

# **POLICIES AND SOCIO-ECONOMIC CONDITIONS OF PRIVATE ENTERPRISE DEVELOPMENT IN TRANSITIONAL ECONOMIES**

Georgine Fogel, Salem International University, [fogel@salemiu.edu](mailto:fogel@salemiu.edu)

## **ABSTRACT**

Implementation of market reforms has been a lengthy process in the countries of Central and Eastern Europe (CEE). Differences exist between individual countries in the scale of the reform process and the type of socio-economic development for entrepreneurial ventures. Hungary has been in the fore-front of the transition from a centrally planned economy to a market economy. This paper evaluates policies and socio-economic conditions of private enterprise development in the transitional Hungarian economy. On-site surveys and personal interviews were conducted among small business owners to analyze perceptions of five selected factors of socio-economic conditions and ratings of satisfaction with seven policy items crucial in supporting entrepreneurial activities. An integrated model of entrepreneurial venture creation was used to analyze policy implications to assist private enterprise development in Hungary and other countries of the region.

## **INTRODUCTION**

Entrepreneurship is crucially important for the market process and economic development. Promoting entrepreneurship is especially important in the generation of market functions in transitional economies in Central and Eastern Europe (CEE). Socio-economic conditions of entrepreneurship in general refer to a combination of factors that play a role in the development of entrepreneurship. Studies were conducted on entrepreneurial operations in various countries according to which the likelihood of new venture creation is greater in countries that keep rules and regulations at a minimum, offer tax and other incentives, and provide training and counseling services to start-up entrepreneurs (Dana, 1987, 1990). Socio-economic factors such as the availability of financial resources, large size urban areas, and the presence of universities for training and research were found to be important in increasing the rate of new venture creations (Pennings, 1982). Previous research also found that entrepreneurs often face obstacles including lack of financial assistance, lack of information on business and management practices, excessive taxation, and high rates

of inflation (Young & Welsch, 1993 and Fogel, 2001 and 1994).

Scholars have proposed a variety of policy options for developing entrepreneurship including provision of venture capital funds, tax-based incentives, government procurement programs, protection of proprietary ideas and innovation, investment in education and research, recognition of entrepreneurship and minimization of entry barriers (Goodman, Meany, & Pate, 1992; and Zapalska and Fogel, 1998). There seems to be an agreement among researchers that the more conducive the business environment, the more likely new businesses emerge and grow. Individuals are more likely encouraged and feel competent to start a business with a social environment that values entrepreneurship, and when various opportunities are available and entrepreneurs have sufficient knowledge and skills required to start and manage a business.

The encouragement of private business activity has been an important element in the economic transformation of Central and Eastern Europe (CEE). Previous research indicates that small business development in CEE countries has been greatly influenced by the country's macro-economic factors such as inflation rates, price stability, interest rates, credit conditions, capital inflows and outflows, and the availability of economic inputs (capital, labor, material, and technology). This paper examines socio-economic conditions of private enterprise development in one of the most progressing CEE country, Hungary, to offer insight in to policy making recommendations for improving entrepreneurial venture creation and small business growth in transitional economies.

## **LITERATURE REVIEW**

Entrepreneurship, the act of creating a new business, is a multi-dimensional process. Approaches to studying entrepreneurship include the characteristics, traits, and behavior of individual entrepreneurs, as well as, socio-economic and political conditions that either promote or hamper the creation and development of entrepreneurship.

Hannan et. al. (1977) focused on the importance of socio-economic conditions in venture creation,

proposing a “population ecology” paradigm. According to this, entrepreneurship may not prosper in societies where the majority views it with suspicion. Similarly, Gnyawali and Fogel (1994) noted that favorable attitudes and public support toward entrepreneurship may be as important to motivate business people as the availability of loans, technical assistance, physical facilities, and information. Under socialistic economy, public attitude toward entrepreneurship in CEE countries has been negative for a long time. With the introduction of market reforms, private enterprise development became one of the priorities of many CEE countries. However, progress in encouraging entrepreneurship and establishing socio-economic conditions supportive of entrepreneurial behavior has been burdensome. Swanson and Webster (1992) reported that negative public attitudes in the Czech and Slovak Republics discouraged many entrepreneurs. Studies conducted in other CEE countries revealed that despite the rapid development of economic reforms and success in privatization, entrepreneurs in Hungary and Poland continued to face obstacles that inhibited the growth and development of their business ventures (Fogel and Zapalska, 2001).

## **SOCIO-ECONOMIC CONDITIONS**

The concept of socio-economic conditions of entrepreneurship is intended to include those forces and elements external to the organization’s boundaries that affect and are affected by an organization’s actions as well as the more general economic, socio-cultural, political-legal, and technological influences that provide the broader context for entrepreneurial growth and development (Bruno et al. 1982, Pfeffer et al. 1978). Studies found that entrepreneurship prospers in societies where most members view it with a favorable attitude. Societies and cultures that value entrepreneurship tend to develop societal systems that encourage entrepreneurship (Vesper, 1983). For example, it was found that among the Chinese, entrepreneurial role models encourage people to go into business and are often supported by close networks of family members and relatives (Kao, 1993; Siu & Martin, 1992). Programs that develop societal awareness toward entrepreneurship seemed to have a positive effect on small business development and growth. Examples can be found in many other countries. Research also shows that tax and other incentives encourage the establishment and growth of entrepreneurial ventures (Davidsson, 1991).

## **FINANCIAL ASSISTANCE**

A number of researchers have found evidence on the impact of fiscal and regulatory environment on entrepreneurial activity. Kent (1984) and Kilby (1971) noted that entrepreneurs require financial assistance for at least one of three purposes: to diversify or spread the start-up risk, to accumulate start-up capital, and to finance growth and expansion. While the availability of financial resources can be a major predictor of the frequency of business start-ups, many lenders in CEE countries are unwilling to invest in high-risk projects or tend to withhold support until the firm has been established successfully (Pennings, 1982). In most developing countries and emerging market economies, venture capital companies and alternative sources of financing are almost non-existent. Thus, a paradox emerges: entrepreneurs cannot start business without financial assistance; at the same time, they do not have access to financial institutions and often cannot secure financial assistance because of lack collateral or prior business experience (Gnyawali and Fogel, 1994; and Zapalska and Fogel, 1998).

## **NON-FINANCIAL ASSISTANCE**

In addition to capital as the major resource needed to carry out the entrepreneurial function, market incentives and infrastructure create entrepreneurial opportunities to be exploited (Kilby 1971 and Stevenson 1985). Studies show that entrepreneurs need various support services in addition to financial assistance. In particular, entrepreneurs need assistance in conducting market studies, preparing business plans, acquiring loans, technology, and access to suppliers and customers. Bruno and Tyejee (1982) noted that the ability of entrepreneurs to use modern transport and communication facilities, along with the development of networks and business information systems can make a substantial impact on private enterprise development. According to Hoy et al. (1991), business incubators can play a major role in providing services to start-up entrepreneurs, especially in CEE countries where infrastructure has been underdeveloped for many years and access to modern physical facilities continues to be costly. The studies of Aldrich (1986) report that entrepreneurs spend nearly half of their time during the start-up phase in making contacts and networks with other entrepreneurs and related agencies. Business networking in general consists of attendance of trade fairs, entrepreneurial exhibitions, membership in industry associations and clubs. Networks were found to provide four essential ingredients to entrepreneurship: (1) support and motivation, (2) examples and role models, (3) expert opinion and counseling, and (4) access to opportunities, information, and resources (Manning et al. 1989).

### **ENTREPRENEURIAL AND BUSINESS SKILLS**

The level of technical and business skills has been found to be a major factor in starting and developing small businesses (Davidsson, 1991; Vesper, 1990). Unless entrepreneurs are well equipped with technical and business skills, they may not be able to overcome problems at different stages of their business development. In Sweden, both business-related experience and business education were highly correlated with the entrepreneurs' ability to start and manage a business (Davidsson, 1991). In the region of Sub-Saharan Africa, entrepreneurs suffered from barriers such as the need for following societal stereotypes and traditions, a general lack of realization of the importance of thrift, and lack of perseverance (Takyi-Asiedu, 1993). Fogel and Zapalska (2001) reported that access to entrepreneurial training and educational services are particularly important in CEE region as these countries make the transition to a market economy because for many years there has been a lack of basic business skill

development under the socialistic system. According to Swanson and Webster (1992), 30 percent of the entrepreneurs surveyed in the Czech and Slovak Republic requested training in business plan preparation, decision making, negotiation, pricing, marketing, consumer behavior, handling of cash-flow, organization, and management of the business.

### **POLICY ENVIRONMENT FOR ENTREPRENEURSHIP**

Governments can influence the market mechanisms and make them function efficiently by removing conditions that create market imperfections and administrative rigidities. They can also create an "enterprise culture" that enables entrepreneurs to take reasonable risks and seek profits (Gnyawali and Fogel, 1994). The review of literature indicates that countries where procedural requirements are kept at a minimum generally have a viable and dynamic entrepreneurial sector.

The studies of Dana (1987, 1990) and Young and Welsch (1993) found that entrepreneurs were discouraged to start a business when they had to adhere to an excessive number of rules and procedures. Extensive procedural requirements for registration, licensing, reporting, and paperwork in general hinder entrepreneurial activities. At the same time, favorable tax laws, incentives, and preferences to small businesses seem to facilitate entrepreneurial venture creation and growths. Studies conducted in CEE countries found that many small businesses considered paperwork time consuming and cumbersome and incentives and tax laws discouraging rather than encouraging to small businesses (Dana, 1987, 1990; Young & Welsch, 1993; and Fogel, 1994).

### **FRAMEWORK FOR SOCIO-ECONOMIC ANALYSIS**

A major premise of this paper is that to start a business, entrepreneurs first should perceive profitable opportunities to exist. Once the opportunity has been recognized, entrepreneurs should feel confident about having the necessary skills to go into business as well as take initiative for starting the business. To the extent that opportunity is the possibility of new venture creation, this paper proposes that entrepreneurial activities tend to be higher in economies that are deregulated, where market mechanisms operate freely, and where entrepreneurs face few barriers to entry. In light of this, the paper contends that government policies and procedures affect the business opportunity and ability to enterprise. In order to examine the socio-economic

conditions of private enterprise development in Hungary, the study utilized Gnyawali and Fogel's (1994) conceptual framework. Five socio-economic factors were selected for analysis: (1) public attitude toward entrepreneurship, (2) promotion of entrepreneurial success, (3) training of entrepreneurial skills, (4) recognition of entrepreneurial success, and (5) economic growth and market opportunity for entrepreneurs. In addition, needs and expectations for financial assistance, non-financial assistance, and business skill training were analyzed to reflect the perceptions of entrepreneurs about the difficulties and assistance needed in entrepreneurial operations in Hungary. Finally, the study examined policies and procedures for entrepreneurial development using satisfaction ratings of seven policy items considered to be crucial for small business development: (1) licensing and registration requirements, (2) representation and functioning of small business networks, (3) laws and regulations for entrepreneurship, (4) filing and paper work, (5) preferences for small businesses, (6) taxation, preferences, and incentives, and (7) credit terms.

## RESEARCH METHODS

The research method used included mail surveys, telephone, and personal interviews of small business owners and operators in Hungary. Assistance for directories and contact lists was received from the regional offices of the Hungarian Chamber of Commerce, the National Association of Small and Medium Size Enterprises (SME'S), the Ministry of Commerce and Industry in Hungary, and the Hungarian Trade Commercial Office in New York. The sample included 320 small businesses having operations for at least one year and having an initial capital investment of \$8,000-10,000 (1.5 million Hungarian Forint). Data were collected in a three-year period from 1998 through 2000.

The questionnaire elicited information about the (1) characteristics of the respondents: size and nature of operations, business objectives, educational background, level of employment and start-up capital; (2) perceptions of five socio-economic conditions of entrepreneurship including public attitude toward entrepreneurship, promotion and recognition of entrepreneurial success, availability of training of entrepreneurial skills, and economic growth and market opportunity for entrepreneurs; (3) needs and expectations for financial assistance, non-financial assistance, and entrepreneurial and business skill training; and (4) satisfaction with seven policy and procedural requirements for entrepreneurs:

licensing and registration, small business networks, filing requirements, preferences for small business, taxation including incentives and exemptions, and credit terms for small businesses. In addition, open-ended questions asked respondents about difficulties in business operations and hindrances to small business development in Hungary.

## FINDINGS

### Characteristics of Respondents

Table 1 presents data on the nature of the respondents. The average length of operation of the businesses surveyed was 3.2 years. One in five (22%) had been in business for five years. Thirty two percent reported small-scale manufacturing or production in plastics, electrical components, timber processing, wood working, and food production. About two-thirds (68%) indicated service activities including real estate, engineering design, computer technologies, restaurant operations, travel, tourism, retailing, consulting, brokerage, and professional services. The majority (42%) had less than 10 employees. About 27% reported more than 10 but less than 30 employees, and close to one third had more than 30 employees.

Hungarian entrepreneurs were found to be well educated. About one third of the businesses indicated college or university education. However, only 18% reported formal business training or prior business experience. The primary financing method used for start-ups was personal savings (57%). Many participants maintained full-time employment to be able to support the business. Friends and family members were mentioned by 18% as the major source of financial assistance. Reasons for starting the business included: market opportunity (33%), supplement family income (30%), unemployment/company layoff (20%), and being independent (17%).

### Socio-Economic Conditions

Data on the perceptions of entrepreneurs on the five factors identified as socio-economic conditions of entrepreneurship in Hungary are presented in Table 2 and Figure 1. Data analysis consisted of mean calculations of each of the five factors on a scale of 1-4, where 1=must be improved, 2=fair, 3=average, and 4=good. The highest rating was reported on "economic growth and market opportunities for entrepreneurs" (M=2.76). "Public attitude toward entrepreneurship" in Hungary was rated fairly high (M=2.44). The lowest rating (M=2.03) was observed on "promotion of entrepreneurial success" with more than one third (35%)

reporting it as “must be improved.” “Entrepreneurial training” and “recognition of entrepreneurial success” were reported mostly as “fair” (M=2.13 and M=2.10) with the majority (42% and 38%) rating them as “must be improved.”

The study found that many Hungarian entrepreneurs benefited from the change in macro-economic conditions introduced by the Hungarian government as a gradual process of market reforms and market liberation. In fact, socio-economic conditions in Hungary provided opportunities for citizens to start experiencing with small business ventures as early as 1968, under the so called New Economic Mechanism (NEM). Although the NEM failed to bring about a functioning market economy, it accomplished an internal decentralization process and a gradual opening to the West which exposed Hungarian enterprises to a functioning market economy.

Historically, the 1980's marked an era of more radical economic reforms in Hungary. In the mid 1980's, the government created a comprehensive legal framework to encourage the establishment of private enterprises. A series of new laws (Company Act, Foreign Investment Act, and Transformation Act) passed in 1988-89 provided a basic guideline permitting state enterprises to transform themselves into corporate entities. Due to these developments, the 1990's was a period of dramatic growth of the small business sector in Hungary. Today, Hungary is one of the fastest growing economy in the CEE region, with GDP expanding by an average of 4.7% annually.

The Hungarian entrepreneurs surveyed exemplify people who were able to realize their dreams and develop their potential. The best people, the most highly skilled workers and best managers, voluntarily left the state sector to start their own companies or work in small business ventures. From the open-ended comments, it became evident that many Hungarian entrepreneurs became successful due to their entrepreneurial skills and talents which was an essential and scarce resource in the post-communist environment.

However, many Hungarian businesses indicated problems traceable to lack of professional management skills. Particularly, it was noted that in the first few years of operations, businesses had difficulty in managing cash flows, finding external financing, and sustain growth in operations and product development.

Overall, the study found that the elements of the socio-economic environment affecting private enterprise development in Hungary include the importance placed by society on entrepreneurial values and behaviors. A larger proportion of experienced entrepreneurs and role models may result in a higher

societal recognition of entrepreneurial performance and a higher likelihood and ability to enterprise.

The study confirms that certain basic institutions are necessary for private enterprise development as guiding structures and patterns of entrepreneurial behavior. For example, it is important to develop forms of economic motivation for individuals and organizations to be innovative and productive. Understanding risk-taking and entrepreneurial decision making requires major cultural changes for societies that were tightly controlled for decades. A broad cultural acceptance of entrepreneurs and enterprising behavior is necessary for continued growth of the private sector. Institutional policies and regulations must guide as well as protect private property rights, freedom of enterprise, fair competition, and entrepreneurial decision making based on market signals.

The results of the survey reveal that socio-economic conditions in Hungary triggered private enterprise development by allowing privatization and small business venture creation as part of the economic transition from socialism to a market economy. However, socio-economic conditions should be further improved to meet the need of the entrepreneurs. The study found that the promotion and recognition of entrepreneurial success and the training of entrepreneurial skills in Hungary must be improved.

Short-term interventions may include programs such as the best-entrepreneur-of-the-year award, provisions of trade fairs, and rewards of entrepreneurial activities to increase overall societal awareness and appreciation of entrepreneurship. A possible long-term policy approach is to introduce entrepreneurial values in the educational system, such as risk-taking behavior, profit incentive, and entrepreneurial skills and attitudes. Especially important is the partnership of universities and representatives of small business interest groups such as the Chamber of Commerce, National Association of Entrepreneurs, and industry and trade associations to jointly promote and assist entrepreneurial training and business skill development.

### **Small Business Needs and Expectations**

Data on financial, non-financial assistance and entrepreneurial business skill training are presented in Table 3. In all three categories, there was a considerable difference between what Hungarian small businesses received and what they desired.

The most desirable form of **financial assistance** noted was tax incentives and preferences. Close to half the businesses surveyed (48%) reported a need for more tax incentives. Compared to the need, the ratio of businesses receiving tax allowances was only 6%.

The second major type of financial assistance required included low-cost, long-term loans, and venture capital/project financing. Close to half (42%) desired low-cost, long term loans and one fourth (22%) expressed a need for venture capital and project financing. Contrary to this, the pattern of financial assistance received reflected an overwhelming reliance on personal sources. A third (34%) of the businesses used borrowing primarily from friends and family and about one in five (28%) relied on short-term credit financing. Many of the businesses noted that until the end of 1991, there were very limited incentives designated to help small business financing. Interest rates were extremely high and the banks used stringent lending requirements which in principle required entrepreneurs to provide evidence of incorporation, registration by a local municipality, a business plan, and relevant financial data. Private property was needed for collateral, and in most cases, banks preferred to secure loans with real estate.

In a market economy, financial institutions constitute a critical factor in entrepreneurial growth. In Central and Eastern Europe, the pace of change in financial reforms has been slow. The poorly developed and inefficient banking system was noted as one of the main obstacles of small business development in the region. Inflation rates continued to be high for borrowing and banks did not offer preferences to small businesses rather they used the same criteria for evaluation in business loan requests as for large state-owned companies. Lending to small businesses was perceived mostly as a risky proposition which resulted in a practice of charging high interest rates. Other difficulties posed for small businesses included the ability to provide credit history. In general, most entrepreneurs lacked sufficient collateral and had only a small amount of capital, most of which was tied up as working capital. This indicates that private enterprise development was severely hindered in the region. There is some evidence that as entrepreneurs establish their reputation, access to bank loans may become easier to obtain.

Overall, we can conclude that entrepreneurial development in Hungary was hindered greatly by the lack of preferential rates for borrowing. The implication is that preferential credits, low-cost, and long-term loans increase the likelihood and ability to enterprise, therefore, these are highly encouraged for private enterprise development in Hungary.

### **Non-Financial Assistance**

Hungarian businesses were asked to list the types of non-financial assistance received and desired. According

to the data, the most desirable non-financial assistance were business network development (44%), small business management training (40%), and technical assistance, mostly management information system development (30%). The study also found that one in 10 of the businesses were interested in utilizing services of incubator centers and industrial parks.

Compared to the support needed, the majority (35%) relied on friends and family for support of the business. Personal networking and assistance by economic development agencies, including the Chamber of Commerce, local trade organizations, fairs and industry shows, were noted as the second most important non-financial support perceived important in entrepreneurial development. About one fourth (19%) of the businesses reported participation in management training seminars and programs, while close to half (40%) indicated it as desirable.

Overall, the survey found that non-financial assistance received by Hungarian small businesses was quite limited. Entrepreneurs were primarily depending on support from friend and family. Management training, technical assistance, information technology, business network development, and trade fairs were highly desirable by the respondents. Providing these services to Hungarian entrepreneurs could increase both the likelihood and ability to enterprise.

### **Entrepreneurial and Business Skills**

Respondents were asked about the availability and need of entrepreneurial training. About half the respondents (52%) desired more management training programs including marketing studies, sample business plans, customer data analysis, information system development, and advertising. It was also found that one in five of the businesses desired consulting services and case study opportunities.

Businesses that survived seemed to have a product strategy which focused on either a unique product or cost advantage. A general pattern of market behavior observed among the Hungarian small businesses surveyed was willingness to seek out customers, concern for high quality products and services, continuous improvement in products and operations, and focus on market factors in decision making.

Despite these achievements, the majority of businesses reported a strong need for guidance and expertise on to select product market strategies, design internal structures, and learn how to be efficient in a global economy. In fact, many of the respondents contributed their success to trial and error. Successful businesses seemed to make decisions based on intuition,

luck, managerial insight, or a combination of these. A large majority of Hungarian entrepreneurs (40%) expressed a need for advice on how to identify customer needs and analyze customer related data and information.

Entrepreneurial and business skills are crucial in private enterprise development. Socio-economic conditions that can enhance the entrepreneurs' ability to start and manage a business may include short term management training seminars, case studies, short courses, workshops, and seminars on business skill development. A long-term recommendation is to reform the educational system to include a greater emphasis on the development of entrepreneurial skills, values, and behavior.

### **Policy Environment for Entrepreneurship**

Satisfaction ratings of policies and procedures for entrepreneurial development in Hungary are presented in Table 4 and Figure 2. Small businesses were asked to rate their satisfaction with seven items identified as "policies and procedures for entrepreneurial activities in Hungary." Ratings were on a 1-4 scale where 1=must be improved, 2=fair, 3=average, and 4=good. The highest rating of satisfaction was reported on licensing requirements (M=3.05). The next highest satisfaction was the availability of business networks (M=3.01), only 10% reporting it as "must be improved."

The fact that the majority of businesses reported average satisfaction with licensing requirements implies that the laws of the 1980's seemed to facilitate the process of entrepreneurial development. Satisfaction with laws and regulations was half-way between fair and average (M=2.6). Filing requirements and paperwork were rated as better than "fair" but less than "average" (M=2.48). Some respondents perceived paperwork as cumbersome which created difficulties in operations.

Three types of policies were rated with low level of satisfaction. Close to half the businesses (46%) rated credit terms as "must be improved." The mean rating indicated less than "fair" (M=1.76). The survey found great dissatisfaction with government credit policies. The high level of nominal interest rates, combined with an instability in real rates, discouraged private borrowing in the 1990's. Regarding future prospects for business growth, most entrepreneurs saw credit terms and the lack of low-cost, long-term borrowing as a main barrier.

Taxation was rated as the second lowest in satisfaction with a mean of 1.88, the majority reporting it as less than "fair" and "must be improved." Seventy two percent (72%) of the businesses complained about the lack of preferences in tax incentives. Many reported burdens from taxes and payment arrears. Preferences to small businesses was rated as the third lowest in

satisfaction (M=1.92). The lack of preferences was seen mostly as a difficulty to small business development.

In summary, the findings reveal that although entrepreneurial growth in Hungary increased substantially in the last decade, Hungarian entrepreneurs are faced with many difficulties. The study suggests that Hungarian entrepreneurs had the opportunity to enterprise. However, we can also infer that the ability and likelihood to enterprise were hindered by the lack of preferences given to small business. Insufficient business skill training and limited financial and non-financial assistance to entrepreneurs further created barriers to entrepreneurs. Continued growth of entrepreneurship in Hungary will depend largely on whether the small business sector can obtain preferential treatment in financing, business skill development, and government taxation.

In summary, the experience with a decade of systemic transition in Hungary suggests that although macro-economic reforms and privatization are necessary to stimulate change, they are insufficient to create a competitive market system. An effectively functioning market requires expanding private enterprise and strengthening institutions that support private sector growth and development. Among the most difficult challenges in the CEE region is establishing effective capital markets. An important economic policy issue for regulatory authorities now is finding how best to support starting over. Overall, the study reveals that policy issues of private enterprise development in Hungary should focus more closely on developing institutional programs and policies that reflect the needs and concerns of the small business community.

## **CONCLUSION**

Entrepreneurial development and growth continues to be a priority in CEE countries. Hungary has made much progress in entrepreneurial development. The study of the policies and socio-economic conditions of small business development in Hungary confirms that several factors contribute to private enterprise development. Although financing is important, often it is not the most critical bottleneck in entrepreneurial venture creation. Many times, the lack of management knowledge can make small business' survival and expansion problematic. The provision of technical support, tax incentives, and venture capital funds are equally crucial in private enterprise development. Access to low-cost borrowing along with support facilities such as incubator centers and industrial parks, combined with opportunities for entrepreneurial and business training, promotion of entrepreneurial success, small business

networks, and a greater societal awareness of entrepreneurship are vital forces that can either assist or hinder private enterprise development.

The findings indicate that despite the rapid introduction of market reforms in the legal principles favorable to private businesses and the Hungarian government's aggressive reforms in macro-economic measures and price liberalization, there has been considerable dissatisfaction with the government not having done enough for small businesses, particularly in the offering of favorable credit terms and tax preferences. The study found that the lack of preferences, high taxation, and the unavailability of low-cost, long-term financing hindered private enterprise development in Hungary.

Based on these, one of the primary policy recommendation for assisting private enterprise development in Hungary and other CEE countries is the design of programs that offer opportunities for low-cost borrowing and venture capital fund financing. Capital enables small enterprises to innovate and use advanced technologies. It is also the primary means of growth. With the accession of Hungary to the European Union, Hungarian small businesses can benefit substantially from developing export capabilities. However, in order to develop competitiveness in export categories, Hungarian entrepreneurs must innovate, invest in technology, and use market-based management and marketing practices. Another policy recommendation for assisting Hungarian enterprise development is the greater offer of technical support and access to technology and business information systems. The third type of policy improvement should focus on the development of tax incentives and preferences to small businesses. There also needs to be an increase in the availability of entrepreneurial and business training programs and the networks for small businesses. In sum, financial and regulatory institutions in Hungary and other CEE countries are advised to create a more "enterprise-friendly" culture that offers incentives and recognition of entrepreneurial talent while it supports entrepreneurs both financially and non-financially.

A major thesis of this paper is that entrepreneurship can flourish when the socio-economic conditions motivate and enhance the entrepreneurs' ability and willingness to start a business. The findings of this paper contribute to the study of private enterprise development by supporting the notion that competitive markets do not emerge merely from macro-economic policy reforms. Rather, they are built on the foundation of institutions that create and sustain entrepreneurial behavior. Particularly important for future research on entrepreneurship is to further examine the types of

policies and institutions that can support entrepreneurial development in transitional economies. The conceptual framework and analysis of this paper is applicable to both policy makers and researchers interested in improving entrepreneurial development in other countries.



**Table 1**  
**Nature of Business Operations**

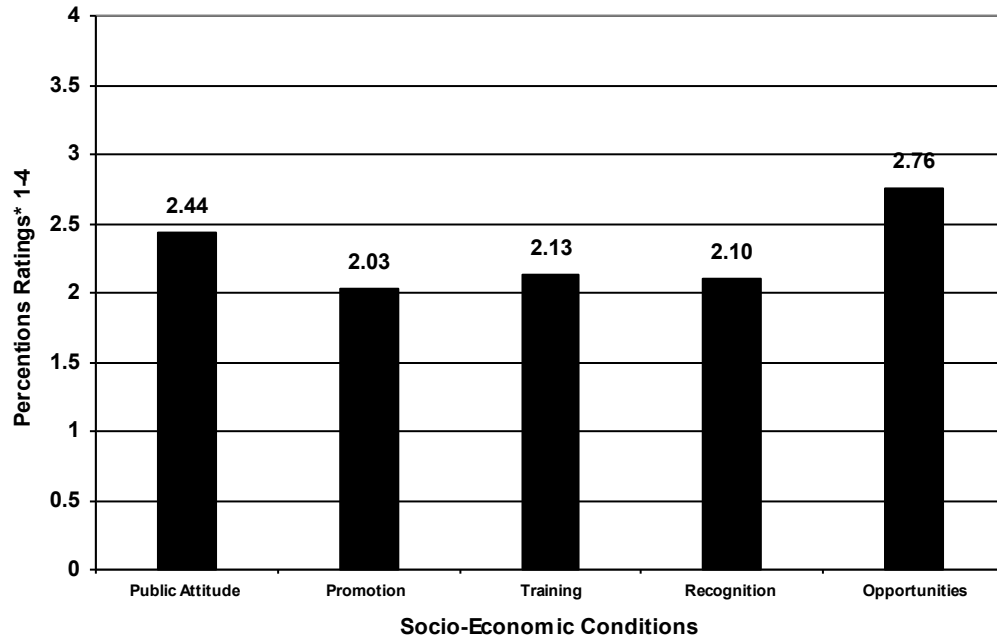
<b>Length of Time of Business Venture</b>	<b>Percentage</b>
Five Years	22%
Three Years	63%
Two Years	10%
Over One Year	5%
<b>Type of Business Activities</b>	
Service Sector (real estate, Manufacturing and Production)	68%
	32%
<b>Size of Business</b>	
Less than 10 Employees	42%
10-30 Employees	27%
More than 30 Employees	31%
<b>Reasons for Starting Business</b>	
Recognized Market Opportunity	33%
Supplement Family Income	30%
Unemployment/Company Layoff	20%
Be Independent	17%
<b>Initial Financial Resources/Start-up Capital</b>	
Bank Loans	10%
Company Assisted Funds (compensation at company closing)	15%
Borrowing from Friends or Family	18%
Personal Savings	57%
<b>Owner's Education/Business Training at Start-up</b>	
College or University Degree	33%
Formal Business Training/Experience	18%
Technical Degree or Diploma	46%
High School and Self-Training	3%

**Table 2**  
**Socio-Economic Conditions for Entrepreneurship**

<b>Socio-Economic Conditions</b>	<b>Improved</b>	<b>Must Be</b>	<b>FairAverageGood</b>		<b>Mean*</b>
	(1)	(2)	(3)	(4)	
Public Attitude Toward Entrepreneurship	22%	22%	46%	10%	2.44
Promotion of Entrepreneurial Success	35%	32%	28%	5%	2.03
Training of Entrepreneurial Skills	42%	18%	25%	15%	2.13
Recognition of Entrepreneurial Success	38%	22%	32%	8%	2.10
Economic Growth/Market Opportunity For Entrepreneurs	15%	22%	35%	28%	2.76

\*Rating: Scale: 1-4, where 1=Must Be Improved, 2=Fair, 3=Average, and 4=Good

**Figure 1: Perceptions of Socio-Economic Conditions for Entrepreneurship in Hungary**



\*Scale on 1-4, where 1=Must Be Improved, 2=Fair, 3=Average, 4=Good

**Table 3**

**Small Business Assistance and Entrepreneurial Business Skill Development**

**Percentages**

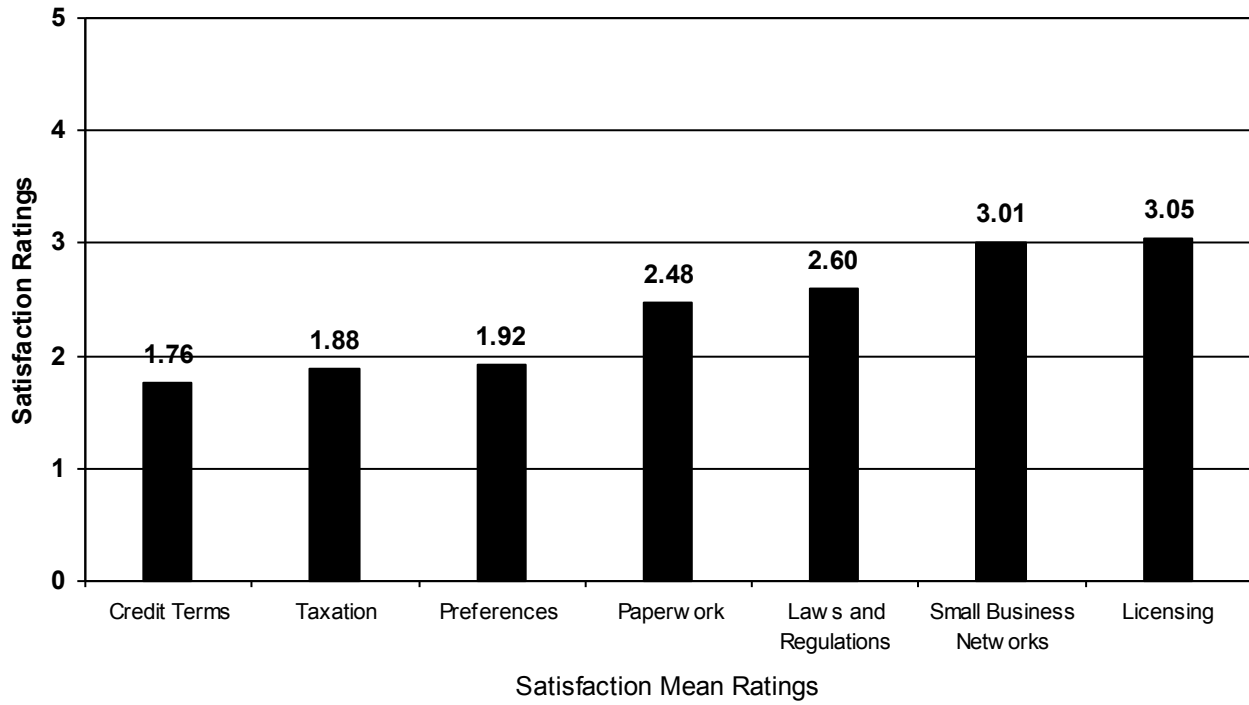
<b>Financial Assistance</b>	<b>Received</b>	<b>Desired</b>
Borrowing From Friends and Family	34%	-
Short-Term Credit (Bank Loan)	18%	10%
Venture Capital/Project Financing	16%	18%
Tax Allowance and Credits	6%	48%
Low Cost, Long-Term Loan	-	38%
<b>Non-Financial Assistance</b>		
Friends and Family	35%	-
Business Networks (Economic Development Agencies, Chamber of Commerce, Trade Representatives, Trade Fairs, Industry shows)	28%	44%
Small Business Management Training, Workshops, and Seminars	19%	40%
Technical Assistance, Management Information Systems	8%	30%
Incubator Centers/Industrial Parks	-	10%
<b>Entrepreneurial/Business Training</b>		
Management Training Programs	25%	52%
Marketing Studies and Sample Business Plans	15%	46%
Customer Data Analysis/Information System Development	8%	40%
Advertising Skill Workshops	5%	36%
Consulting and Case Studies	3%	24%

**Table 4**  
**Policies and Procedures for Entrepreneurial Activities in Hungary**

Small Business Conditions	(1)	(2)	(3)	(4)	Mean*
Licensing/Registration	-	20%	55%	25%	3.05
Requirements					
Small Business Networks	10%	17%	35%	38%	3.01
(Representation)					
Laws and Regulations	12%	16%	72%	-	2.60
Filing Requirement (Paperwork)	15%	22%	63%	-	2.48
Preferences for Small Business	38%	32%	30%	-	1.92
Taxation (Incentives and Exemptions)	42%	28%	30%	-	1.88
Credit Terms	46%	32%	22%	-	1.76

\*Rating Scale: 1-4, where 1=Must Be Improved, 2=Fair, 3=Average, and 4=Good

**Figure 2: Ratings of Satisfaction with Small Business Conditions in Hungary**



1=Must Be Improved, 2=Fair, 3=Average, 4=Good, 5=Very Good

**Table 5: Perceived Difficulties of Small Business Operations In Hungary**

<b>Perceived Difficulty</b>	<b>Percentage</b>
Unfavorable Credit Terms	78%
Lack of Preferences for Small Business	76%
Attitudes of Banks to Small Business	72%
Lack of Tax Allowance and Credits	69%
Lack of Venture Capital/Project Financing	62%
Access to Technology	58%
Cash Flow Problems	55%
Extensive Paperwork	37%

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