

Unemployment is the main problem facing young people born after the fall of the Communist regimes. Setting up one's own business is an alternative to emigration. But creativity and risk propensity are

Doing business in the East? Difficult for the young

RESEARCHES 1

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not enough, because an adequate financial system to support enterprise is lacking. Hence there is a need for committed policies able to put in place...

After years of economic and social hardship, the accession states showed a high and stable rate of GDP growth in the run up to membership (see [table 1](#)), which is likely to be continued now that they became new member states. At the same time though, unemployment rates remain often high and tend in some countries even to increase. This is especially true for unemployment amongst the young (see [table 2](#)) and in particular in rural regions. For instance, in Poland the highest unemployment rate at the end of 2002 was in the northern region of Warmia-Mazury, at almost 30%, while the lowest was in the central region of Mazowsze, at 13.9% [EIRO]. At the end of 2004, the overall unemployment rate in the Zachodniopomorski voivodship – a predominantly rural area with the worst unemployment rate in Poland – was 27,4% compared to a national rate of 19,1% [FDPA].

Partly, the former communist countries are following world-wide trends towards increased youth unemployment (at least twice the adult rate) as part of an overall transformation from industrial to post-industrial societies, and, partly, problems of

youth unemployment have their origins in an economy with structural problems, related to the legacy of communist economic systems and industrial organization.

An increasingly popular solution to overcoming this structural problem in economies of transformation – high levels of youth unemployment and threatening out-migration in particular of more highly educated and skilled young persons – is proposed in the form of youth self-employment and youth entrepreneurship. It is seen to be a significant, alternative way to integrate young people into the labour market in economies in transformation and to contribute to the overall dynamism of these economies. Young people were left out in privatisation of the assets of State-owned companies that were privatised in the early stages of transition, because of their young age and lack of political capital. It was mostly the former nomenklatura (middle and higher levels of the communist party and the State administration hierarchy) who were able to convert their political into economic capital. And, from the early 1990s until today, the labour market does not offer sufficient and decently paid jobs for a



large part of the young people who are looking for employment, particularly for those who are without skills sought after in the labour market and those belonging in minorities. Gender discrimination is also important among the young looking for employment.

Confronted with this difficult situation policies can pursue two strategies: job creation and enterprise foundation (entrepreneurship). There may be an alternative in spontaneous development, i.e. leaving the young to find their own way, perhaps by pursuing self-employment. This latter alternative may seem to be a promising way to avoid long-term unemployment and the low wage standards of the average employee. In reality, however, this alternative proves to be a difficult option for young people in Eastern Europe. The needed financial and real infrastructure is often undeveloped, particularly so for young people. They often lack the necessary skills and business reputation, and even if they are able to overcome the difficulties of getting the financial resources to start up a business, they may not be able to fix the other conditions that make a business prospective, including getting all the needed permissions in due time and finding reliable suppliers and interested buyers. Chances are that contextual difficulties, even if they may not prevent self-employment or establishing a business, may render prohibitive the expansion and modernisation of activities. This is damaging for the young entrepreneurs and the society alike, since young people in transition countries are particularly innovative. Indeed and added to

the in-born innovativeness and risk-proness typical of young age, they are the only generation who is socially born in the new system and who has consequently embodied market institutions.

Economic transformation in Eastern Europe

The wide-scale transformations of the former communist countries, in terms of the move away from centrally planned, State-owned economies, and from a single-party regime to pluralist democratic systems, have been underway for more than 15 years. However, the transformation cannot said to be over. Distinct problems, directly or indirectly related to the communist past, remain important today and influence the possibilities of young people to play a productive role and support transformation. The communist economies consisted of economies virtually entirely in the hands of the state, with very little room for private initiative (the exceptions are Poland and Hungary, where small, but persistent "second economies" emerged from the late 1960s onwards). The economic transformation in these countries faced the task of radically changing the fundamental economic, political and social institutions; the structure and functioning of the economy (in particular developing markets, introducing new actors such as banks and other financial intermediaries, restructuring the size and governance of firms, moving away from older trade patterns and integrating into the capitalist world economy); and introducing private forms of ownership and independent economic activities.

The dominant theory behind these economic

1. REAL YEARLY GDP CHANGE IN THE NEW MEMBER STATES, PRIOR TO ACCESSION

Real GDP change	2001	2002	2003	2003	2004	2005*	2006*
Czech Republic	3,1	2,0	2,9	3,7	4,0	4,6	4,1
Estonia	6,4	7,2	5,1	6,7	7,8	8,4	7,2
Hungary	3,8	3,5	2,9	3,4	4,6	4,5	4,5
Latvia	7,9	6,1	7,4	7,2	9,8	9,1	7,7
Lithuania	6,4	6,8	9,0	10,5	7,0	7,0	6,2
Poland	1,0	1,4	3,8	3,8	5,4	3,5	4,4
Slovakia	3,8	4,4	4,2	4,5	5,5	5,1	5,4
Slovenia	2,7	3,4	2,3	2,5	4,6	3,9	4,0

Source: UN/ECE (2001-2003) and ICEG EC (2003-2006) * Forecasts

transformations has for the greater part been the “Washington consensus”. This means that the emphasis in macro-economic policy-making in the 1990s has been foremost on “rolling back” the state, in particular by means of the privatization of state-owned enterprises. In this way, enterprises have been created from the “top down” by means of privatization, spin-offs from large state-owned enterprises and liquidation of state-owned assets. Each of these privatization approaches have gone to the advantage of insiders or foreign investors, not the young potential entrepreneurs. A rather neglected way of enterprise creation is the establishment of enterprises ex novo, that is, by singular individuals or families from the “bottom up”. While in many countries in the region such – often small-scale – private initiatives, although often at the survival level, have increasingly become important in creating economic growth, dynamism, and employment, attention and support from the part of the state has been relatively absent. In Romania, for instance, large-State firms have been able to survive with the help of “soft budget constraints”, while the development of the SME sector has been mostly ignored. It is the latter, however, that in recent years has contributed most to employment creation. In many countries, including Poland and Hungary, governments in the region started paying more attention to local development and support to small business creation only at the end of the 1990s.

As mentioned earlier, in sharp contrast with promising economic growth rates in Central and Eastern European countries in the run-

up to the accession are the levels of unemployment, which remain on a high level or are in some cases even deteriorating. In particular, the level of unemployment among young people remains very high (often more than two times the adult rate), even if the number of young people looking for a job is relatively modest and their participation in the labour market is low as a consequence. This is so, because young people remain for longer periods in secondary and higher education, go into the informal economy, abstain from looking for a job, or choose for out-migration.

Importance of youth entrepreneurship and small business in Eastern Europe

Youth has particular importance in societies in transformation. Indeed, it is young people who embody in the fullest way the new institutions and consequently are most pro-reform and most willing to support significant change in their economies and societies. However, young people simultaneously face a relatively disproportional part of the difficulties and strains of transformation: in a sense, they are among the victims of transformation due to lack of labour demand, the fiscal crisis of the state (in particular, social security) and disruption of the welfare state amidst surviving privileges, principally for the elderly. In particular in terms of access to the labour market young people face a serious disadvantage. The stable jobs and career paths of communist times have in smaller or greater part disappeared as a result of the collapse of the centrally planned economy. At the same time, economic restructuring and a rapid de-

2. UNEMPLOYMENT AND YOUTH UNEMPLOYMENT RATES (%) IN THE NEW MEMBER STATES, PRIOR TO ACCESSION								
	General	Youth	General	Youth	General	Youth	General	Youth
Czech Republic	8	17,3	7,3	16,9	7,8	18,6	8,3	21,1
Estonia	11,8	23,5	9,5	19,3	10,1	22,9	9,7	21,0
Hungary	5,6	10,9	5,6	11,8	5,8	13,1	6,1	14,8
Latvia	12,9	23,1	12,6	23,9	10,5	17,6	9,8	19,0
Lithuania	16,1	30,2	13,6	23,9	12,7	27,2	10,9	19,9
Poland	18,5	39,8	19,8	41,8	19,2	41,1	19,1	39,5
Slovakia	19,4	39,0	18,7	37,6	17,1	32,9	18,0	32,3
Slovenia	5,8	16,0	6,1	15,3	6,5	15,9	6,0	14,3

Source: DG for Employment, Social Affairs and Equal Opportunities and ICEG EC

industrialization have led to the enormous loss of employment in the industrial sector (up to close to half of the previous employment level in countries such as Bulgaria and Romania), which have only partially been recreated in the private, non-industrial sector. Indeed, overall employment is presently between two thirds and three fourths of pre-transition level. In some countries this even led to a "return" to the agricultural sector (particularly in Romania and Poland, but to a lesser extent also in other countries).

Not only the quantity of available employment, its division by sector and branch of activity and by enterprise size changed. Also the qualitative nature of employment changed through a tendency towards flexibilisation and an increasing lack of stable, long-term career paths. There is presently demand for higher and sophisticated technical content of labour skills and the necessity to learn continuously and adapt one's knowledge to the endlessly changing requirements of production. Apparently, these are developments that should favour the demand for young labour and skills.

However, significant is that economic growth of recent years has not led to an equivalent rise in overall employment and even less so to jobs for young people. Economic growth does thus not necessarily lead to job creation due to the increasing importance of productivity rise finalised to domestic and international competitiveness. Young people have more difficulty finding employment, and when they do find a job, it is likely to be of a precarious nature. In addition, formal figures often do not reflect unregistered unemployment, which means that real youth unemployment is likely to be even higher than reflected in national statistics. At the same time, perhaps a substantial number of young people work in the underground economy and are consequently unregistered.

In economies in transformation, the starting up of a business can therefore be a clear alternative to unemployment or seeking a job abroad. As the restructured State sector is unable to provide the amount of jobs to cover labour supply from young people (and indeed this sector substantially reduced employment), the small and medium size

enterprise sector could be an important source for job creation. Apart from diminishing social tensions, and frustration and social marginalization amongst young people, youth entrepreneurship can have two important economic results. First of all, youth entrepreneurship can lead to the creation of employment for the entrepreneur him/herself, and possibly also for other (young) members of the local community, although most job creation takes place in well established and growing firms.

Secondly, youth entrepreneurship might involve innovative activities that can have beneficial consequences for the (national and local) economy and lead to increased dynamism and competitiveness of the economy. To be sure, young people lack experience and consequently may have difficulties in managing successfully the intricacies of innovation. However, they may be less conditioned by past experiences and more open to novelty and thanks to this they could prepare tomorrow innovation based on very innovative ideas. They are more prone to support discrete innovation



than elder entrepreneurs, who are instead better equipped to implement incremental innovation. In the particular context of transition countries, an additional advantage of young entrepreneurs is that they were economically and socially born in the new system and consequently they embody the new market and innovation friendly institutions. In particular, in the small and medium size enterprise sector, such innovative ideas and behaviour can lead to diversification, flexibility and adaptability, and can foster the positive segment of “creative destruction” that Joseph Schumpeter identified as so significant for economic development.

Obstacles and difficulties of youth entrepreneurship

The start-up of new businesses in economies in transformation faces a number

_Unemployment levels remain very high, but the number of young people in search of a job is relatively small. This is because they stay in school for a longer time, get involved in the informal economy or emigrate

of difficulties, in particular when young people are involved. In transformation settings, the wider cultural and social context often does not provide incentives for entrepreneurship. Also, a certain continuity in behaviour and attitudes from the communist past – the “habits of the heart” – might be expected, that the problematic experiences with transformation in general and privatisation in particular have reinforced, even if many countries have undergone drastic transformations not least in youth culture. In Eastern Europe, social and cultural acceptance of entrepreneurial behaviour – pro-active, individualist – sits uneasy with the dependent, conformist, and collectivistic forms of behaviour of the past (“Homo Sovieticus”). One cannot, of course, generalize here, as there are significant differences between different countries in the region, rural and urban areas, jobs in the branches of old industrialisation and new branches, as well as between older and younger generations.

Institutional support, education and training with regard to skills and knowledge necessary for successful enterprise are often unavailable and financial and real services and infrastructure are undeveloped. As direct experience with forms of entrepreneurial activities and familiarity with business practices and related tacit knowledge are seldom at hand, the transmission of codified and re-contextualised knowledge and entrepreneurial skills through formal and informal education becomes important if entrepreneurial behaviour among young people is to emerge. Furthermore, the connection between formal educational curricula and local economies and business communities are in many of the new member states far from optimal, leading to a mismatch between the skills young people learn and those demanded by the labour market.

Also, the administrative and regulatory framework is often burdensome, outdated and not conducive to entrepreneurship. Targeted policies of small business promotion and financial, operational, logistical, and post start-up support are often lacking. Entrepreneurs perceive the instability of macroeconomic policies as conducive to business uncertainty,



regulations as unresponsive to business needs, taxes as too high, and bureaucratic structures as non-transparent and uncooperative (for instance, in the form of complex and lengthy licenses). In addition, as mentioned earlier, the State can be non-cooperative with SMEs by being disproportionately favouring large enterprises, perhaps due to the latter capturing the former. In transition countries SMEs are typically weak in lobbying for more favourable conditions and young entrepreneurs are nearly irrelevant in doing so.

The lack of access to finance through regular credit channels and the conditions attached to it are usually an important obstacle for setting-up small firms and even more so for supporting investment in their upgrading and growth. Young people have a particularly hard time finding the start-up and working capital to found a business, since the typical financial sources of small businessmen – own savings and relatives' and acquaintances' support – are also modest in the case of young entrepreneurs, due to the weakness of their social and business networks. Banks are averse to provide small loans to young entrepreneurs, in particular because young aspiring entrepreneurs have no business reputation, cannot provide collateral to underpin loans, and lack in soundly elaborated business plans.

Support to small business creation

Much of the policy-making towards development and economic growth since the early 1990s has had more of a regressive character – combating unemployment and industrial decline – rather than a progressive one, stimulating innovation and competitiveness. For small business creation and entrepreneurship, it is exactly this element that is often missing: a supportive institutional, infrastructural and governmental environment. Also the support by business associations, chambers of commerce and similar private or mixed organisations is typically weak or inexistent in the case of young entrepreneurs, since those organisations support primarily their long-lasting members. There are at least three areas where in particular local governments could intervene much more effectively and with wider social benefits.

The first area is that of information, awareness-building and education. For young people to make a conscious choice for entrepreneurship they need to be aware of its potentialities as well as risks. But there is also the need to disseminate entrepreneurial attitudes to young people that can be useful in a variety of jobs in an innovative and competitive context. In the case of a person deciding in favour of pursuing an entrepreneurial career, there emerges the need for much more specific training in business and entrepreneurial skills.

Promotion programmes of youth entrepreneurship need to deal with the translation of a business idea into a convincing business plan, knowledge of how to run a business on a daily basis, including management and technical skills, administrative and legal knowledge, and financial/accounting skills.

The second area that is relevant for policy-making is the provision of actual start-up and development assistance. Although in general access to capital does not constitute a prohibitive obstacle for starting a business, for young people the situation may be less favourable. Here, local governments as well as other institutions such as business organisations, business angels and mentors from among established entrepreneurs can support young people by providing micro-credit, mutual credit guarantee schemes, and venture capital funds. These solutions would provide a more balanced access to regular capital channels, as those young people who do not have access to informal resources often have to face the discrimination and risk-aversion of banks against young entrepreneurs.

Next to financial support, and as a third element, young entrepreneurs are in need of logistic support in terms of the actual premises, equipment and materials, as well as support with legal matters for their business to operate normally. Here, local governments and other organizations can support young people by offering premises and the usage of equipment at favourable conditions through different channels.

Finally, it is essential to underline the need for post start-up support. It is clearly not enough to help young people merely to start up new businesses; continued support, mentoring, and legal and financial advice is

crucial to contribute to the development of new small enterprises into competitive flourishing and expanding businesses, rather than to create unstable forms of precarious self-employment.

In conclusion, a number of cautions with regard to youth entrepreneurship need to be made. One such caution is that youth entrepreneurship could be a general solution to youth unemployment. It is clear that youth entrepreneurship, even if benefiting from a supportive environment, cannot resolve the problem of structural youth unemployment in economies in transition. Only a small number of young people will be able to pursue entrepreneurial activities in a successful way. The wider effects on youth employment of such efforts should not be overestimated. Indeed, failure rates among young entrepreneurs are particularly high. Only few of those businesses surviving competition and attracting a sustained demand will actually be able to transform themselves in medium-sized companies that can play a more substantial role in employment creation. Therefore, it is unlikely that youth entrepreneurship can contribute substantially to employment creation, while the promotion of entrepreneurship is not desirable if it leads to precarious job situations, disproportional risks, and uncertain future outlooks. These

considerations stress that policies supporting youth entrepreneurship are particularly demanding and their outcome uncertain. They have to include incentives to education upgrading; incentives and support to investment innovation, including both financial resources, real services and business infrastructure; the creation of a supportive context, including growth policies; role models, for instance by means of tutorship by successful entrepreneurs. Most important is the distinction between job creation and innovation by means of youth entrepreneurship. In the economies in transformation, the former is often not an active choice for an entrepreneurial career, but rather a necessity in order to avoid long-term unemployment and a refuge from poverty. Although in some cases youth entrepreneurship can effectively contribute to the integration of marginalized young people into society, self-employment under these conditions does not mean the creation of a steady, decent, and well-remunerated form of employment. Other policies have proved to generate superior results, in particular the support given to dynamic competitive firms to further expand their activity.

One should also be realistic in that local markets in depressed areas are often unable to provide sufficient demand as the purchasing power of the population is too low. This makes it very difficult to create dynamic, profit-generating, and investing businesses. Here, the risk is that the creation of new business simply results in the mere displacement of existing businesses, leading to a zero-sum game. In order for youth entrepreneurship to be successful and to have beneficial results for the wider society, it is important that governments not only provide the necessary support to young starting entrepreneurs (in terms of training, logistical support, financial support), but particularly to stimulate and support investment in innovation and development and competitiveness of the enterprises established by young entrepreneurs, in due consideration of those sectors that might be promising in the local context, that have export potential, and enhance local competitiveness.

That Seminar in Milan

On 27 January, a seminar on "Youth Entrepreneurship and Local Development in Eastern Europe" was organized by the Unidea/Unicredit Foundation together with the Joint European Master in Comparative Local Development of the University of Trento and the OECD/LEED programme. The seminar, in which international experts from both East and West participated, dealt with crucial issues that the post-communist economies face in the process of transformation, including high levels of youth unemployment, threatening out-migration of young people, and the absence of social cohesion. The debate focused among other things on the role of youth entrepreneurship in the creation of employment and innovation, the specific barriers young people face in economies in transition, and the role of policy-making in stimulating young people into setting up businesses. A book publication based on the seminar's contributions is in preparation.