A new face of Europe emerging

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The new face of Europe

Central Europe was the venue for the recent Global Executive Forum. We traveled to Austria, Czech Republic, Hungary, Slovakia and Slovenia, meeting with high-level officials to learn how their economies were faring in the post-communist era. I was reminded of another trip we took to this part of the world twelve years ago.

In 1992, we led a business executive group to Prague, Warsaw and Budapest. This was just after the Berlin Wall fell and the USSR collapsed. These countries had just installed the first democratic governments and were either contemplating or implementing reforms such as privatization, as they began the process of opening up to the world. At that time, there was a mix of enthusiasm, fear and puzzlement. Previously state owned companies that had been privatized were trying to understand what it meant.

In their prior lives somebody from the outside told them what to produce, how much to produce each month and allocated them the resources to meet their quotas. As privatization progressed, they had to figure out what a “market” was, how to acquire resources, how to finance and how to sell to the market. This produced a lot of anxiety as these were, for the most part, yet to be acquired skills. In addition, the change in governments was traumatic for many citizens as privatization usually meant unemployment, which was unheard of in Communist times.

As one professional said to me at that time, “Under the Communists we were all poor but we were safe. Now we see some people becoming very rich but many don't have jobs and the safety net is gone.”

Twelve years later, these countries, which have had several governments since 1992, have just entered the European Union--the "major league" of democracies and open market-based economies in this part of the world--and are still working on privatizing state-owned industries.

On May 3, 2004 ten countries entered the EU (Czech Republic, Hungary, Slovakia Slovenia, Cyprus, Estonia, Latvia, Lithuania, Malta and Poland) bringing the total to 25. Most of the 10 were former Soviet controlled countries of Central and Eastern Europe. These countries are still developing, with GDP per capita at one-quarter to one-third of the Western European members. The new members are still in the process of privatization and each of them we visited is actively seeking foreign investment.

More kids or more immigrants

Everywhere we visited we asked citizens of each country about entry into the EU and what it meant to them. Virtually all of them didn't know what to think or weren't sure what the impact would be. They seemed quite passive about it although each country voted in a referendum and the vote was positive in each case.

The most optimistic and enthusiastic were the people under 30 years of age who have grown up in a post-Communist world. They have experienced the turmoil of reform to a market economy, learned to deal with it and are finding lots of opportunity. They are the entrepreneurs and they see lots of business deals coming their way.
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The young people we saw, particularly teenagers, had both hands full all the time. One hand held a cigarette and one hand held a cell phone. Many more young people seem to smoke although our 22-year-old guide in Prague said the new trend for the young is to not smoke.

The folks who are of the parents' generation, over 50 years of age, have not responded the way their children have to the new face of Central Europe. The older generation grew up under the Communists, often witnessing the brutality of the regimes of the 1950s-1970s, and learned to survive. They are not entrepreneurs and even after the fall of the Soviet Union, they have not made much of an adjustment to take advantage of their economic freedom. Truly, the future lies with the younger generation, which is why several of these governments are offering subsidies to families to have more kids.

Western Europe is a rapidly aging area with low birth rates and, hence, fewer working age people to build Social Security reserves for the retired folks. The new EU countries are trying to stimulate birth rates to assure an adequate workforce in the future. In Slovakia, for example, the next generation of workers will be either young Slovaks or young immigrants from their Eastern neighbors or other poor countries in the region.

Disorienting changes

One story that stands out is a conversation with our local guide in Piran, Slovenia, on the Adriatic Coast. He was about 40 years old, had lots of business interests and saw a lot of opportunity for himself. However, he emphasized that most Slovenians did not have the perspective needed to take advantage of economic opportunity. He felt they were passive and too often looked to the government to solve their problems. What the country needed, he said, was an influx of Western entrepreneurs to stimulate economic development.

To explain the prevailing attitude of apathy, he spoke of his 93-year-old grandmother who had lived in the same house in Piran her entire life. "She lived in one house but four different countries during this time," he said, underscoring the disorienting changes in this region over the last century.

So for many older folks in this region the EU is just another conquering force, albeit an economic conqueror, and they will lay low and see what develops before deciding if it is good or bad.

Some of the more entrepreneurial businessmen we spoke with see opportunity in their country but say there is much need for reform. Among their Western European neighbors, Germany and Austria are viewed as rich and unmotivated. German companies are hanging on by their fingernails because they are such high-cost operations and the only way they can go is down.

One businessman described Austria as a no-growth country of small and family businesses that were self-satisfied and didn't want any change. They said: "In Austria a company knows that it has to come up with something new every five-seven years so they try to do that. But other than that they don't want to grow."

Each of the countries we visited relied on "cheap foreign labor" to do many of their low-end jobs. The workers come from Georgia, Ukraine, Turkey, the Middle East and North Africa, some of them legal and some not. Most Americans tend to think that the movement of low-wage jobs to developing countries is primarily a US phenomena, but it's happening all over the world. No matter how poor a country's economy, there are still lots of low-end jobs that attract workers in even poorer countries.

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The businesses in Slovenia that need math and computer scientists get them from Romania, which has excellent university programs in these areas.

The Slovak Republic has adopted an across the board flat tax rate of 19 percent for personal and business taxes. Hungary is adopting the same structure and the Czech Republic is discussing the same. This is causing much concern in western European countries, especially Germany and France, where tax rates are more than double those of Slovakia.

A major strategic issue here is the viability of the social welfare benefits accorded to western European citizens who have unmatched vacation, sick leave, maternity, job protection, health care, education and retirement benefits. In some of these countries, unemployed individuals receive 80 percent to 90 percent of the income of employed people. Hourly wages in Germany are 8-10 times the wages in Central Europe. In Slovakia, where there is major investment of global auto manufacturers, the workers earn about $4.50 per hour compared to $40 in Germany.

Even under the Communists, the education system in these countries was strong, so the workforce is well educated and skilled. There will be a struggle for the high-wage developed countries of the EU to compete with their new members. In fact, this has been the case for over a decade and is reflected in the long-term unemployment in western Europe which is approaching 10 percent. In the US, an unemployment rate of even half that rate is seen as too high.

Forum member Peter Widmer feels EU enlargement will be good for all of Europe. Peter is a Swiss citizen and retired investment banker whose insights we value. He says, "There is plenty of room for optimism over the outcome of this unprecedented and peaceful enlargement of the EU as an economic and political bloc."