax system or legislation
	More progressive and market-oriented than the general population

Environment. The main characteristic all transition countries share is the transition process i.e. the switch from a centrally planned economic system to a more market-oriented system. Though different in terms of degree of change, all transition countries have experienced dramatic changes to socio-economic and political conditions on the macroeconomic level. On the microeconomic level, all transition countries have had to address the 'reorganization of work' (Johnson & Loveman 1995) which includes the acceptance of private forms of enterprise. Even though in some CEE countries limited forms of private enterprise were allowed even under socialist regimes, most transition countries lack a recent 'productive' entrepreneurial tradition (Smallbone & Piasecki 1995). A 'hostile economic environment' (high inflation rates, persistently high unemployment rates, declining real earnings, etc.) again in various degrees, has characterized the transition process (Smallbone & Piasecki 1995; Smallbone & Welter 2001). Given varying measures of market liberalization and excessive consumer demand, we observe an initial explosion of business activities in transition countries followed by declining SME start-up rates (Smallbone & Piasecki 1995; UNDP 1998; Kontorovich 1999; Glas et al. 2000). The lack of private enterprise tradition in most transition countries resulted in an absence of business infrastructure (Smallbone & Piasecki 1995). Further, the initial growth of private business activity coupled with the implementation of neo-liberal transition programs resulted in a lack of private business support services (ibid.). A main barrier encountered by many private business owners is the lack of external financing (Smallbone & Piasecki 1995; Pissarides 1999, 2000).

Role of the State. In most cases, national governments took a neo-liberal stance (often under the guidance and pressure from the International Monetary Fund and exhibited a general hesitance to intervene in market processes (Smallbone & Piasecki 1995). As would be expected, policy mistakes were made especially in areas where there was little previous experience such as with the introduction of a business tax system and business legislation. However, national governments were hesitant to take responsibility for the effects of bad policies on private business development (ibid.). A later trend has been the tendency for transitional governments to over-regulate and interfere with private business activities reducing the expansion and growth of the private business sector. This has also led to increased corruption (Dallago 1997; Frye & Shleifer 1997; Bartlett & Bukvic 2001; Smallbone & Welter 2001). Finally, a negative attitude towards private business owners and entrepreneurs in general continue to influence government officials (Marot 1997; Glas et al. 2000).

Business Owner Characteristics. For many business owners in transition countries, private business ownership signaled the start of a new career (Roberts & Zhou 2000). Business owners under these conditions tend to come from diverse social origins and backgrounds (ibid.). Given the underdevelopment of the private sector, many business owners in transition countries used quite rudimentary and primitive business methods but still obtained profitable results (ibid.). The lack of developed business infrastructure and support services leads many business owners to depend on business assistance (financial, advice, etc.) through private networks (ibid.). Most business owners also exhibit skepticism towards the national government (Smallbone & Piasecki 1995). Though business owners are often critical of the government, they tend to adopt a passive rather than pro-active attitude[4]. In addition, new business legislation and taxes creates difficulties for business owners in transition countries who generally lack experience with income and profit tax or private business legislation (Roberts & Zhou 2000). Finally, private business owners in transition countries tend to be more progressive and market oriented than the general population (ibid.). In that sense, they are greater supporters of market oriented changes and reform.

9. Central and Eastern European and former Soviet Union countries compared

Environment. As shown in chart 2, the affinity with Europe and the European Union countries has had a strong influence on the more western-oriented development chosen by CEE countries (Roberts & Tholen 1998). For many, the memory of private enterprise as well as the retention of a small and limited private sector even during the socialist period, has resulted in the rapid development of a private sector. Further, in most countries, the profound changes to the existing socialist political and economic order has led to the replacement of old political elites.

The situation for business owners in the FSU is quite different. In many countries we still see a dominance of the old Russian language networks that continue to link newly independent FSU countries to Russia (Roberts & Tholen 1998). As a result, the Mafia-style capitalism that is taking root in Russia is having a broader regional influence (ibid.). Most FSU countries have no memory of private business ownership and the Soviet policies resulted in a non-existence of private business culture during communist rule. Even though the collapse of the Soviet Union resulted in the emergence of many new independent countries, most ruling elites remained in power, in many cases simply changing their name (ibid.).

The Role of the State. For the most part, CEE countries have ascribed to an 'invisible hand model' for the government that limits intervention or interference in private business development (Frye & Shleifer 1997). However, this is not the case for FSU countries. The Soviet state was built on an ideology that stifled independent innovative culture and allowed for a punishment-oriented 'inspection culture' to develop. The disintegration of the Soviet Union has led to a political and economic vacuum in many FSU countries which has facilitated the development of a 'grabbing hand model' of government intervention. This type of governmental structure is characterized by corrupt behavior occurring in a disorganized way that leads to the personal enrichment of governmental officials to the detriment of the government and the country as a whole (ibid.).

Business Owner Characteristics. Private business owners in CEE countries tend to be specialized in their business activities in a diverse array of business sectors and for the most part, view their businesses as a full-time endeavor (Roberts & Tholen 1998). In this context, business development is seen as a gradual step-by-step process. Individual businesses versus business partnerships are the dominant form of private business engagement. For the most part, private businesses function in the official economy.

In contrast, given the unstable economic and political conditions in a number of FSU countries, many business owners focus on short-term get-rich-quick business strategies instead of long-term strategies (Roberts & Tholen 1998). Business owners in FSU countries tend to engage in generic business activities (many activities as once in order to spread risk) and are primarily involved in trade activities (ibid.). Many business owners are also still employed in the state sector and engage in their businesses as a part-time activity (ibid.). Business partnerships are the dominant form of business activity since they seem more effective in protecting business operations (ibid.). Also, many private businesses function in both the official and informal economy (Roberts & Tholen 1998: Kontorovich 1999).

Chart 2: Differences between entrepreneurship in CEE and FSU countries

Factor	Central and Eastern European countries	Former Soviet Union countries
Environment	Affinity with Europe and European Union countries	Dominance of old Soviet Russian language networks
	Western-oriented development	Mafia-style capitalist development
	Memory of private businesses	No memory of private businesses
	During socialist period, small and limited private business culture sustained	During socialist period, private business culture non-existent
	Communism collapsed and resulted in a rotation of political elites	Communism collapsed with only partial rotation of political elites
The role of the state	Invisible hand model	Grabbing hand model
		Inspection culture
Business owner characteristics	Specialization of business activities	Business development focused on the 'big strike' or getting rich quickly; coping with unstable market conditions
	Full-time private businesses	Generic business activities
	Diversified business sectors	Business activities primarily engaged in trade
	Businesses function in official economy	Part-time businesses in combination with employment in the state sector
	Individuals businesses are the dominant form	Partnerships for business protection and survival predominate
	Business development seen as a gradual step by step process	Businesses function in both official and informal economies

10. Entrepreneurship in Lithuania

Environment. In many respects, the situation for business owners in Lithuania is a blend of the CEE and FSU country situations (chart 3). Though Lithuania was part of the Soviet Union, it also shares some similarities with CEE countries. As a Baltic country with historical ties to Europe, Lithuania feels an affinity with Western Europe especially with the EU countries. Lithuania also prioritizes western-oriented development. Further, during its brief period of independence between the First and Second World War, Lithuania was able to develop a market-oriented economy based on private business ownership. In this sense, Lithuania is similar to other CEE countries in its retention of a memory of private business ownership. Lithuania regained its independence in 1991 and though many political, economic and social realities have dramatically changed, it can be argued that political (and subsequently economic) power was retained by the ex-Communist Party elite (a pattern observed in other FSU countries).

Role of the State. The legacy of the Soviet-style inspection culture continues to play an influential role in independent Lithuania. In general, the Lithuanian State seems more focused on penalizing and punishing deviant behavior than promoting or providing incentives for exemplary private business activities. The role of the state in Lithuania has not regressed to a 'grabbing hand model' as in other FSU countries; nor has it reached the level of CEE countries in adopting an 'invisible hand model' (Frye & Shleifer 1997). Lithuania's situation falls somewhere in between with an 'interfering hand model' i.e. continuing governmental interference that hampers independent private business development.

Business Owner Characteristics. Many business owners in Lithuania tend to engage in generic business activities especially in the trade sector and focus on short-term business strategies to 'get-rich-quick' as in other FSU countries. However, for most business owners in Lithuania as in CEE countries, business ownership is a full-time activity. It seems that most Lithuanian businesses function simultaneously in both the official and informal economy as do the majority of FSU business owners (Roberts & Zhou 2000; Kontorovich 1999). In addition, in Lithuania some business owners seem to form protective partnerships as in the FSU countries while others function as individual businesses as in the CEE countries.

Chart 3: Entrepreneurship in Lithuania: General characteristics

Factor	**Lithuania**
Environment	Affinity with Europe and European Union countries
	Western-oriented development
	Memory of private businesses
	During socialist period, private business culture non-existent
	Communism collapsed with only partial rotation of political elites
The role of the state	Interfering hand model
	Inspection culture
Business owner characteristics	Business development focused on the 'big strike' or getting rich quickly; coping with unstable market conditions
	Generic business activities
	Business activities primarily engaged in trade
	Full-time private businesses
	Businesses function in both official and informal economies
	Both individual business and protective partnership businesses formed

11. Conclusion

Within Economics, entrepreneurship research was an important area of study up until the early 20th century. Thereafter entrepreneurs seemed to disappear from mainstream economics. This disappearance of the entrepreneurial function within economics seems to coincide with the incorporation of the modern theory of the firm in orthodox economics. The main explanation for the entrepreneur's disappearance from microeconomic theory has to do with consistency requirements. Entrepreneurial functions do not fit neatly within the modern theory of the firm. An important contemporary contributor to entrepreneurship theory has been William Baumol's historical account of the influence of incentives on the development of productive or unproductive forms of entrepreneurship

(1993). More recently, the economic importance of the SME sector has increased the interest in understanding and researching the entrepreneurial process.

In contrast to advanced western economies, transition economies seem to be characterized by a high level of unproductive entrepreneurial activities since most entrepreneurial activities in the centrally planned system were focused on rent seeking and were economically destructive (Dallago 1997). In that sense, productive entrepreneurship in transition countries cannot be taken for granted. In constructing a working definition for productive entrepreneurship in transition countries, we incorporate Schumpeterian innovativeness and Knightian uncertainty and do not limit entrepreneurship to new venture creation. Further we restrict our definition of entrepreneurship to describing the creation of a viable 'productive' business. Drawing from a definition proposed by Wennekers and Thurik (1999) and including a focus for productive business creation, our working definition for productive entrepreneurship focuses on innovative activity under uncertainty resulting in an economically productive business:

Productive entrepreneurship is … *the manifest ability and willingness of individuals to (a) perceive and create new economic opportunities through innovative activity (new products, new production methods, new organizational schemes and new production-market combinations) and to (b) introduce their ideas in the market in the face of uncertainty and other obstacles; and (c) their efforts result in a viable business that contributes to national economic growth and personal livelihood.*

A growing body of literature on entrepreneurship in transition economies seems to indicate that general trends in the entrepreneurship characteristics can be identified for Central and Eastern European (CEE) countries and Former Soviet Union (FSU) countries. However, some transition countries do not fit neatly into these two categories. The specific case of Lithuania is highlighted as an example of a transition country that seems to incorporate elements from both CEE countries and FSU countries.

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Notes

[1] Here we are focusing on the individual, but it is also true that entities such as cities, regions and nations at the meso or macro level can also be entrepreneurial (Wennekers & Thurik 1999:47).
[2] This definition is based on the assumption that the national government is striving for a benevolent role towards productive entrepreneurship development. If however, the government is of the rent-seeking variety then it may in fact be necessary at times for productive entrepreneurs to evade national regulations in order to continue their productive entrepreneurial activities.
[3] We recognize that there are differences between countries that we have grouped into generally categories. For the purposes of this analysis, the two categories (CEE countries and FSU countries) most clearly delineates the differences between transition countries.
[4] This seems to be a legacy of the post-socialist state. See also Kobeissi (2001).