



Liberating human potential

By Vernon Ellis

As the economies of Central and Eastern Europe enter the new century on a wave of technological change and entrepreneurship, the region's companies are emerging as strong and credible global competitors. And this is giving some of their executives second thoughts about the virtues of membership in the European Union.

You shall go to the ball, Cinderella—but not just yet. First, suitable transition arrangements must be in place. And there must be an agreed-upon timetable. But you do have our firm commitment to your admission sometime before the stroke of midnight . . .

Are the 10 former communist countries that have applied for membership in the European Union—Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, the Slovak Republic and Slovenia—feeling just a little frustrated these days about their dealings with a somewhat hesitant fairy godmother?

Enlargement of the union is now officially near the top of the EU agenda. In September 1999 the EU appointed for the first time a commissioner whose focus is on this issue exclusively. But it is already clear that accession of the Central and Eastern European applicants will slip well beyond the declared target of

2002. Indeed, the Economist Intelligence Unit has predicted that none will join before 2005.

Yet to meet even this extended deadline will require the speedy resolution of a range of complex and politically contentious issues, including the timing and terms of CEE applicants' entry into the single European currency regime, the impact of their accession on the Common Agricultural Policy, the scale of the financial transfers they may require and the reform of EU governance to accommodate additional members.

But in the final analysis, how much of this will really matter? The transformation of the CEE economies during the past decade—all the more remarkable considering the suffocating effect of more than 40 years of communism—has been achieved not by a wave of the European Union's magic wand but largely through the efforts of these countries themselves.

This economic renewal has occurred at different speeds and with some variation in method from country to country. The driving force has been the same in all 10 countries, however: Change has been propelled primarily by individuals and businesses rather than government initiatives. And the transformation is set to continue for the next 10 years, whatever happens to the official relationship between the countries of Central and Eastern Europe and the EU.

Sustainable dynamism

Multinational businesses would do well to understand the sources of this historic economic transformation, whether they wish to seek partners in the CEE countries or to meet them effectively as competitors.

It is a common, but mistaken, assumption that the CEE countries are building their economic success entirely on low labor costs. There is no denying that this has been important during the early years of transition. But increasingly, the countries' potential

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advantage rests on other factors, especially their application of new technology and their ability to capitalize on the unique experience and attributes of their people. This human dynamism is providing a much more sustainable basis for competitiveness than low wages can.

(Indeed, the gap in wages is closing already. Between 1991 and 1997 the wages of American car workers rose by 19 percent, compared with their counterparts in the Czech Republic, Hungary and the Slovak Republic, who received increases of between 130 percent and 160 percent.)

Under communism, the CEE countries were technologically backward in every area except the military and the security services. Since the collapse of the old regimes, these countries often have leapfrogged into the most advanced systems available today, especially in telecommunications and computers,

bypassing the Western problems of updating complex legacy systems.

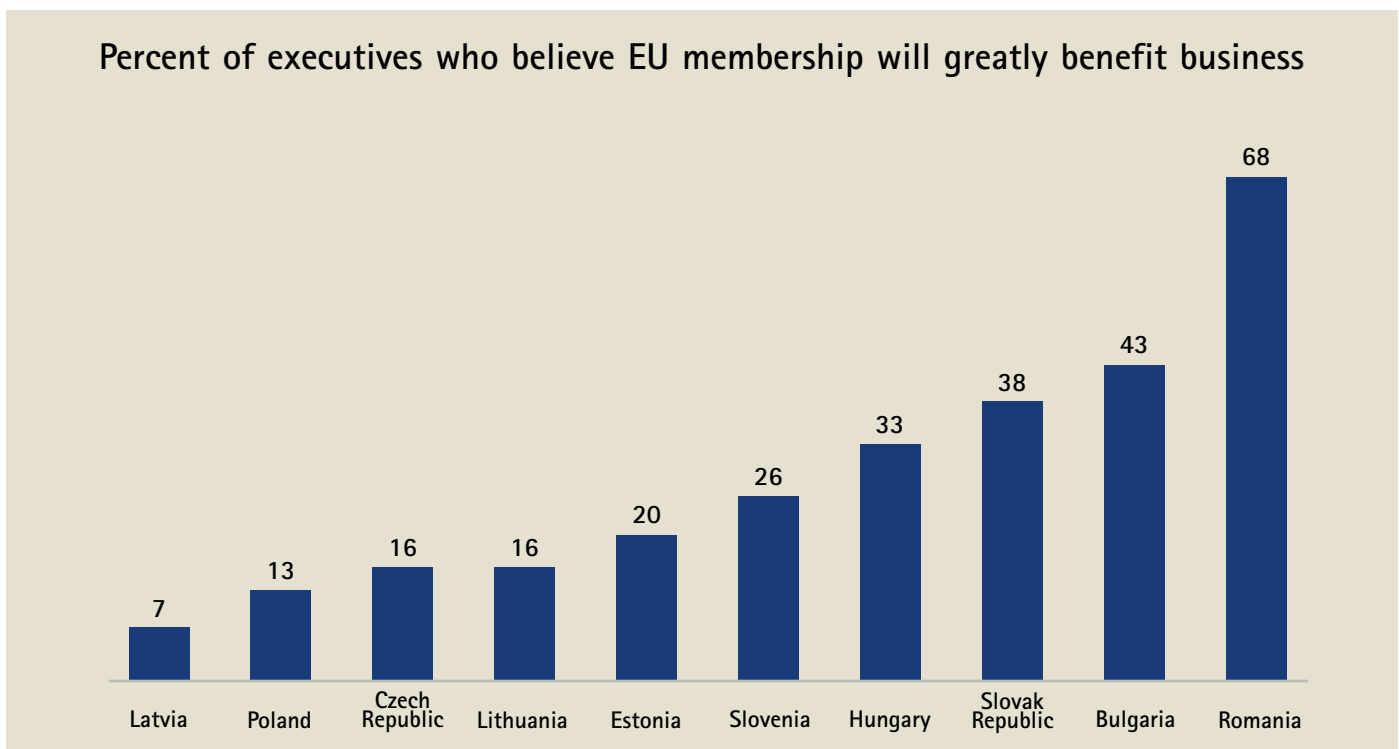
A colorful illustration of the change can be found in Hungary. Under that country's communist government, few people owned landline telephones. The chief executive of a leading pharmaceutical company remembers when his company had to use a public call box outside the building for its headquarters telephone.

Today the once slow and sleepy provider of public telephone service—the Hungarian Post Office—has a privatized offshoot, MATÁV, which is not only a highly efficient supplier of fixed-line telephones but also the biggest mobile-phone company in the country. Average waiting time for a telephone in Hungary has fallen from 10 years to two days.

New technology has transformed the quality and the reputation of CEE

Questionable gains

The countries closest to joining the EU are less certain of the benefits than some for which membership is a more distant possibility.



SOURCE: ACCENTURE STUDY

goods and services, enabling the region's companies not only to compete successfully in recently opened domestic markets but also to capture new ones overseas.

For example, cars produced by the Czech manufacturer Škoda used to provide Western comedians with an easy target for jokes. Today Škodas are made on one of the most advanced production lines in the world; 80 percent of the cars are exported to 70 countries. Now an integral part of the Volkswagen group, Škoda Auto's quality ratings are considered excellent, even by VW standards. In striving to achieve this ratings level, the company, in turn, has had a huge impact on the quality of the supplier base across the Czech Republic.

Even more important, new technology has brought rapid and dramatic change in the way enterprises are run and industries are structured, in the way governments operate and individuals live and work.

Technology has created domestic markets for new services, especially travel and banking. It has driven companies to seek new relationships with suppliers, distributors and foreign partners; to discover more about their customers; and to redirect new investment toward R&D and knowledge capital rather than physical assets.

Banking on technology

This is particularly apparent in the financial services sector, the biggest user of technology in the region. Under communism, there were no private retail banks. Today many of the new private-sector CEE banks have moved straight to automated banking, without the intervening stage of local branches.

For example, the Czech bank Expandia Banka has launched the country's first Internet bank, which serves

both retail customers and small and medium-sized businesses. Customers can access account information and authorize payments either online or from their mobile phones. And in Estonia more than 10 percent of Hansapank's clients bank via the Internet—and about 85 percent of all client transactions are electronic.

The effect of new technology can be seen across a range of successful CEE enterprises. Apart from Škoda, examples include the Czech travel company Fischer, with its advanced Internet-based reservation system, and Poland's thoroughly modernized Gdynia shipyard, which survived a liquidity crisis to become the sixth largest shipyard in the world.

eGap

But while there are many success stories, new technology has yet to reach many businesses and customers in these countries. Above all, Internet penetration is still very low in the region. According to the International Telecommunications Union, only 3 percent of Central Europeans own computers; in the Baltic Republics the figure is less than 1 percent.

eCommerce is still very much in its infancy. Business-to-consumer online revenue adds up to only \$0.04 per capita in Hungary, compared with \$24 in the United Kingdom and \$114 in the United States. Of course, further Internet take-up will provide a boost to this business.

However, it is these countries' rapid adoption of mobile telephony that should have the biggest impact in the longer term, as advanced telephones (along with interactive digital television) take over from computers as the primary point of access to the Internet. These could be the engines that enable some CEE economies to become real players in global eCommerce.

Under communism, people found it difficult to innovate and make effective decisions—not because they lacked the basic ability but because they were prevented from doing so or were diverted into other activities. Hard-working and inventive employees wasted their time and talent trying to get outmoded technology to function. Managers were often highly resourceful, but they deployed this talent negotiating ways around the strictures of the command economy.

People had little to no incentive to improve their skills or to work independently or more efficiently. Entrepreneurship was either nonexistent or criminal. Consumers were passive recipients of the output of state monopolies, holding no power of choice or discernment.

Now—reempowered as workers, managers, entrepreneurs and consumers—these people look forward to the rewards of hard work, education, innovation, self-sufficiency and initiative.

These qualities have been strengthened in this period of unparalleled change, reviving what John Maynard Keynes once referred to as “the animal spirits” of their respective economies. One needs only to view the immense advertisements that now plaster the sides of the Stalinist apartment blocks of many CEE cities to get a sense of the region's new wave of consumerism.

The dramatic improvement in the quality of consumer goods in the CEE countries has allowed domestic producers to begin reconquering market share from imports. The quality of distribution and service to consumers also has improved significantly. This trend will continue as CEE companies follow the lead set by progressive, consumer-focused businesses, such as Poland's new mobile-phone giant, ERA GSM.

There is an apparent paradox in EU membership for these countries.

This is not to say that transformation has been easy or painless, or that everyone has coped with the pace of change. According to Janusz Szlanta, CEO of the Gdynia shipyard, "Some people thought that the changes were just short-term and waited for the old times to come back." Moreover, although there is increasing consumer power for some, this phenomenon also serves to highlight the growing social divide between the haves and the have-nots.

Flexibility, adaptability, innovation, education, initiative—all these words sound surprisingly familiar. The reason is that these are precisely the skills needed to be successful in today's rapidly changing global economy. Not coincidentally, they are also the survival skills that helped the region's people endure their post-World War II history and that today give CEE businesses a potentially important competitive advantage over their Western counterparts.

The big issue now is whether CEE businesses can capitalize on this advantage.

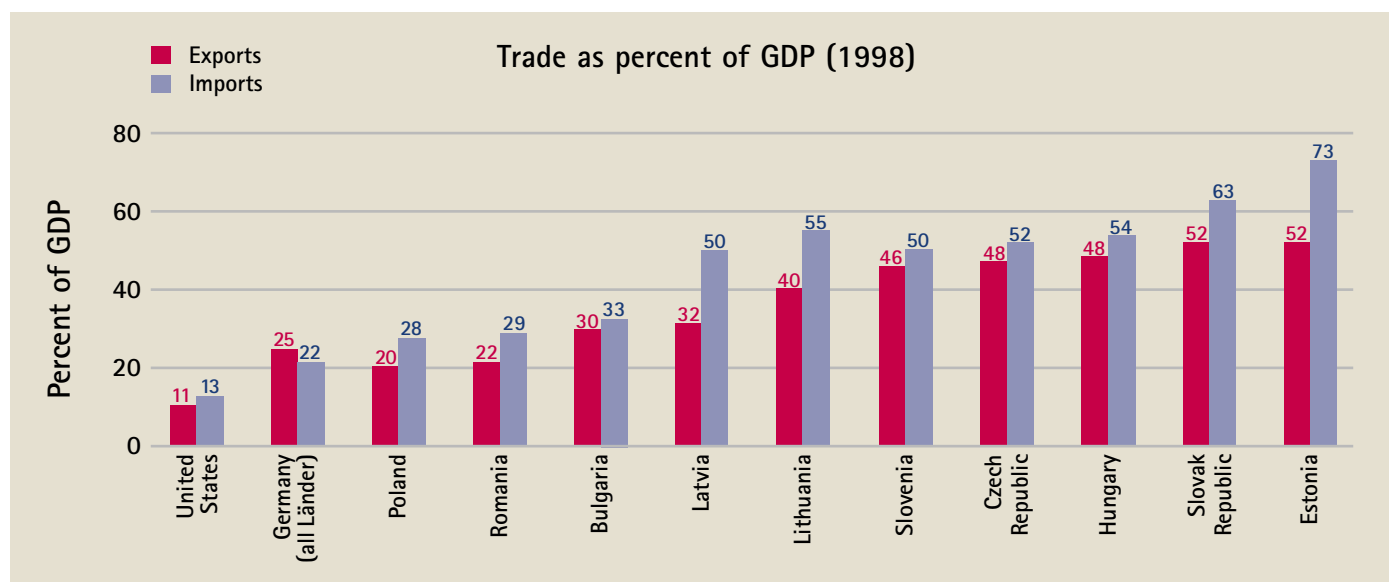
The benefit of liberating the human potential in the CEE countries has been expressed most clearly through management and entrepreneurship. The extensive survey that Accenture conducted across the former communist countries has revealed a remarkable improvement in management. Three-quarters of the executives interviewed said that the quality of decision making in their company had improved.

The new breed of CEE managers has shown itself to be open to the views of their workforces and customers, willing to delegate and able to motivate staff. However, before completing this economic revolution, these countries must deal with a critical shortage of appropriately trained managerial talent. Too often, current managers and staff still demonstrate the old mind-set of the communist past.

The fall of communism prompted millions of CEE citizens to set up shop as individual traders or small businesses.

Importance of trade to transition economies

The countries in Central and Eastern Europe are more dependent on trade than either the United States or Germany; in a number of countries imports top 50 percent of GDP.



SOURCE: EBRD ESTIMATES; US DEPARTMENT OF COMMERCE; EUSTATS

In the Czech Republic the number of entrepreneurs increased by more than a hundredfold in five years. Poland currently boasts 2 million small businesses out of a population of 39 million (by contrast, Russia has just 850,000 small businesses among nearly 150 million inhabitants).

Apart from the sheer increase in their numbers, there has been a striking change in the motives for starting a small business. A Polish study found that before 1981, "family tradition" was the main reason small businesses were founded. But today the chief motives are the pursuit of independence, personal fulfillment and better living standards.

The momentum of these changes and the continued willingness of the former communist countries to embrace new technology and new ways of living and working are making CEE businesses strong and credible competitors in the emerging global economy.

Paradox

Many of the more recent changes in Central and Eastern Europe have been driven by the desire to meet EU accession criteria. Yet there is an apparent paradox in EU membership for these countries.

Executives in those countries closest to accession, such as Poland and the Czech Republic, are somewhat lukewarm about joining the club. By contrast, enthusiasm for accession appears to be highest among executives in two of the countries furthest from membership: Romania and Bulgaria.

Indeed, the greatly improved performance (particularly in terms of increased flexibility and responsiveness) of the more successful economies has led some business leaders in the region to wonder whether EU mem-

bership might be something of a mixed blessing.

These executives are wary of certain aspects of EU membership and, indeed, of Western European business culture more generally—especially the inflexible labor markets and over-regulation with which they associate many current member states.

As György Mosoni, CEO of MOL, Hungary's leading oil and gas company, notes: "In certain respects, Hungary is more flexible than some of the EU countries in terms of the working hours and some of the other regulations. I do not see who will win in the EU. Will the EU move toward flexibility to be able to achieve competitiveness against the United States and the Far East? Or will it move towards the more rigid, centralized, nonflexible systems, which will be a step back for Hungary?"

But this is, perhaps, a cause for optimism rather than concern. The CEE countries and the EU member states have much to learn from one another. In fact, there is a very real chance that the flexibility of the people of the former communist countries, combined with their commitment to free trade, could serve to reignite the entrepreneurial spirit of the entire continent.

After years of waiting for an invitation to the EU ball, has Cinderella finally stopped looking for a fairytale romance and instead become more interested in a thoroughly modern relationship—a partnership of equals? ■



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