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Leading Radical Change in Transition Economies

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Leading Radical Change in Transition Economies

Abstract

New managers in central and east European companies were faced with daunting challenges to manage their companies through the transition from central planning to competition and to change their companies radically so that their firms would be capable of competing effectively. Based on the analysis of six longitudinal company cases from the Czech Republic, I identify the key skills that new managers had to have and where they were able to obtain those skills. The seeds of current managerial expertise could often be found in experiences under central planning, despite the fact that central planning more generally rewarded behaviors that were counterproductive in market-based competition. Results are discussed in the context of leading radical organizational change.

Leading Radical Change in Transition Economies

Firms in central Europe faced an unprecedented change in business conditions with the fall of Soviet-dominated communist governments. State-owned enterprises that had been embedded thoroughly in the social, political, and economic institutions of central planning were thrust suddenly into market-based competition. In a matter of two or three years, the apparatus of central planning was disassembled, prices were freed, borders were opened, currencies were revalued, and privatization of state-owned enterprises was begun. These were extraordinarily difficult circumstances for companies. Most firms were ill-prepared to compete because their strategies, structures, systems, and leadership capabilities were adapted to central planning, not market competition. Radical change was necessary and leading radical change was a critically important task for top managers in the region.

How change was led and with what success is the subject of this article. Using case data from six firms in the Czech Republic, I will identify skills and abilities that these managers needed for success and how they acquired these skills. I will argue that the seeds of success for managers often were found in their experiences under central planning, even though the system of central planning more generally encouraged many behaviors that were inappropriate for competition.

Conceptual Domain: Leading Radical Change

Top management plays a critical role in radical organizational change. Managers in central and eastern Europe had little discretion prior to the fall of communism and therefore played a smaller role in the success or failure of their firms than their western counterparts. Their latitude for action was much greater after the change in government, so the choices that managers made had the potential to affect company outcomes more significantly. As Greenwood & Hinings (1996: 1039-1040) note,

> Radical change cannot occur without the organization's having sufficient understanding of the new conceptual destination, its having the skills and competencies required to function in that new destination, and its having the ability to manage how to get to that destination.

Theories of organizational change suggest that new top management facilitates radical change,

especially if new top managers are from outside the firm (Romanelli & Tushman, 1994; Virany, Tushman, & Romanelli, 1992). Top managers generally are more exposed to and aware of changes in their business environment than rank and file employees (Thompson, 1967; Brunsson, 1995), and therefore may perceive the need for change more readily. New leaders may see opportunities and threats in the environment differently from old managers (Staw, Sandelands, & Dutton, 1981; Kiesler & Sproull, 1982) and bring new competencies and mind sets to bear (Ancona, 1990; O'Reilly & Flatt, 1989). New leaders may have less invested in the existing power structure, may be less committed to existing core values, and may be less constrained by the alliances and obligations inherent in the existing social structure of the firm. In essence, new leadership, especially from outside the firm, is less tightly linked to the status quo and may see the external world differently from internal managers, resulting in a greater propensity to initiate and oversee radical change.

Change in top level company leadership in central and eastern Europe was common if not universal after 1990, yet new leadership per se was unlikely to be a sufficient condition for the kind of radical change necessary in company operations. All new leaders, to one degree or another, had grown up under central planning and had developed their managerial skills under an economic system that was significantly different from the one in which they were newly operating. Where these new managers gained their experience, how they used it, and how they acquired new knowledge they needed are the focus of this research.

The Research

This analysis is based on case data from an investigation of organizational transformation in the emerging market economies of central and eastern Europe (Newman & Nollen, 1998). Case research methodology was used because the research questions were exploratory and events in the region unfolded over several years, often in unpredictable ways. Many forces bearing on the companies were at work and most of them could not be controlled.

I used a multiple longitudinal embedded case design (Yin, 1989) that allowed three levels of analysis over several years. The first unit of analysis is the firm. The second is top managers within the firm. The third is the actual changes made by managers. Both with- and between-case analysis were undertaken to first understand each case and then to analyze the similarities and differences among them (Eisenhardt, 1989).

Companies were included in the study based on three criteria. First, I required access to the top managers of the company – the chief executive officer and some of his senior colleagues. Second, after the pilot case (Zetor), cases were added based on their potential theoretical contribution to the analysis (Eisenhardt, 1989; Glaser & Strauss, 1967). Cases were added to test emerging conclusions, to incorporate different industries and privatization patterns, and to explore different types of change. Third, to control for some sources of variance that might otherwise confound the analysis, I studied only companies in the Czech Republic.

The Czech Republic is a good setting for this research because the pre-1989 institutional context was among the most pervasive and consistent of all communist regimes. About 97 percent of the economy was state-owned and the economy was biased by the Soviet Union's cold war defense needs. The Czech institutional context also changed more rapidly, radically, and consistently than others in the region after the fall of communism. The right-of-center government elected in 1992 remained in power until late 1997 and pursued rapid privatization in a domestic competitive climate that was relatively unfettered by regulations.

The data were collected between 1991 and 1997. Data sources included face-to-face interviews with top company officials, work observation, archival data, press reports, and interviews with investment analysts, bankers, partner company officials, and government officials. Financial data were collected from annual reports, investment analysts' reports, and documents provided by top managers. All firms in the study were manufacturing firms, all were state-owned before 1990, and all were formally privatized

between 1992 and 1993. Characteristics of the companies and the data sources from each are shown in Tables 1 and 2. The cases are summarized very briefly in Appendix A.

Tables I and II about here

Skills and Abilities Necessary for Top Leaders in Competitive Markets

Most firms in the Czech Republic had little or no capability for creating business strategies, making decisions, taking reasonable risks, or managing change. Existing capabilities developed under central planning were not appropriate for the new competitive environment in which firms found themselves. The dearth of appropriate skills and abilities resulted in strategic confusion and "adaptation by chance" in many firms (Hrebiniak and Joyce, 1985) as managers tried to enact concepts about which they had read but with which they had little or no actual experience.

Managers had to learn new role behaviors, develop new skills, and take on new tasks to lead their firms successfully in a competitive environment. Followers had to become or be replaced by leaders and bureaucrats had to become or be replaced by decision-makers. New tasks were required, including strategic planning, controlling costs, and producing according to market demand rather than centrally-planned directives. Top management therefore had to become more proactive, more flexible, and more risk-willing. It had to understand the firms' resources and capabilities and potential competitive advantage. Three important new abilities were necessary: strategic thinking; decisiveness and initiative; and attention to efficient operations (Table III).

Table III about here

Strategic Thinking

By strategic thinking, I mean three things. The first is the ability to *understand the firm's resources and capabilities* and how they are relevant in the marketplace. Many managers were not able to step back from their day-to-day production responsibilities to assess what the firm did well or could do well. The ability to assess accurately the company's resources and capabilities was clouded by forty years of producing to a plan. Poldi was a good example. When Vladimír Stehlík bought the company in 1993, he undertook direct selling to customers. He closed Poldi's joint venture with Ferromet, its foreign trading partner, and consolidated selling activities. Unfortunately, few Poldi employees had selling experience and few customers had experience working with Poldi directly. The firm had few capabilities in this area because Ferromet had responsibility for all of Poldi's foreign trade prior to 1990. Poldi did not have selling capabilities, and sales declined precipitously as a result.

Aero Vodochody's CEO, Adam Straňák had a better sense of his company's capabilities. When the Boeing partnership was announced, he said, "Surely Boeing will want to use our design engineers. They are the gold of our company. You can assemble an airplane anywhere, but you cannot design it anywhere." Earlier, when Aero Vodochody's top managers decided to manufacture a civilian aircraft, they designed a plane that was similar in size to their jets, applying their very specific design and manufacturing capabilities to another product.

Veba's Josef Novák, too, understood his firm's capabilities and resources. In his post-1990 decisions he created new products that were closely related to what the firm had produced for the previous 40 years. He expanded Veba's highest quality capability to terry cloth and added products based on existing or related technology. He did not try to use excess plant capacity for unrelated production activities.

Královopolská, by contrast, showed strategic confusion in the mid-1990s. Pánek and Jelínek, the General Manager and Chairman of the Board respectively, made at least two forays into unrelated

businesses. Both of these initiatives were motivated by a need for cash and a desire to use unused plant capacity. In neither case, however, did Královopolská have experience in the business or a closely-related capability to produce the products. Both initiatives failed.

The second aspect of strategic thinking that is important is the ability to *understand the market*, assess its characteristics, and adapt the firm appropriately. Many top managers as late as 1997 did not appreciate the importance of meeting customers' needs, producing reliable products, producing in a timely way, and servicing their products after sale. All of these concepts were new to Czech managers. Many did not have a market-oriented mind set and found it quite difficult to understand why their firms were having trouble in the new environment.

Josef Novák at Veba did have the skills to assess the market. Before 1990 he had traveled extensively in Europe and West Africa, visiting with customers. His outward focus served him well later on. He was able to determine that high labor costs in German and Austrian textile mills would drive them out of business, creating an opportunity for Veba. He also recognized an opportunity to manufacture king-size sheets, even though they are popular in only part of Europe. Veba's cost advantage gave the firm a foothold in the familiar European market which, in turn, gave Veba the market-based experience that enabled its entry into the North American market where king-size sheets were very popular.

Pánek and Jelínek at Královopolská were able to assess the familiar market better than they were able to assess the firm's resources and capabilities. As early as mid-1992, Pánek developed a strategic plan in which he decided to focus on high value-added business (this was his language), to focus more on engineering than manufacturing, and to devote resources to Královopolská's small turnkey business in water treatment plants. Pánek and Jelínek correctly anticipated the government's support of new water treatment facilities, and positioned the firm advantageously during the mid-1990s in this business. In addition, Královopolská's technical director, Vladimír Relich, conducted an industry-wide bench marking survey in 1993 and 1994 to determine which of the company's products were competitive globally, what

was needed to improve other products, and which products should be discontinued. Královopolská was well ahead of other Czech heavy manufacturing firms in its bench marking activities.

Evidence of Richard Kuba's (PBS) ability to assess the marketplace is shown in his strategic analysis, conducted in 1991 and 1992. In his words,

> I knew that we did not have the latest technology. We were at least ten years behind in gas turbine technology. We also did not have the market economy experience to implement our strategy for improving our international competitiveness. In 1991 and 1992, I visited several PBS customers in foreign countries such as Pakistan and Iran. They knew about Škoda Plzeň and Škodaexport [our foreign trading firm], but not about us. Škoda Plzeň had 10 businesses. If one of their businesses failed, they had nine others. We had one, and we had no name. ... There are four big international companies — General Electric, Siemens, ABB, and Mitsubishi — that control a big majority of the world market. There are tens of smaller companies like us, and some will not survive. I decided that it would be necessary to bring in a foreign investor, for both technology and market reasons.

Miroslav Poláček, the general manager of Zetor, was a manager whose background did not give him the capabilities to assess the market as well as others. In 1997, after three consecutive years of losses, Poláček said, "Why did our effort not get better results? The world market is tough. I am not happy with our results. What is my part of the blame? What did we do wrong? I don't know." Poláček was young (in his mid-40s), highly motivated, and an outsider to Zetor. However, his background as the director of production at one of Zetor's suppliers did not give him the market exposure or the whole product perspective that served Pánek and Kuba well after the Revolution. Poláček did not understand at the beginning of his tenure that customers would pay more for quality, reliability, timely deliveries, and after-sale service. He faced a very hostile, unfamiliar, confusing, competitive business environment.

The third aspect of strategic thinking that is important is the ability to *envision and plan for a new*

future, based on an accurate assessment of the market and the firm's resources and capabilities. Because planning for the future had not been part of managers' job before 1990, they were not accustomed to imagining possible futures for the firm, other than those that were a direct extrapolation from the past.

Many managers articulated a "strategy" during the early 1990s, but these strategies were not grounded in market reality. The Královopolská 1992 Annual Report, written by Pánek's predecessor, was indicative:

> Management intends to concentrate its efforts on the long-term development of the company, to increase productivity to a level that is five times its current status by 1997, to increase the value of the company by 30% every year, and to pay dividends to its shareholders starting in 1994.

The company lost money in 1993 and 1994 and experienced an operating loss in 1995. The words came easily but the goals were unrealistic. Královopolská, in 1992, did not have leadership that could articulate a positive, motivational, and realistic future.

Pánek was different. His future vision for Královopolská was as a high value-added turnkey provider of plants. The first step toward realization of this vision was aggressive growth of Královopolská's turnkey water treatment plant business. This business grew rapidly between 1992 and 1996, and was always profitable.

Novák, at Veba, was the best example of a visionary leader. In 1997 he had already developed three visions for the company:

1. *Product Extensions for Top Markets.* This was for the period from 1992 to 1997. The objectives were to add related products in familiar markets.
2. *Rationalization and Restructuring.* This plan was for the period from 1995 to 1999. It included rationalizing the production plant to improve logistics and reduce costs.

3. *Go East*. The "go east" strategy was for the period 1997-2005. Some textile production would be moved to East Europe and into the former Soviet Republics to follow expected lower-cost locations for production and to take advantage of expected growing markets for standard quality goods.

Novák was unusual in his capacity for strategic thinking. He understood the firm's capabilities and resources. He identified related products for expansion. He focused on the markets he knew well and carefully expanded into related but new markets (North America).

Most firms' top managers did not understand enough about the markets in which they operated to do the kind of analysis done by Novák and to take the steps he and his top managers took to pursue their vision. Managers who understood the ideas of business strategy and corporate strategy and who could think strategically were more likely to be successful leaders during the transition years. The fact that these skills were in short supply because of two generations of central planning made them all the more important. Managers who understood the implications of the economic and political changes were more likely to set a viable strategic course for their firms (Table IV). Managers who underestimated the magnitude of change that competition would require and managers who defined solutions according to the pre-1990 production quota logic were not as likely to lead their firms effectively through the transition.

Decisiveness and Initiative

Leaders must be available, mobilized, decisive, and willing to take the reasonable risks. In the Czech Republic there was a clear difference between managers who were and were not willing to make decisions and take initiative. Top managers at Zetor and Aero Vodochody were virtually paralyzed in 1995 and 1996, waiting for and negotiating with potential new partners. Poláček said at Zetor, "We were not able to made decisions partly because of our situation with Deere and our ownership by Konsolidační Banka," when talking about Zetor's performance. While both of these firms were legitimately hamstrung by their unsettled ownership, neither showed the kind of proactivity observed at Královopolská and Veba.

Pánek at Královopolská and Novák at Veba made bold decisions as early as 1992, Pánek to pursue turnkey projects and Novák to borrow extensively for product expansion. In retrospect these were obvious decisions, but at the time they were risky and the managers who made them were taking far more initiative than had been permitted prior to 1990. There is some evidence that managers who perceive they have greater discretion do, in fact, initiate more change (Huber, Stucliffe, Miller, & Glick, 1993). Novák and Pánek, perhaps because of their relative youth (both in their late 30s in 1992) or because of their experience with competitive markets on the one hand and turnkey products on the other, believed they had the discretion to make change and did so, even though neither company's future ownership was settled at the time.

After 40 years of central planning and a command and control style of management it was not surprising that many managers did not perceive that they had a great deal of discretion, even if they did. For 40 years survival skills had included working only within one's narrow job description, asking for permission and approval for the slightest deviation from standard practice, implementing plans derived by others, and pushing decisions up the hierarchy. Yet initiative can be learned in the former Soviet Bloc countries if rewarded and if supported with protection from too much downside risk (Frese, Kring, Soose, & Zempel, 1996). Josef Novák took initiative himself and encouraged it among his management team, perhaps because he had considerable discretion during the central planning era. He said, "If you treat people as responsible managers they will start to behave that way." He built a top management team of six very different personalities. His strategic thinking resulted in securing short-term, risky financing in 1993 but led to long-term bank financing, stable ownership, and profitability.

Table IV about here

Attention to Efficient Operations

Finally, Czech managers had to learn to manage costs effectively while also finding new sources of revenue (Allmendinger & Hackman, 1996). Firms in central Europe were in desperate shape. Their costs were too high, their equipment was out of date, they employed many more people than necessary to do the job, and their traditional markets had evaporated. Without attention to immediate matters of productivity there would be no future.

The first step in cost control was to determine costs Under central planning, costs and prices were set by the State, not the market. Accounting systems produced information that was not useful to managers for decision making because managers had not been the decision makers. Therefore virtually every Czech firm needed new accounting, order tracking, inventory, and human resource systems.

Veba was one of the first Czech firms to use activity-based costing. Building on advice from a consultant, Veba managers installed a management information system in 1993 that allowed them to calculate variable costs separately from fixed costs, thus improving their ability to set prices and know their profitability. In 1997, managers from Zetor, PBS, Královopolská, and Aero Vodochody all voiced dissatisfaction with their old information systems and the very slow speed with which new systems were being developed.

Vladimír Relich, the Technical Director at Královopolská, voiced concerns about his information system.

> Our delivery time is a problem because we don't have a good information system. What used to take us one year now takes four months, but we should get to two-and-a-half months to be competitive. It is hard to reduce the time without better controls. We need an information system to connect product design and product sales and delivery. We are developing a system ourselves, step by step, but we lose business sometimes because of slow delivery time.

Many Czech managers assumed their firms had a cost advantage, compared to western competitors, because of the low wages paid to Czech employees. However, when time-to-produce for the same product was taken into consideration, many managers discovered that their labor cost advantage disappeared.

Time-to-produce was longer in the Czech Republic than in western Europe for at least three reasons. First, equipment was older and in poor repair in the Czech Republic. Without the latest technology, Czech firms were at a disadvantage. This problem was fairly easily solved with money. PBS solved it through its joint venture with ABB and Veba solved it with debt financing.

The second reason for longer time-to-produce was plant logistics. Many plants in the Czech Republic had grown haphazardly during the central planning era, with scant attention paid to layout and efficiency. This problem, too, was solved with money and some know-how. One of ABB's first initiatives at PBS was physical plant rationalization. Veba undertook similar activities as part of Novák's second vision. Zetor began plant rationalization during 1996 and was able to sell part of the physical plant to another firm. Královopolská undertook similar activities in 1994.

The last reason for longer time-to-produce was employee motivation, a much more intractable problem and a significant challenge for top managers. Before the change in governments employees were not expected to work a full eight-hour day. There was not enough work to do. These habits, ingrained after 40 years, were hard to change. Solving this problem did not require money as much as time, will, and persistent leadership. Top managers had to recognize the problem, devise incentives that would encourage employees to change, create systems and processes that supported the change, and above all, be steadfast and consistent in their pursuit of new employee behaviors. Most managers recognized the problem but had not solved it by 1997. Kuba at PBS said,

> It is easy to change the structure of the company, and it is easy to change the facilities, but it is not easy to change people's minds. ... Employees don't yet understand the consequences of their actions. They don't take responsibility.

His ABB country manager agreed:

> The first level of change in Czech companies comes easily. To make nice new offices and new factory layouts is quite simple. But the transfer of real human resource learning is slow.

> ... Responsibility and initiative are poor because it was not rewarded for two generations...
> The tasks themselves were compartmentalized — I did mine and you did yours. I did my duty so I'm okay.

Jelínek at Královopolská had put many hours into training to try to change employee behavior. He, too, was frustrated:

> We are trying to change the corporate culture, and have been trying hard for three years. The easy thing is to write it down. The hard thing is to persuade the people so that they are convinced about the company.... People don't like to take responsibility for their own decisions. They expect other signatures on decisions. We are trying to find people who are not afraid of big decisions.

Perhaps the greatest source of high costs was from over-employment. Czech firms employed up to twice the number of employees actually needed, owing to pre-1990 full employment policies. For each of the five going concerns, employment in 1996 was about 60 percent of pre-1990 employment. Real revenue had fallen more than employment at Aero Vodochody, Veba, and Zetor. Only at PBS and Královopolská had employment declined relative to revenue. These data suggest that much restructuring was ahead for Czech firms. Managers had not made the employment cuts that would be necessary to get labor costs under control.

Strategic thinking, decisiveness, and attention to costs were three important managerial skills that were not nurtured during the central planning era, yet that were important for any enterprise whether in central Europe, Asia, or North America. These skills were in short supply after the fall of communism.

Proposition 1: *Managers in transition economies who show evidence of more strategic thinking, decisiveness, and efficiency awareness will be more likely to undertake radical organizational change than others.*

Learning Leadership Skills for Competition

Virtually all firms changed leadership after 1990, if for no other reason than the political necessity of removing Party functionaries from their positions. Several firms also took the opportunity to place new types of managers in top jobs, not just young people, but also people with backgrounds that would not normally have garnered a top position. The quality and success of these new corporate leaders in the Czech Republic varied considerably from firm to firm. I suggest two types of explanations for the relative success of some managers, summarized in Table V. The first derives from their pre-1990 experience, including turnkey business experience, direct customer contact, and experience operating in competitive markets. The second derives from their post-1990 experience and includes access to relevant role models, partnership with a strategic investor from the West, and learning from the rigors of unprotected competition.

Past Experience

Managers tend to define problems and respond to them in terms of their own experience. Those with a background in production are likely to define problems and solutions in terms of production. Those with a marketing background are likely to define problems and solutions in terms of the market (Gupta & Govindarajan 1984; Hambrick & Mason, 1984). The pre-1990 experiences most relevant for top managers were contact with customers, contact with a competitive market environment, and turnkey experience.

Managers who had worked in a *turnkey business* prior to 1989, however small, developed knowledge about the relationships and dependencies among customer specifications, product design, manufacturing, installation, and service that other managers did not have. Experience in a turnkey business gave managers a measure of independence, autonomy, and responsibility not shared by others. Managers with turnkey experience were more decisive after 1990 than others and were more willing to accept responsibility and take risks.

In firms such as Královopolská, appointing a manager from the turnkey division was like appointing a new leader from outside the firm. Pánek was from the Královopolská's turnkey water treatment plant business. His background was economics rather than the usual engineering and he had been a sales engineer who worked directly with customers in the field rather than a production manager who worked in the factory. Pánek brought to top management a clear and unequivocal emphasis on quality and customers' needs. Unhampered by the old assumptions and values in the production divisions, Pánek acted like an outsider with a mission.

Kuba, too, had turnkey business experience. It was his responsibility before 1990 to "commission" new power plants. He was the person on-site who flipped on the switch and was responsible for fixing problems once the plant was operational. He had responsibility for quality, performance, and customer satisfaction in the field. He had discretion about how to meet customers' needs at the installed site. He understood clearly the relationships and dependencies among the parts of a plant. He saw first hand the problems created by low quality.

Kuba and Pánek had been as close to mid-level general managers as were found immediately after 1990. Their pre-1990 business experience, though not considered crucial before then, became one of the factors that helped them be successful after 1990.

Direct customer contact, whether as part of a turnkey business or not, was a second pre-1990 experience that facilitated leadership later. Both Pánek and Kuba had direct customer contact. Novák, at Veba, also had direct customer contact because he traveled extensively to Africa and Western Europe before 1990 to visit his customers.

Employees with experience in a foreign trading firm often had the market and customer know-how needed after 1990. Aleš Zouhar, the director of marketing at Zetor, was a case in point. He went to Zetor from the U.K. branch of Motokov, Zetor's foreign trading partner. Zouhar had spent six years in the U.K. before returning to the Czech Republic. His understanding of customers, competitors, and markets was

extremely valuable to Zetor. Zouhar established Zetor's first-ever world-wide parts and service business unit. He created a separate wholly-owned subsidiary, Zetor-ČR, in 1997 to oversee Zetor's network of 34 domestic dealers and to provide a complete package of services, including customer financing, so that customers could borrow from Zetor rather than a bank for a new tractor. He brought a customer focus to Zetor that was new and much-needed.

Finally, *experience in competitive markets* was relevant for company leadership. Through contact with businesses and customers in competitive economies, managers in central Europe knew from experience how different market competition was from a planned economy. They had observed alternative organizational forms and ways of doing business (Palmer, Jennings, & Zhou, 1993). Firms that operated in competitive environments before the transition had some knowledge of costs, markets, and customers. Novák's experience was an example, owing to his contact with customers and his presence in Western Europe. Novák infused Veba with his knowledge of customer needs and the importance of highest quality to attract and keep customers. Zouhar at Zetor was another example. His experience in a competitive market brought a valuable perspective to Zetor, reflected in Zetor's strategic decisions within a year after his arrival.

These data suggest that seeds of future success after extraordinary institutional upheaval may be found within current employees' past experiences. Those who had direct contact with customers or experience in competitive markets, and there were some, were more likely to have the skills and knowledge necessary for future competition.

Proposition 2: *Managers in transition economies with previous experience in a turnkey business, direct customer contact, or experience in a competitive economy will show more evidence of strategic thinking, decisiveness, and efficiency awareness than others.*

New Experience

A number of capabilities necessary for success in competitive environments were not found in the companies' pasts; in their competitive environments during transition; or in the managers themselves. These capabilities, however, were learned after 1990 from role models (usually consultants), from strategic partners, or from the rigors of market competition. Managers who were able and willing to learn from others, who were lucky enough to find consultants or business partners with relevant, region-sensitive knowledge, or who faced unfettered competition and adapted quickly were more likely to develop the capabilities needed for long-term success in the new competitive environment (Table V).

Again, Novák at Veba provided a good but rare example of the value of *role models*. He benefitted from a very fruitful relationship with a Dutch consulting team. This husband and wife pair worked side-by-side with Novák and his managers on matters large and small, ranging from strategic planning to MIS to activity-based costing. The relationship worked well, according to Novák, because the consultants had experience in Czechoslovakia prior to 1990 and because Novák was willing to learn from them. Novák described the relationship with the consultants:

> We did not have a sophisticated program [with the consultants]. Their approach was to raise questions. Others looked for a report, an analysis, an easy fix. Not us. They were reasonable in their approach. They had experience with the Czech mentality... they were patient enough and relatively inexpensive. Their biggest value was the new ways of thinking they showed us.

Probably the most important aspect of the relationship between Veba and the consultants was mutual respect. The consultants had Czech experience. They understood Czech history and culture. They did not suggest solutions to problems that were not feasible. Instead, they worked with Novák to derive practical solutions to pressing problems in a way that took into account the business realities of the day. As a result, the consultants earned the trust and respect of Veba management which, in turn, made it easier for Novák and his top managers to learn from the consultants.

Importantly, trust and respect were reciprocated. The consultants developed considerable respect for Novák and Veba between 1992 and 1997. The consulting relationship became a partnership in 1997, as the Dutch consultants became Veba's agents in the Netherlands and Belgium. Veba's status as an official supplier to Holiday Inns in Europe was one concrete result of the consultants' business activity on Veba's behalf.

Kuba at PBS benefitted from a *strategic business partnership* with one of the world's most respected companies, ABB. Apart from technology transfer, he and his managers learned management know-how from ABB. He said,

> The best thing about ABB is being able to learn new management techniques from ABB sister companies. We can benchmark ourselves, identify our weaknesses, and improve... The most learning comes from bi-monthly business-area meetings. We do presentations and they ask really tough questions. THIS is management know-how transfer.

Richard Kuba also discussed the tough learning that resulted from the *rigors of competition.* Kuba and his colleagues were accustomed to working together with other companies on big projects; before 1990, PBS worked with other companies in the Škoda group. But ABB was different. Cooperation coexisted with competition, and that was outside Kuba's experience. Sibling rivalry among the ABB sister companies was very much a fact of business life, he discovered. Kuba related an unhappy episode about his company's unfamiliarity with these business relationships. He said:

> We weren't naive, but we were inexperienced. Unexpected things happened. I expected market economies to be more fair than they are. Swedes, Germans, Americans all act differently. It's tougher than I thought it would be, and it's tough to explain to employees. We have to fight more in order to succeed in this environment.

Again, the learning process was slow and painful, but necessary in order for PBS to achieve its competitive potential. ABB was a tough parent. It did not protect subsidiaries from the discipline of the

marketplace. ABB held each subsidiary to a profitability standard and was willing to sell subsidiaries that were not profitable.

Companies such as Aero Vodochody and Zetor were in a different situation. Their situation precluded some of the tough market-based lessons from being learned. Aero Vodochody was in a "wait and see" position before the Boeing partnership was arranged. Protected from bankruptcy by the government, Aero Vodochody managers did not get a chance to try their skills in the marketplace. After a few post-1990 sales, Aero was not able to sell its aircraft because its situation in the Czech Republic was unclear. No country wanted to buy aircraft from a firm that was not likely to be in business in a few years or from which its own government was not willing to buy aircraft. The result, though largely out of Aero Vodochody managers' control, was that little if any learning about market competition was available to them before 1997. Zetor, too, was bailed out twice by government recapitalizations and loans from government-owned banks. As late as 1997, the firm had not downsized relative to its revenue, it had not rationalized its operations, and losses continued. Both firms were protected from the rigors of the marketplace and both were slow to change as a result.

Though the leadership talent pool was thin, there were experiences from before and after 1990 that contributed to rapid learning on the part of new managers in the Czech Republic. Pre-1990 experience and post-1990 learning opportunities distinguished those leaders who were able to take their firms forward into radical change from those who were not.

Proposition 3: *Managers in transition economies with access to relevant role models, constructive relationships with business partners, and who competed in an unprotected market environment will show more evidence of strategic thinking, decisiveness, and efficiency awareness than others.*

Table V about here

Discussion and Conclusions

These data suggest that three leadership qualities were necessary for these new managers; strategic thinking, willingness to make decisions and take initiative, and ability to manage costs. These are no different from top leadership qualities one might look for in the West, except that these qualities were in short supply in the Czech Republic because of the structure of central planning. Nevertheless, these qualities could be found, at least in their nascent form. Three pre-1990 experiences seemed to produce top leadership skills: turnkey business experience, direct customer contact, and experience in competitive markets. Three post-1990 circumstances, similarly, accelerated the rate at which new top managers learned requisite skills and abilities: relevant role models, constructive business partners, and the rigors of the marketplace. These results are summarized in Figure 1.

Veba was clearly the most advantaged firm of the six. Novák had experience with customers and competition prior to 1990 which helped him understand both the marketplace and the sources of his firm's competitive advantage within the marketplace. He was accustomed to taking initiative because of his extensive travels but also, perhaps, because Veba was located in a remote town out of the gaze of central planners (then) or government officials (now). Finally, Veba benefitted from the Dutch consultants in ways large and small. Many Czech companies had very different experiences with their western-oriented consultants.

PBS also had undertaken considerable change, largely because of Kuba's insistence on finding a foreign strategic partner. ABB contributed capital, management know-how, and tough market experience, all of which helped PBS become competitive.

Zetor was the least well-off of the going concerns (Poldi was in bankruptcy in 1997). Zetor's

management had little experience before or after 1990 from which it could learn strategic thinking, decisiveness, or attention to efficiency. Zouhar was the one exception but he was not hired until 1996, too late to have a strong effect on Zetor's outcomes.

Figure 1 about here

Skills and abilities of top managers derive, in part, from their training and their experience. It was no surprise that many managers were ill-prepared to lead their companies effectively in a market-based system. Because inter-firm and geographic mobility were so low, firms could not realistically draw on new talent from outside. Firms had to find insiders who might act like outsiders. Kuba and Pánek were the clearest examples. Their experience was in areas that had not been on the main career tracks to the top of the firms before 1990. The problems associated with promoting from the traditional production function were best illustrated by Poláček. Though young (low 40s) and motivated, he could not turn Zetor around. He could not rationalize production, cut-back employment, or reduce costs sufficiently. He continued to think in terms of units produced, not profit or quality.

This study provides insights into sources of leadership under conditions of radical institutional change and sources of leadership expertise in less turbulent conditions. Companies facing changes in their competitive markets might look for new top management talent in unusual places, but places in which knowledge has been gained that is relevant for the new business conditions.

I do not suggest that these are universal predictors of managerial success. Rather, because of the effects of central planning, these predictors of managerial skill will be important and powerful in the generation after the change in governments. Once the effects of central planning have dissipated, there should be much more variability in the paths by which successful managers became so.

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TABLE I:
Longitudinal Company Cases

Company	Managing Director in 1996	Products	Data Collection Interviews at the Company	Other Data Sources
Aero Vodochody	Adam Straňák	Jet trainers and light attack jets. L-159 is new product.	5/94, 6/94, 7/95, 7/96, 4/97, 11/97	Company documents, analysts' reports, media reports
Královopolská	Zdeněk Pánek	Tanks and pipes for chemical & water treatment plants, turnkey water treatment plants, and steel structures and cranes	3/93, 12/93, 6/94, 12/94, 7/95, 7/96, 4/97	Company documents, MBA Enterprise Corps report , consultant's report, analyst's report
PBS (Including joint venture partner and owner as of 2/97 ABB)	Richard Kuba	Boilers and turbines for power generating plants. Turnkey power plants.	7/95, 7/96, 4/97, 11/97	Company documents, press releases, ABB personnel
Poldi	Vladimír Stehlík	Rolled construction steel Stainless steel	3/93, 12/93, 6/94, 12/94, 7/95, 7/96, 4/97	Company documents, press reports, Kaiser Engineering report
Veba (including Centrotex, owner as of 4/96)	Josef Novák	Textiles -- damask and terry cloth	7/95, 7/96, 4/97, 11/97	Company documents, Centrotex personnel CMC # 93-008 and 94-022 by J. Matesová
Zetor (including John Deere, commercial partner)	Miroslav Poláček	Tractors, bearings until 7/93	5/92, 3/93, 6/93, 12/93, 6/94, 12/94, 7/97, 7/96, 4/97, 11/97	Company documents, media reports, John Deere employees, former employees, banks

TABLE II:
Company Characteristics

Company	Revenue [a] 1990/1996 (CZK million)	Profits before Taxes 1990/1996	Employment 1990/1996	Exports (% of revenue) 1989/1995	Dependence on Soviet Bloc[b] (% of 1989 revenue)	Average Receivables 1992-1994 % of revenue/ ratio to payables
Aero Vodochody	1,750 1,340	125 (2,688)	3,600 2,300	95 100	> 90	33 1.1
Královopolská	1,745 3,000	120 49	5,500 2,800	75 na	50	31 0.8
PBS	2,050 10,960	224 (820)	9,600 3,200	24 28	20	38 [d] 2.0 [d]
Poldi	3,000 < 100	n.a. >(1,000)	20,000 4,300	32 n.a.	85	67 0.7
Veba	650 1,100	111 9	3,200 1,800	46 71	<10	16 1.4
Zetor	4,000[c] 4,570	424 (1,600)	10,000 5,500	75 92	50	66 [d] 1.4 [d]

[a] The official exchange rate in 1990 was approximately 19 CZK per U.S. dollar (and about 29 CZK per dollar on the black market). The exchange rate in 1996 was approximately 30 CZK per U.S. dollar.

[b] COMECON + domestic defense sales + sales to Iraq

[c] Author's estimate

[d] Excludes 1993

TABLE III
Old and New Managerial Capabilities

Central Planning	Market-Based Competition
Use existing resources for existing production program	Understand firm's resources and capabilities for sources of competitive advantage
Produce to a quota	Understand the market for new product development and growth
Implement a plan	Envision and plan for the future
Work within a job description and get permission for deviations	Be decisive and take initiative
Obtain the biggest budget possible and employ as many people as possible	Create cost-efficient operations

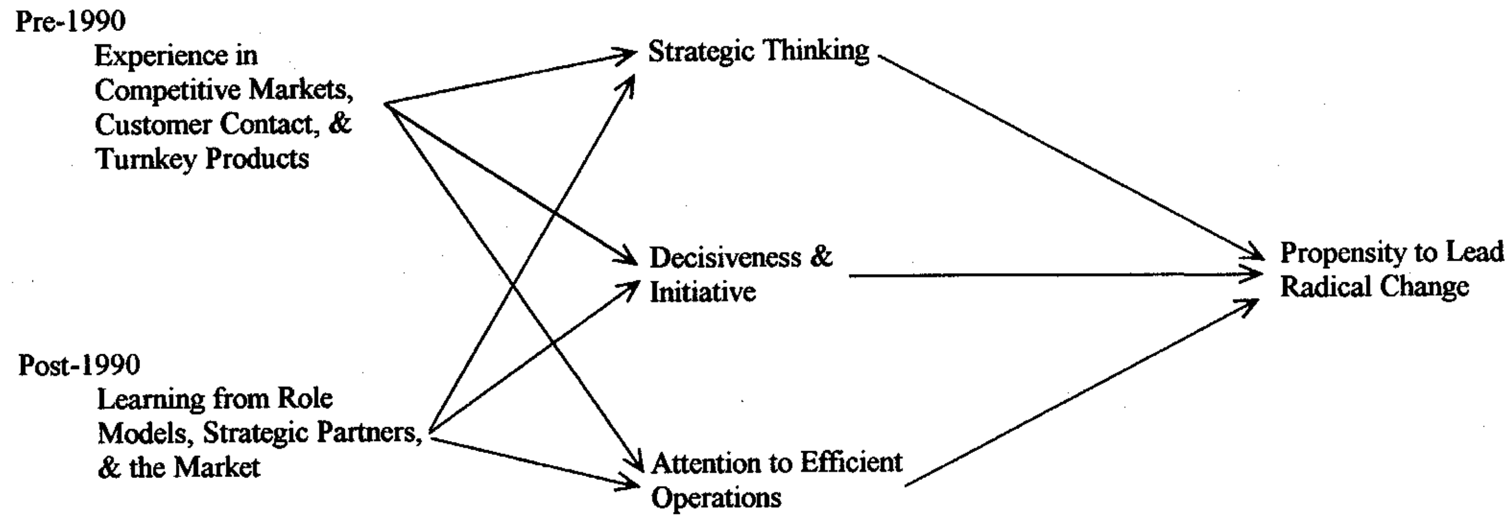
TABLE IV:
Leadership Skills by Company

Company	Leadership Skills		
	Strategic Thinking	**Decisiveness and Initiative**	**Efficiency Awareness**
Aero Vodochody	Yes: "Engineers are gold" No: Market for civilian aircraft	No. Waiting for new owner	Not yet
Královopolská	Yes: Turnkey business, extent to chemical plants. No: Confusion -- buses and brakes	Yes	Yes, but not supported with systems
PBS	Yes: Kuba's strategic assessment	ABB required it	Growing
Poldi	No	na	na
Veba	Yes: Novák's three visions, 1992 competitive assessment	Very strong	Strong
Zetor	No: Few quality and service fixes	Waiting for new owner	Not yet

TABLE V
Sources of Learning about New Managerial Skills and Abilities

Company	Sources of Learning from Before the Revolution			Sources of Learning After the Revolution		
	Customer Contact	Competition	Turnkey Business	Role Models	Strategic Partners	The Market
Aero Vodochody	No	No	Aircraft	No	Yes, Boeing	Not yet
Královopolská	Yes	No	Water treatment plants	No	No	Yes
PBS	Yes	No	Power plants	No	Yes, ABB	Yes, ABB
Poldi	No	No	No	No	No	No
Veba	Yes	Yes	No	Yes, Dutch consultants	No	Yes
Zetor	No	Yes, but through Motokov	No	Deere advisors to small degree	Four-year Deere commercial agreement	Not yet

FIGURE 1:
Leading Radical Organizational Change in Transition Economies



Appendix A:

Brief Summary of the Companies

(See Newman & Nollen, 1998 for full-length cases)

Aero Vodochody

Aero Vodochody (Ī′-rō Vō′-dō-hō-dē) was the monopoly manufacturer of military jet trainers and light attack aircraft for the Soviet Union and its allies. It was the largest manufacturer of jet trainers in the world. The company was founded in 1919 as an airplane and automobile maker. Aero Vodochody had revenue of CZK 1,750 million (about USD 50 million at the early 1998 exchange rate) and employed 3,600 people in 1990. Over 90 percent of Aero Vodochody's revenue was obtained from its exports of these airplanes to the Soviet bloc before 1990. None of its new orders came from former Soviet bloc countries between 1991 and 1996.

Aero Vodochody's main post-1989 product was the L-159 trainer with a U.S.-built engine and avionics integration from Rockwell. The NATO-compatible L-159 was to be Aero's main product for the next 20 years. Its claimed advantage in the market would be equal performance at lower life cycle cost. To survive, Aero had to sell this plane first to the Czech government and then to other countries in the region and in the developing world. Aero also developed a small civilian turboprop aircraft with a fuselage similar to the L-159 and began subcontracting assembly work for Boeing and Northrop.

Aero Vodochody's financial health began to deteriorate in the mid-1990s. All of Aero's Soviet business was lost after 1990. New orders were scarce and some new customers did not pay. Aero had always "sold" aircraft through a foreign trading company as the result of government-to-government negotiations. After 1989, the expertise that resided in the government and the foreign trading company were no longer available to Aero for sales. Without those capabilities, Aero employees found it difficult to sell aircraft to good customers.

Profits turned to large losses, up to CZK 2,700 million in 1996, twice Aero's revenue that year.

Bank debt exceeded CZK 5,000 million in 1996. By mid-1996, Aero Vodochody was technically bankrupt. The first post-Revolution managing director had resigned under fire and been replaced by Adam Straňák, a 40-year old life-long Aero Vodochody employee whose background was design engineering. He had some American business education in 1993, had traveled to the U.S. to visit Rockwell several times after 1989, and spoke English fluently. He was a pragmatic problem-solver with good relationships with key government officials.

Straňák and the Czech government put a final privatization plan into operation in 1996. The government restructured the company financially, writing off some of its debt owed to commercial banks, (which were still government-owned) and swapping the rest of it for more equity held by one of the banks. The value of this bailout was CZK 2,900 million. In May 1997 a Boeing-ČSA[1] joint venture agreed to buy 34 percent of Aero and to invest nearly CZK 1,000 million in the firm. The Czech consulting firm engaged by Aero for advice during the negotiations was described by one Aero manager as confirming the adage that, "consultants are people who borrow your watch to tell you what time it is."

A contract with the Czech government for 72 airplanes, first suggested in 1995, was signed shortly thereafter. Even so, the government order represented less than half the volume needed for break-even on the L-159. After almost a year of tough negotiations, Boeing made its investment and assumed management control of Aero Vodochody. The firm was finally ready to begin strategic change in 1998.

Královopolská

Královopolská (Krah′-lō-vō-pōl-skah′) was a 100-year old manufacturer of industrial equipment located in Brno, the second largest city in the Czech Republic (Newman & Nollen, 1996). It made tanks and pipes and other metal parts for chemical plants, water treatment plants, and nuclear power plants, as

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[1] ČSA is the Czech national airline. Boeing had purchased Rockwell's avionics business earlier - - the company that integrated avionics for Aero's L-159. Boeing also purchased McDonnell Douglas which made jet fighters that were competing for new business in the region among new NATO members. Aero reported to McDonnell Douglas in St. Louis on a day-to-day basis after the strategic alliance was negotiated.

well as cranes, bridges, and other steel structures. It also had a small turnkey water treatment plant business. The company had revenue of CZK 1,745 million in 1990 (about USD 50 million at the early 1998 exchange rate) and employed 5,500 people. Three-quarters of the company's revenue came from exports before 1990, mostly to Soviet bloc countries where there were few if any competitors. In the domestic market, Královopolská was a monopoly supplier.

Královopolská lost most of its export business after 1989. Domestic sales to the chemical and nuclear power industries also fell as those industries weakened, but Královopolská's water treatment plant equipment and turnkey businesses grew rapidly because of the new government's support for environmental clean-up.

Královopolská's management reorganized the company from a functional structure to product divisions in 1992 and announced a new customer- and quality-oriented business strategy. Several subsequent reorganizations resulted in consolidated divisions and separation of the production function from the product divisions. New top managers were appointed in 1992. The general director was Zdeněk Pánek, who was 37 years old, educated in economics, and who came out of the turnkey business where he had been a field representative. He undertook a competitiveness analysis of Královopolská in 1993; created subsidiaries to conduct trade with Russia and other eastern European countries; created a strategy department; achieved ISO 9000 certification in 1994; created a chemical engineering department to try to enter the crowded turnkey chemical plant business; and initiated forays into new, unrelated businesses. Pánek encouraged his employees to learn English though he was not an English-speaker himself. He had little experience with the West and little trust of consultants after an incident in 1993 in which Královopolská engaged a German consulting firm (and paid it DM 38,000) for an analysis that turned out to be little more than pages duplicated from books that could be found in the library.

Královopolská was nominally privatized in May 1992. In March 1995 a partnership among seven company managers called KENAP agreed to buy a 51 percent stake in Královopolská from the National

Property Fund (the government entity created to hold unsold shares in companies, pending final privatization). KENAP, led by Pánek, was granted management control of the company immediately, agreeing to purchase the shares over several years.

Between 1992 and 1996 Královopolská posted better financial results than many other Czech companies. Although revenue decreased in 1990 and 1991, it increased after that. Pánek wanted to make Královopolská into a full-service engineering company for chemical as well as water treatment plants, not just a tanks and pipes supplier. He wanted turnkey business to account for 70 percent of revenue by 1997, and by 1995 it had already passed 50 percent of revenue and accounted for all of Královopolská's profit. Yet the future of the company was not secure. The big water treatment plant business that benefitted Královopolská declined after 1996. New turnkey chemical plant business was being developed in the Middle East and Kazakstan, but these were unstable regions and new businesses for Královopolská. No turnkey chemical plant orders had been received through 1997. KENAP's debt burden for purchase of the company placed a premium on cash flow. There was no cash available for new investment in new technologies, plant and equipment, or information systems.

In the fall of 1997 Pánek was briefly jailed while under investigation for "tunneling," a practice whereby assets from one firm (Královopolská) were moved to other firms (allegedly other KENAP-controlled entities or firms controlled by Pánek's family or friends) to the detriment of other shareholders of Královopolská. Tunneling was endemic in the Czech Republic in 1996 and 1997, yet despite numerous high-profile arrests, no one had been convicted of any tunneling crimes and the practice continued. KENAP missed a payment to the National Property Fund for Královopolská shares in late 1997 and the Fund repossessed Královopolská. By 1998 Pánek was no longer managing the company and its fate was uncertain.

PBS

První Brněnská Strojírna (Prv′-nee Br-nyěn′-ska Stroy-ïr′-na), or PBS, was a Brno-based

manufacturer of boilers and turbines for power plants (Nollen, Newman & Abbey, 1998). The company also built complete power and heating plants on a turnkey basis, serviced old plants, and made a variety of other small industrial components. PBS employed more than 9,600 people and had revenue of CZK 2,050 million in 1990 (about USD 59 million at the early 1998 exchange rate).

Boilers and turbines made by PBS were well-engineered and long-lasting. With 140 years of history, PBS was regarded as a "family silver" company in the Czech Republic. Its turnkey power plant business was a significant part of the company. Exports accounted for a quarter of PBS sales as of 1990, and 80 percent of all exports were made to Soviet bloc countries.

PBS was nominally privatized in 1992. The general manager, Richard Kuba, believed that the company's final privatization would require a relationship with a foreign company. He thought it would take PBS too long to catch up technologically, and that new investment was needed from the West because capital was not available in the Czech Republic. In an over-capacity industry dominated by four or five giant producers, PBS had unsatisfactory prospects without a strategic partner.

In 1992, the International Finance Corporation (IFC), acting as consultants to PBS, helped arrange a joint venture with ABB that began business in April 1993, called ABB PBS. The IFC was selected by Kuba because of its experience with similar companies in the Czech Republic. According to Kuba, the consultants were critically important during the board meetings in which the joint venture was decided. ABB held a 67 percent stake in the joint venture; about 80 percent of PBS's revenue and just over half its employees went into the joint venture. Kuba was its managing director.

Business was good in its first two years. Orders and revenues increased and the joint venture was profitable in 1994 and 1995. ABB PBS completed the bulk of its physical capital restructuring in 1995, including factory renovation, improvements in engineering facilities, and award of ISO 9000 certificates. Labor productivity increased markedly and a new information system was ordered.

However, a variety of problems became evident in 1996. The domestic service business, which had

been created as a separate profit center, was disappointing as new small competitors entered the market. The coal-fired steam boiler business in which ABB PBS had technological capabilities was becoming strictly a rehabilitation business; there were no new orders.

Relationships with ABB sister companies also were difficult. One project in Germany went badly for the joint venture and the new management information system took a year longer than planned to come on line. Managers admitted that they "lost control of the company" for almost a year while the new information system was installed. Human capital restructuring was difficult as well. To get employees to take responsibility, show initiative, and confront adversity were all challenges. ABB tried to help, but believed that local Czech managers and not expatriates would have to bring about the mentality changes. One critical problem was referred to as "good news management" by ABB personnel and "telling a good story" by Czechs. Czech managers were accustomed to telling the boss what they though the boss wanted to hear. A holdover from central planning, good news management was a survival skill then, but dysfunctional in the ABB partnership. The extent of problems with the German boiler project and the new information system were not communicated to ABB until considerable damage had been done. As a consequence, the joint venture lost money in 1996 and 1997. Though ABB bought-out the joint venture in early 1997, Kuba was no longer involved in day-to-day operations. The new subsidiary of ABB, now called ENS (Energetické Systémy) no longer did business in western Europe. Instead, its geographic domain was its traditional one - - central and eastern Europe.

Poldi Steel

Poldi Steel Works at Kladno, just west of Prague, celebrated its centennial in 1989, the same year as the Velvet Revolution. Poldi produced CZK 3,000 million worth of steel that year and employed 20,000 people. Poldi produced carbon and alloy structural steel and stainless steel bars of varying sizes for use in a wide range of industries. Poldi had been a leader in steel-making technology in the 1920s and 1930s. There were three other large steel producers in the Czech Republic, all located in the Ostrava region

hundreds of kilometers distant from Kladno. The industry was over-capacity in western Europe as well as the Czech Republic.

About half of Poldi's output depended directly on Soviet needs, either for export to Russia or for military hardware produced domestically. Exports to western Europe were small (about 15 percent of tonnage) and subsidized. By the end of 1991, Poldi's business had fallen to half its pre-1989 levels. Soviet exports disappeared completely, and losses and debt mounted.

Poldi's urgent need in 1993 was to sell steel. Prospects in the domestic market depended on the economic health of big customers such as Zetor, PBS, and Aero Vodochody, which was not good. Expanding sales to western European customers was hampered by the market downturn in the European Union and by trade restrictions. By the end of 1993, the plant was operating at a third of capacity. Poldi could not afford to pay its electricity bill nor its scrap iron supplier and consequently endured power cuts and raw material shortages. At one point Poldi cannibalized its old, unused physical plant for scrap iron to make steel. Younger managers voiced discontent with the company's lack of strategic thinking. No money was available for new information systems or new technology.

The Czech government sold a majority interest in Poldi in a bidding contest in 1993. Among three bids, one at CZK 1,750 million was more than twice as high as the next closer bid, and it was accepted. (A report that the buyer learned of the competing bid and pencilled in a '1' before his original '750' at the last minute was not denied.) The new owner was Bohemia Art, a small company (800 employees and CZK 500 million in revenue in 1992) that was in the art and architectural restoration business. Bohemia Art was owned by Vladimír Stehlík, a 50 year old Czech. Neither Stehlík nor his company had any experience in the steel business.

Stehlík raised the price of Poldi steel to German customers and lost those customers. He tried to cut out distributors and sell direct to customers. Output continued to drop but employment stayed the same. Losses worsened. Bank debt grew. In November 1996, Vladimír Stehlík and his son, Marko, were jailed

on charges of "illegal property transactions and misuse of information in commercial transactions," or tunneling. Poldi shut down shortly thereafter.

Several former Poldi managers said that Poldi's demise had been allowed purposefully by government officials. The Czech Republic's high steel capacity and low labor costs were worrisome to the EU. Some of the Czech capacity would have to go. According to one senior Poldi official, the government allowed a bad privatization so that Poldi would fail and the reduction in capacity would be accomplished without government officials having to shut down or consolidate companies. Whether through bad luck or clever scheming, steel-making capacity in the Czech Republic was reduced. After a century of history in Kladno, Poldi Steel was only a barren landscape of rusting machinery and empty halls.

Veba

Veba (Vĕ′-bah) was a century-old maker of cotton textiles located in the small town of Broumov in northeastern Bohemia. With Poland on three sides and a mountain range on the fourth, Broumov was isolated from the rest of the Czech Republic. Veba's two main product lines were damask yard goods and terry products, principally towels and robes. The company's revenue in 1990 was CZK 650 million (about USD 19 million at the early 1998 exchange rate), and it employed 3,200 people.

Veba did the spinning, weaving, finishing, and some sewing of its products. Purchase of raw cotton and product sales were handled by Centrotex, the foreign trading company for the textile industry. Nearly half of Veba's products were exported, mostly high quality damask products to western Europe (much of which was re-exported to Africa). Less than 10 percent of Veba's revenue depended on other Soviet bloc countries; most of the terry products were sold domestically.

Veba was privatized in 1992 via voucher privatization. In 1996, Centrotex bought two-thirds of Veba's shares from investment funds to gain control. Veba managers welcomed the Centrotex purchase because they were uneasy about being owned by investment funds that did not have expertise in the textile business or by a new majority owner that might shut down the mills to eliminate competition. Centrotex

had helped Veba avoid one such hostile takeover in 1995.

A new general director, Josef Novák, was appointed in 1993. He was age 38, had an economics master's degree and was head of the sales function in 1989. He had traveled extensively during the communist era to the West and was a fluent English speaker. Veba had a tradition of strong management and little government ministry interference, partly because the textile industry was not considered to be important strategically during the central planning era. In addition, Veba's geographic isolation contributed to a sense of resilience and independence.

Based on a strategic analysis conducted in 1993, Novák concluded that Veba's competitive advantage was product quality and that its main threat was low-cost, middle-quality Asian producers. Veba accordingly sought to increase its business in the rich markets of western Europe and North America and to produce more high quality, high margin finished products. Initially, Veba extended its damask product line by adding king size bedding, finished tablecloths, and jacquard shirting, borrowing from Czech and German banks in 1993 to do so. Veba also entered a new market by selling complete sets of bedding, towels, and robes to luxury hotels in Europe. Plant rationalization began in 1994 and continued through 1997.

Business results for Veba were reasonably good throughout the transition. The company was profitable in every year except 1993. Receivables that threatened to become a problem during the liquidity crisis in these years were managed vigorously and were kept small relative to revenue. With the help of a Dutch husband and wife consulting team, Veba implemented an activity-based cost system, an inventory management system, a new accounting system, and market expansion into western Europe and North America. Novák said about the consultants, "We did not have a sophisticated program [with the consultants]. Their approach was to raise questions. Others looked for a report, an analysis, an easy fix. Not us. They had a good impact on the long run. They were reasonable in their approach. They had experience with the Czech mentality. They worked with other Czech firms before us. They were patient

enough and relatively inexpensive. Their biggest value was the new ways of thinking

Novák obtained his first North American contracts in 1997. Veba was competing in one of the largest, most demanding markets in the world - - "our emerging market," in Novák's words.

Zetor

Zetor (Zĕ′-tŏr) was a monopoly manufacturer of medium-sized farm tractors located in Brno (Newman & Nollen, 1995), founded after World War II. It was the biggest enterprise in Brno with 10,000 employees, annual output of 27,700 tractors, and revenues of CZK 4,000 million in 1989 (about USD 115 million at the early 1998 exchange rate). Zetor also had two small businesses making spherical roller bearings, and castings and forgings, of which only a few of the latter were used in tractor manufacture.

The Zetor tractor was a low-specification machine that was sturdy, easy to repair, simple, yet technologically up-to-date. It was low in price and represented good value for money. It had a reputation as "the best communist tractor" before 1989.

Over three-quarters of Zetor's output was exported in 1989. Nearly one-third of all its tractors went to other Soviet bloc countries and another 25 percent was exported to countries in western Europe and North America. Zetor's single largest customer was the government of Iraq which accounted for another quarter of its sales in 1989. Export sales were handled entirely by Motokov, a state export trading company. Domestic sales were handled by Agrozet, another state trading company. Zetor designed and manufactured tractors. It did not sell, service, or finance tractors.

Zetor was privatized in July 1993 through a merger with its engine supplier, Brno Diesel. The bearings business and the non-productive assets were privatized separately. In October 1994, Zetor was recapitalized in a debt-equity swap, and the Konsolidační Banka (a government bank created to facilitate privatization) acquired 79 percent of Zetor's shares. Business conditions facing Zetor in the early years of the transition were poor. Tractor exports to the former Soviet bloc dropped more than half, and exports to Iraq disappeared completely because of the Gulf War embargo. Zetor lost money every year between 1994

and 1997 and was expected to lose money until 1999.

A new managing director in his 40s, Miroslav Poláček, took over Zetor in July 1993. Poláček had been head of production at Brno Diesel, the engine company. In 1993 Poláček had very little experience in the West and was not an English-speaker. He reorganized the company several times, creating "daughter companies" that might be sold, adding business units, and consolidating business units on the advice of members of his Board of Directors. He made technical improvements and design modifications in Zetor's tractors but quality and on-time delivery remained serious problems. He began installation of a new information system that ran a year or more behind schedule. He undertook some rationalization and modernization of the plant beginning in 1995, financed with new borrowing, but was unable to complete it. Bank loans increased to half of Zetor's total assets by 1995.

Despite some progress, Zetor's performance was unsatisfactory. Output only inched up from its 1992 low point, and revenue decreased in real terms. The over-capacity world tractor industry was dominated by four large producers. An attempt to sell Zetor to the U.S. manufacturer, Deere and Company, fell through. Deere had become a major customer for Zetor in 1993, purchasing tractors for Latin American distribution. Deere moved five employees to Brno to oversee operations and help Zetor improve its product quality and service orientation. These efforts were less successful than hoped and Deere pulled out of Brno in 1997. More debt was restructured in 1997, giving Konsolidační Banka a 98% stake in Zetor, while Zetor searched for a much-needed strategic investor. However, in early 1998 Konsolidační Banka sold its Zetor shares to Motokov, effectively eliminating a strategic investor. Motokov had no money to invest in Zetor and little know-how to share.