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Managing Deep Restructuring: Danish Experiences in Eastern Germany[1]

Abstract

This paper discusses the restructuring in post-socialist economies. Case evidence from East Germany illustrates that foreign investors must do more than provide crucial resources and integrate firms into global production networks. They also have to become involved in the process of organizational change in the enterprise itself. This is often inhibited by compatibility problems and discrepancies between the new strategic management and the local organizational culture which evolved under socialism. Therefore, post-acquisition management in former socialist firms needs to take an evolutionary approach to organizational change. To facilitate the process of organizational integration, to train employees to operate in a market-economy which requires the communication of tacit managerial and organizational knowledge. This paper offers some suggestions as to how this may be done.

Keywords: Enterprise Restructuring, Post-Acquisition Management, Organizational Change, Systemic Change, Eastern Germany.

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1. Introduction

Many foreign investors in the countries of the former Soviet bloc found the task of converting acquired firms into competitive units of their multinational operations more cumbersome than they expected. The costs incurred in restructuring and integrating formerly state-owned firms frequently exceeded the costs of the original acquisition.

In this paper, we analyse this process with an evolutionary economics perspective.[2] The enterprise transformation requires quantum leaps forward in several dimensions, including ownership structures, corporate strategy, operational management and corporate culture. However, firms as organizations follow an evolutionary path of development. Some key variables may be changed by a shock-therapy, for instance the ownership or strategic objectives. Foreign investors can overcome major barriers to strategic restructuring by providing crucial resources and integration into an international network. Yet an organization as a social organism adapts only gradually to external changes. The basic routines and attitudes of groups and individuals have a high degree of persistence and adjust to changes in the environment in often unpredicted ways. Therefore, the superimposition of new institutions may lead to frictions between the agents of change and the previously existing organization.

This research is based on three cases studies of Danish investors in Eastern Germany - with quite distinct experiences. Rockwool, a world leading manufacturer of stone wool, acquired via its German affiliate a producer of isolation materials in Eastern Germany. They succeeded to upgrade the production line to a capable supplier within the investors network. Danisco, a food processing conglomerate, took over eight sugar refineries. They invested in technological upgrading, accelerating technological progress, but changing little in the basic rationale of production. Managers experienced unexpected obstacles but, seen in perspective, the integration went smoothly and can be judged as a success.

MEAT A/S,[3] on the other hand, intended to move a meat processing plant from a Fordist-type production based on economies of scale and standardized products, to modern production management with high diversification and flexibility. This required deep changes in the organizational structure and in the corporate culture. In attempting to take several steps of organizational evolution simultaneously, the investor encountered tremendous obstacles.

The paper is laid out as follows: in section two, we review the experience of enterprise transformation in Eastern Germany using the concepts applied for analysis in other transition economies, and reflect on the impact of politics on the enterprise transformation. We argue that the shock-character of change inhibited an evolutionary process of institutional development.

In section three we present the cases of Danish investors. In section four we interpret the findings of the case studies, identifying several influences impeding the process of strategic restructuring. The main

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[2] See Nelson (1995) for a review of evolutionary economics. Evolutionary analysis has been applied to the East European transition e.g. by Murrell (1992), Kogut (1996) and Swaan (1997).

[3] ‘Meat A/S’ is used to protect the anonymity of our case firm.

underlying cause is, in our view, that the adaptation of routines and attitudes in local business units did not evolve along with the strategic changes at corporate level introduced by new owners. The existing national and organisational cultures conflicted with the new strategies and work organisation introduced by foreign investors.

We conclude with section five which points out implications of the evolutionary perspective on the management of change in countries undergoing economic transition. Although East Germany's transition may be very different in a macroeconomic perspective, many of the managerial challenges are very similar across Eastern Europe and the former Soviet Union.

2. East German Enterprise Transformation in Perspective

The tasks of enterprise restructuring in transition economies are summarized in figure 1. The first step of enterprise transformation was passive: the central plan system broke down. Some observers, e.g. Abel and Bonin (1993), thus speak of 'plan desertion' rather than market reform. This step was formalized by giving enterprises their own economic identity through formation of limited liability companies, in the German case AG's and GmbH's. This commercialization thus created economic agents, and managers found themselves with the responsibility for a wide range of decisions entirely different from anything experienced under the previous regime. Initially, newly established privatization agencies, in Germany the Treuhand-Anstalt, held all the shares, but did generally not interfere in the day-to-day operations of the firms.

Figure 1: Strategic Transformation

Socialist Firm	==>	**Competitive Private Enterprise**
Production unit in the central plan	*Commercialization*	Economic agents
State owned	*Privatization*	Private owned
Low productivity Inputs and production volume are determined by the plan	*Defensive adjustment, downsizing*	Competitive productivity Adjustment of production volumes and inputs to demand and costs
Plan bargaining Products at the end of their life cycle Passive financial transactions Plan fulfilment Vertical and horizontal integration	*Strategic Restructuring*	Strategic management Products at early stages of their life cycle Financial management and accounting Marketing New boundaries of the firm

source: based on Meyer 1998

In terms of formal changes, privatization is the second step. Through privatization, ownership of the firm is transferred to one or many private owners, who are expected to take control over the firm and to instruct management to steer the firm through the rough waters of competition. As new owners would normally be profit oriented, they would create incentives for management to act in a profit-oriented way.

Across Eastern Europe, the formal changes occurred following lengthy political processes of establishing the legal framework and often equally complex negotiations over the arrangements for each individual enterprise. During this time, enterprises had to start their restructuring process. As ample empirical evidence shows (reviewed by Brada 1996, and World Bank 1996), enterprises did start restructuring ahead of privatization, though primarily in a passive or defensive way. Managers made short-term adjustment to output and input levels to increase productivity. They changed production volume, employment and capacity to reflect market demand, and reduced operating costs and exposure to bad debt. Studies also find evidence of entry in new domestic and foreign markets, though mainly for existing rather than new products. Only occasional evidence suggests that managers took advantage of the weak governance structures at the time to divert assets from state-firms to their private interests.

However, strategic restructuring emerged only very slowly, and indeed rarely without cooperation with a foreign partner. Yet only strategic restructuring positions the enterprise in the competitive environment for the medium or long-term. It requires the development of marketing and finance as functions in the company, and the introduction of new products that are in demand by the market. Often strategic restructuring also required the sale of operations because of the high degree of vertical and horizontal integration that was efficient under a state-planning regime, but is not in a market economy. The strategic restructuring is inhibited by four gaps faced by transition firms (Meyer 1998):

- The access to financial resources is inhibited by an underdeveloped financial sector and the high risk of investing in an uncertain environment.
- Weak systems of corporate governance often lead to ineffective control of owners over management, or conflicting interests of insider-owners (Frydman et al. 1996).
- The success criteria for management and entrepreneurship in a market economy differ fundamentally from the leadership skills, experience and vision that evolved under socialism.
- Relationships with customers and suppliers have been interrupted, and new contacts to international production networks have not yet been established.

If firms are sold to foreign investors in the course of the privatisation, the western firm takes over the control of the firm. Western investors control crucial assets that can facilitate successful transformation, bridging the aforementioned four gaps (figure 2).

The formal changes of commercialization and privatization, and the defensive and strategic restructuring evolved gradually in most transition economies, with no clear pattern of sequencing. Indeed, even privatization did not induce strategic restructuring in many firms, especially if they were transferred to insider control or if ownership was widely dispersed (Brada 1996). In contrast, a clear sequencing could be observed in Eastern Germany:

(1) Commercialization ==> (2) Defensive Restructuring

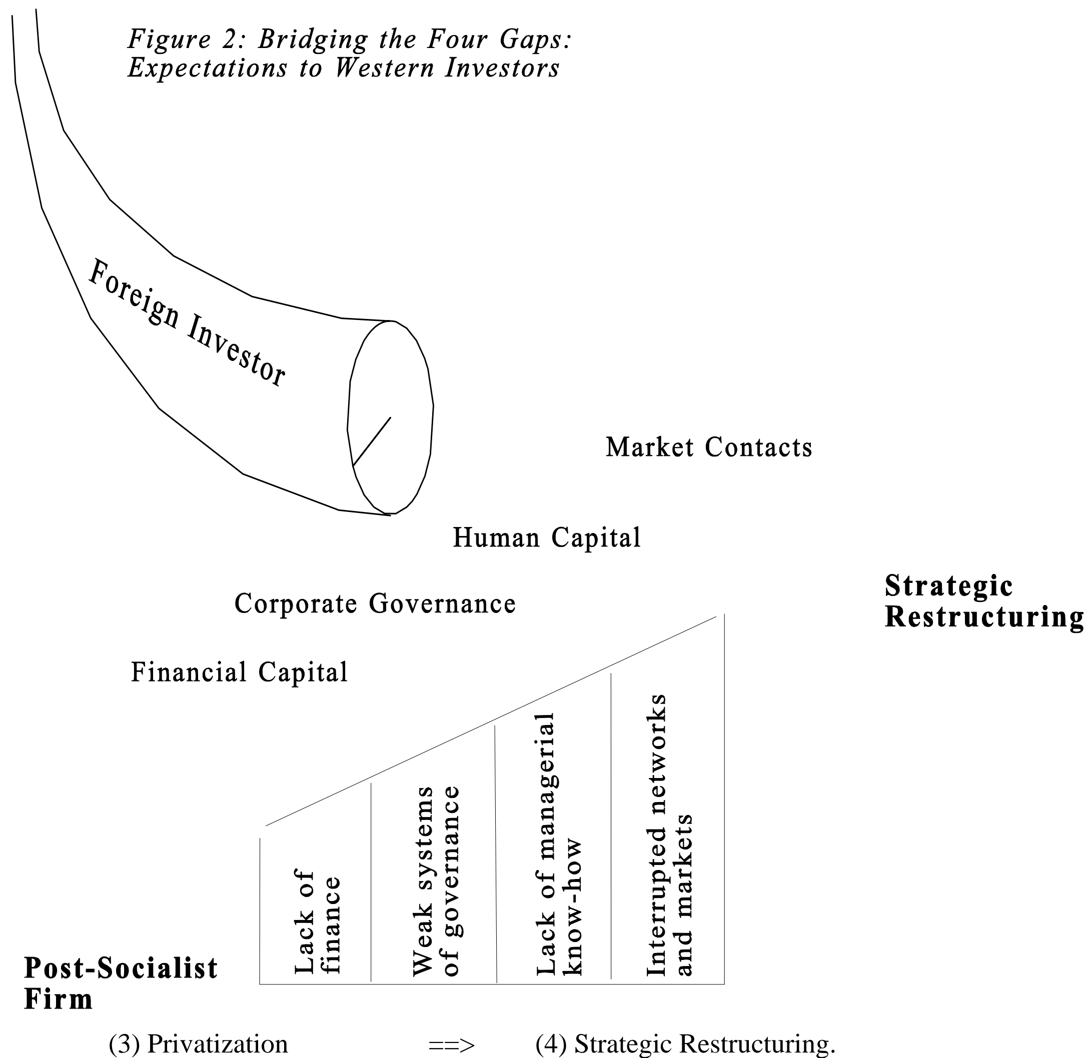

Figure 2: Bridging the Four Gaps: Expectations to Western Investors

In 1990, the Treuhand-Anstalt was created as a holding company for all industrial enterprises in the still independent German Democratic Republic. By law, its objectives were defined as the privatisation of the enterprises and the recreation of competitiveness for the firms under its control. Following German unification, the agency concentrated on privatization of firms through auctions and, for large firms, by individual negotiations with potential investors. Voucher schemes, which were common in most other East European countries, have never been seriously discussed for Germany. Before privatisation, companies were dis-integrated to reduce the extent of vertical and horizontal integration. In some cases, such as the sugar case below, several small firms were sold together as one unit. The individual approach to privatisation enabled the Treuhand to set specific conditions for each privatisation project, including employment and investment guarantees. Most firms were sold to West German companies in the same industry, which thus were able to expand their operations to the East (Geppert and Kachel 1995). Less than 10% of firms were sold to foreign investors.

Prior to privatization, the Treuhand made resources available if they were needed for adjustments in the firms. Yet, with few exceptions, the Treuhand permitted only investments that were 'investor neutral', that is investment should not favour one potential acquirer over another (Müller 1996, Geppert and Kachel 1995). This however excludes, by definition, any strategic investment as described above.

The policy was motivated by the desire not to throw good money after bad at a time when there was not an effective mechanism of corporate governance that would insure effective allocation of the funds. Evaluating individual investment projects proposed by its 10,544 affiliate firms is simply beyond the managerial capability of any state-holding company (Müller 1996). Delegating restructuring to the managers would have resulted in complex principal-agent relationships which, because of continued soft budget constraints, were unlikely to create suitable incentives for managers (Brückner 1997).

While the ‘privatization-before-restructuring’ approach appears sensible from a corporate governance perspective, it implied that East German firms were unable to initiate strategic investments during the time of most radical changes in their markets. During these crucial months and years, they were unable to take strategic decisions that would stimulate a positive evolutionary process of organizational change. In fact, there was enormous strategic investment in Eastern Germany at the time by West German and foreign businesses dividing the markets, almost, amongst themselves. Few independent East German firms were able to develop marketing assets, such as brand names, though some retained brand names proved valuable later. Only after privatization and under new ownership, firms could initiate strategic restructuring and (re-)entry to competition as affiliates of western firms.

Since the initial barriers could rarely be overcome without a western partner, the process of change was very much directed by outside ‘change agents’, rather than through self-reflection, learning and adaptation of the organization itself. Sociologists thus speak of an externally determined transformation in East Germany which explains some of the frustration often felt in Eastern Germany, but not in neighbouring countries (Wiesenthal 1996). Thus enterprise transformation generally did not build on an evolutionary process within the organization, but started with a forced break with the institutions of the past which were perceived as a liability by the new owners (as well as many new local leaders). Our three case firms illustrate dimensions of this process.

3. The Cases

The case studies provide insights into technological modernization induced by foreign investors, and the subsequent learning processes and organizational restructuring in the acquired firms. All three cases analyse Danish investors who entered in 1991, in competition with other West European companies. The research is based primarily on on-site interviews with individuals at different layers of the new organization, including Danish, West German and East German managers as well as shop floor workers in 1992. Up to 24 interview partners were selected as key agents for the process of transformation, or as actors at crucial position in the organization. The field research was followed up, and reviewed, with archival research and with interviews in corporate headquarters in Denmark (Bjerg Møller 1996).

3.1. Rockwool International A/S: Technological Upgrading in a Stone Wool Company.

The Danish Rockwool Group is the world’s largest manufacturer of stone wool, with around 6000 employees worldwide and an annual turnover of more than US$ 800 million. Stone wool is the basic material used by the group for a variety of applications, most importantly thermal insulation and fire protection (82% of turnover). The company is active worldwide, but focuses on the markets of the European Union where Germany is the largest single market.

In recent years the group has seen a strong expansion into Eastern Europe, where the acquisition in

Flechtingen, East Germany was its first stepping stone in 1991. The strategic objective was primarily to enter the rapidly growing East German building markets with the opening of a local marketing office in 1990. In 1993 and 1995, Rockwool also acquired two factories in Poland. The East German production facilities are managed from the West German affiliate, who took the leadership for the restructuring and integration of the acquired firm.

The acquired firm had been established in 1985 to manufacture insulation materials using western technology, but it was inhibited by unreliable supply and by product quality problems. In 1989, the markets and networks of the GDR building industry broke down. The firm initially survived by assigning some of its employees as a sales force in order to establish contacts with the new building industry. However, they faced the uphill struggle of a small, technologically inferior player in a market dominated by large Western competitors.

After the take-over, Rockwool followed a strategy of technological transformation through gradual investment. It was based on the introduction of latest technology and the integration into the production structures of the West German Enterprise. The first step was to rebuild the production with a single specialized production line based on company specific technology. New lines were to be added later. The production was shut down for three months to rebuild the systems and to train all East German employees. Rockwool reduced employment from 400 to 200. The remaining employees were educated in formal courses held in West Germany and through continuous workplace instructions by West German colleagues.

This investment and training strategy reduced the capital investment required to about US$ 15 million, compared to US$ 60 million for a new factory. It clarified the envisaged strategic role of East German firm, and thereby gave its employee a vision, and defined goals to pursue, soon after the take-over. Interview participants from both sides considered the strategy of the initial transformation period to be fruitful, and feasible because of the rather small size of the acquired firm. The employees appreciated the training but were critical of general courses such as PC instructions that were often considered inadequate. On the other hand, employees praised the practical workplace instructions as useful and interesting.

After the rapid transformation, the firm had one Western top manager in Flechtingen, while marketing and sales were managed by West Germans, who initially were based in a marketing office in Magdeburg. Thus, Westerners remained in charge of the external relationships of the firm, whereas the internal organization, including the production as well as personnel and accounting departments, was run by East Germans.

3.2. Danisco A/S: High-Technology in the Sugar Industry.

Danisco A/S is a Danish food-conglomerate with sugar, ingredients, food and beverage, and packagings divisions. Danisco Sugar accounts for 37% of corporate turnover, and is the market leader in Denmark and Sweden. To broaden its area of operation, Danisco Sugar entered Eastern Germany in 1991 to expand production possibilities and to enter the German market.

The sugar industry is one of the most regulated industries in the European Union (EU). With the German Unification, the EU regulation was extended to Eastern Germany giving each of its 43 small sugar refineries a quota under EU rules. This quota turned out to be the most attractive asset of the firms

in the perspective of prospective foreign investors, even though they are location-bound and thus require production in the region and procurement from local sugar-beet farmers. Initially, the Treuhandanstalt sold the sugar refineries to West German sugar refining companies. Following complaints to the EU monopoly regulators, Danisco A/S could enter a bidding process for 8 sugar refineries in the Vorpommern area that were sold ‘en bloc’.

During central planning, the sugar industry was a neglected industry. Production technology was, according to Danish managers, lagging 10 to 25 years behind West European standards. This led to frequent production stops and severe problems in maintaining product quality. According to the Danish management, their role was to provide financial resources and implement technological modernization to overcome bottlenecks in crucial resources.

The initial acquisition covered eight factories. Yet Danisco’s objective was to establish one single large production facility which would be integrated into the production structure of the parent firm. Transformation thus required closing down the old plants while output at the new production facility rises.

Employment has been reduced to 249 in 1994, from 1600 at the time of privatization and 3000 before 1989. Thereafter employment increased to 269 in 1996. The future workers were selected based on work experience and an age limit of 40 years. Management explained the age limit with the considerable costs of staff training. East German employees had a specific education for the sugar industry. Although they were used to other types of technology and, in the closed GDR context, had no access to international know-how, they possessed essential core skills.

The Danish management chose a strategy of radical technological modernization thus jumping over stages of development that western sugar refining went through during the past decades. Danisco introduced formalized education programs to enable the move to centralized, computer-based operations. The small group of production managers and skilled workers selected for these jobs participated in two week-long courses in Denmark, introducing them to computer technology and upgrading their knowledge of sugar processing technology. It continued as training on the job with technical engineers available to support employees at their work place.

Danisco retained East Germans in the key local executive positions, while technology experts frequently visited the plant. Only two Danish expatriates were stationed permanently in East Germany, both as co-managers, one beside the local general manager and one beside the technical manager. During a transition period of two years, the East Germans gradually took over as the executing actors. Both stated that the scale of transformation in such a short time would not have been possible without the escorting management from outside.

In retrospect, a Danish manager evaluated this technological transition as undramatic. It is however important to note that the training of local employees focused on operative functions. Projecting and programming engineering, as well as marketing and sales, are managed in Copenhagen. Notable difficulties emerged during the integration of budget management into the accounting system of the company. During central planning, the firm had detailed book keeping but no budgeting. Therefore, a Danish co-manager was accompanying the East German budget manager for years to supervise the financial management.

3.3. Flexible Production in the Meat Industry

MEAT A/S is a meat processing firm which until recently was part of a major Danish multinational corporation. Its strategic acquisition of a meat producer based near Berlin aimed at penetrating the German market. In the acquisition contract with the Treuhandanstalt, MEAT A/S committed to invest US $ 35 million in modernization of the production, and to guarantee employment for 1250 persons for three years.

IN the past, the East German firm used to slaughter and process meat on a very large scale. Its production technology was of international standards as it had been established as prestige project of East German engineering using imported machinery. Technologically, the facilities were among the largest and best equipped in Europe. Nevertheless, the firm was poorly prepared for the market economy. It focused on economies of scale and the production of a standardized product, procuring meat from a single supplier and delivering output to Berlin and to the export ministry. With the break-up of both the supplier and the customer relationships, this mode of production became uncompetitive.

However, its geographic location brought MEAT A/S close to the large and growing market of unified Berlin. Here, existing and anticipated new supermarkets were the prime target. However, the market was dominated by West German suppliers. Unexpectedly, MEAT A/S faced a major image problem as an East German producer in West German markets. Procurement also became a major obstacle when the sole previous supplier, a nearby cattle combinat, was closed.

The restructuring was led by a team of Danish and West German managers who occupied all top positions in sales, marketing, and financial management, as well as middle management positions in the personnel and logistics departments. Among top management, only the production manager was East German.

To be able to compete in new markets, deep restructuring of the production was essential. New types of customers required customer specific products, individual packaging, flexible production adjustment with small batch sizes, and market-oriented product development. The production process needed to become far more flexible, differentiated and responsive to customer demand. This had major implications for factory floor work organisation.

In the GDR, firms had large reserves of workforce and materials. The plant was organized in specialized sub-units with their own closed structure based on functions and responsibilities. The division of work had been taken to an extreme, and each worker had a rather narrowly defined job description. This structure had to be broken up, and workers had to extend their perspective and their knowledge of connected areas and relations. Every worker had to extend his/her activity to - as the management put it - ‘flexible work arrangements’.

Shop floor team leaders and workers had to organise themselves according to broad objectives. The new work organisation required frequent changes of the type and place of work. This was a radical break because in the old system a steady workplace was a sign of respect to a skilled worker. Everyone worked hard at his specific function during the periods of stress, while in between, they socialized. The interviewed shop floor butchers expected that the “chaotic changes” would stop at some stage in the future once market relations were established permitting a return to the previous stability.

In the new organization, costs, time, and quality control are essential. In the GDR, the key economic

variables were stated in volume, and thus the prime concerns were the *volume* throughput and the procedures of cutting meat. With the changes, the organisation was expected to maximize the *value added* of its meat products, a subtle but essential difference. Most difficult to convey to the local workforce was the practice of "working up" meat, that is the use of meat additives. Danish managers described this problem as East German workers being unable to "see money". The lack of adequate organizational solutions to the problems of cost-awareness and detailed quality control led to excessive use of expensive inputs. In the words of a Danish manager:

> "It is a danger for losing really much money quickly if you are not in control of what is going on. There is nothing easier for a 'Meister': If he wants to avoid quality problems, he simply makes the sausage a little bit better than it should be, and that is expensive! That is very expensive. He must be in control of that!"

The problems with respect to cost and quality control persisted even among the new function leaders. The new work organisation delegates tasks of coordination, planning and decision making. Now, everyone, from top management to shop floor worker, has to analyse situations ad hoc, develop alternative solutions, and take responsibility for decisions.

Western managers described this as problems for the Easterners lacking comprehensive and connected knowledge about the basic production rationality. Although the GDR firm had detailed computer-based production planning, it had no adequate follow-up and fine-tuning of the actual process. This resulted in problems concerning 'self-reflection' at all levels of organisation, and of "initiative to take action" if unexpected problems emerged. The new organisation created entirely new role expectations for section managers and workers.

4. Interpretating of the Cases

As we expected, the Danish partners made major contributions towards overcoming the four gaps to strategic restructuring. In all three cases, the investor provided capital for urgently needed investments, be it for upgrading of facilities or building new plants. They transferred extensive technological and managerial knowhow and established effective control over the formerly state-owned firms. The break-up of existing supply and distribution networks was experienced in particular by MEAT A/S. The task of establishing new market-based networks was interrelated with the development of new procurement and marketing functions in the firm. Danisco and Rockwool, which to a larger extent competed in Europe-wide markets, overcame the problem by centralising marketing operations in Denmark and West Germany respectively. Yet pouring in resources and establishing new networks turned out to be only part of the task.

The cases show two different patterns of enterprise transformation which correspond to patterns described in the literature for Eastern Germany and other countries of Eastern Europe. Some post-socialist firms can, with some investment in facilities and skills, be converted to a production line of a western firm. Yet, for many others, the transition is not only from the central-plan economy to a market environment, but to a modern multi-product firm. This requires very deep changes inside the firm for two main reasons:

- The adaptation to a new economic system often has to be accomplished simultaneously with the shift to post-Fordist[4] production method, which requires entirely different methods of organizing the business (Sorge 1993).
- Success in a market economy depends on tasks, skills and performance criteria that are beyond the experience horizon of organizations used to the central-plan system. Deficiencies in these areas can only be overcome through the acquisition of tacit know-how which requires an inter-active and time-consuming learning process (Frydman and Rapaczynski 1997, Swaan 1997).

Industrial production in the former Soviet bloc was based on the Fordist model of production with high job specialisation and extensive use of economies of scale. Some plants, like those acquired by MEAT A/S and Rockwool, produced a standardized product in facilities of high technological standards. From this base, Rockwool developed its new East German affiliate as a specialised supplier while reducing employment. The transformation had, compared to the other cases, a clearly defined goal, which required primarily a classic upgrading and rationalisation within the Fordist model of production.

The Danisco case is special due to the regulation of the industry. The restructuring of the sugar plants was also a classic rationalization, but more ambitious in terms of the advance of technological standards. The upgrading could be achieved with less direct managerial involvement by Danish managers as it could utilize existing professional knowledge and experience. Yet, crucial aspects of transformation were bypassed as some parts of management, notably budget-coordination and marketing, were centralized in the Danish headquarters and were thus not part of the restructuring task.

This form of enterprise transformation within the Fordist model is typical for East Germany, and has been criticised as building 'extended production lines' of West German Companies.[5] It solves current problems of the firms, but offers few strategic long-term perspectives. This is not only because of the resulting dependence on top management and innovation in the Western parent firm, but because of the minor role of Fordist production in Western Europe at the end of the 20th century. Its competitiveness is based on, in Porter's (1983) terms, 'cost-leadership' which, with few exceptions, is not sustainable in high wage countries. Therefore, growth industries in West Germany are focusing on up-market segments. With its high labour costs, East German industry has to follow this direction. Exceptions may exist in industries with high transportation cost such as staple foods (e.g. sugar) or building materials (stone wool), and in capital intensive production. Yet, these industries are too small to generate the

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[4] 'Fordist' production refers to the classical mass-production technology with rather narrowly specialized labour first introduced by Henry Ford in automobile manufacturing. Post-Fordism refers to various alternative types of decentralized production concepts which challenge the classical mass-production.

[5] See e.g. Heidenreich (1993), Geppert and Kachel (1995).

exports and employment that the region needs.

A ‘differentiation strategy’ (Porter) requires not only a diversified product portfolio but also flexibility and worldwide competitive quality. The failure to accomplish this shift to “differentiated quality production” has, according to German sociologist Sorge (1993), been a key failure of industrial transformation in East Germany. Sorge interprets the observed rationalisation as emergent strategies, i.e. not as the result of strategic decisions by management (or the Treuhandanstalt), but evolving from the persistence of habits of leaders within the organisations. Local employees continue their routines, while Western managers in the Treuhand and in the businesses apply concepts of management developed elsewhere and adapted insufficiently to the local conditions.

These observations correspond to the basic tenants of evolutionary economics. While changes in ownership and top management can be achieved within short time, changing the ways an organisation functions is a process that is subject to substantial ‘inertia’. Evolutionary economists consider knowledge of a firm as embodied in the routines it develops (Nelson 1995). Routines enable groups and individuals to follow their objectives while overcoming limits of bounded rationality. However, once routines are established, they are difficult to change. Inertial forces aim at securing continuity for individuals and subunits within the organisation.[6]

However, the discrepancy between established routines and those needed in a market economy is huge in the case of a change of economic systems. It is of greater magnitude than the technological progress analysed in the established management literature (e.g. Adler and Shenhar 1990). Often, a completely different set of routines needs to be developed. This leads to major inertia inhibiting enterprise transformation in Eastern Europe (Michailova 1997).

The case of MEAT A/S illustrates how inertial forces inhibit change even after a foreign take-over. Despite the financial power and management know how of a multinational company, there were great difficulties in implementing deeper changes in the acquired firm. Not only the corporate strategy needed redefinition, but the pattern of work organization as well as individual behaviour and attitudes had to be modernized. Figure 3 illustrates the nature of these changes. Some of the challenges identified for operative management emerged to a certain degree in all cases, but they became most apparent in the case of MEAT A/S. We believe that this case, in particular, illustrates challenges for post-acquisition management across economies in transition.

Figure 3: Challenges of operational transformation

	Socialist firm	**Affiliate of a Multinational Enterprise**
Model of production	Fordist	post Fordist

[6] Inertia in organisational change are also observed for organisations in Western economies embarking on radical change, see e.g. Anderson and Tushman (1990).

Product range	standard, large volume	diversified, small batch sizes
Skills	highly specialised	towards generalists
Work organisation	centralised decision processes, narrowly defined job description	delegation of responsibilities, broad tasks, flexible adjustment to market forces
Business culture	plan implementation based, technological perfection of quantitative target with given means	cost-benefit based, continuous improvement of the value of production using new means under economic considerations
Evolutionary perspective	Stable routines, few innovations	New basic routines, and frequent innovations

To be competitive, MEAT A/S had to offer a variety of related products, each in smaller batch sizes. This required more frequent changes in the production process, and flexibility in adjusting production to market conditions. The skills required were more generalist, in contrast to highly specialist skills promoted in socialist firms. Employees needed to be retrained to master a variety of tasks and take over responsibilities as needs emerge.

5. Building Competitive Enterprises

The level of education in the Soviet bloc was relatively high, especially in mathematics and natural sciences. Technical skills and basic research are generally above those of countries with comparable levels of per capita income. Yet, as Swaan (1997a) showed, complex organizational and technological skills, that would for instance enable persons to apply their knowledge in a different context, are weak. These capabilities involve a high degree of "tacit knowledge". This is defined as "knowledge that individuals possess, but are not able to explain" (Polanyi 1966).[7] It is often team-embedded and requires complex learning processes to be effective. Examples are knowledge on how to manage human relations or how to make decisions under uncertainty.

Thus, the East-West knowledge gap concerns primarily skills that can only partially be transferred

[7] Teece (1977) showed the extend of costs associated with the transfer of tacit knowledge. Kogut and Zander (1992) argue that the tacitness, and thus limited transferability, of knowledge is the core to understanding the evolutionary process of firm growth. In the Eastern Europe transition literature, Swaan (1997, 1997a) showed conceptually and empirically the need for tacit knowledge to accomplish the system change.

through formal education or exchange of blueprints. Rather, it is knowledge that needs to be transferred through active interaction between teacher and recipient, or by "learning by doing". This would explain why our interview partners found active support on the work place and training in the Western parent company more useful than formal training courses. The need to transfer tacit organizational knowledge creates special challenges for managers as they have to communicate aspects of expected individual behaviour that are taken for granted among employees who grew up in a market economy.

Beyond acquisition of new skills, the way individuals interact and relate to their work has to be changed.[8] This affects all levels of the hierarchy from the shop floor to the top management. New procedures for planning and control need to be implemented, a new organizational structure, possibly a matrix structure, needs to be introduced, and a new corporate strategy needs to be developed, communicated and internalized. Top management can be changed through hiring a few key individuals from outside, as we have seen especially in the MEAT A/S case. However, organizational changes at lower levels have to integrate the existing culture and the new corporate strategy.[9]

The change in culture is deeper than the adaptation of corporate culture following an acquisition of a company that also is operating in an established market economy (cf. Cartwright and Cooper 1993, Birkinshaw 1997). This is illustrated in figure 4. The integration of corporate culture within the systemic change has specific features:

- Changes in the internal and external relationships of the firm are interdependent. The nature of new relationships depends on the progress that the firm, its partner, and the environment make on the path of institutional transformation. As all the variables are very instable, it requires frequent readjustment. This interdependence can both accelerate or inhibit further progress if the speed of change differs between partners.
- The required change is deeper than a change within a market economy because the new economic order is based on different attitudes, and even values, of economic agents. Management focusing on strategic integration often appears to pay insufficient attention to the human side of post-acquisition integration.

Before 1989, plan fulfilment was the prime objective - irrespective of cost-benefit considerations. The

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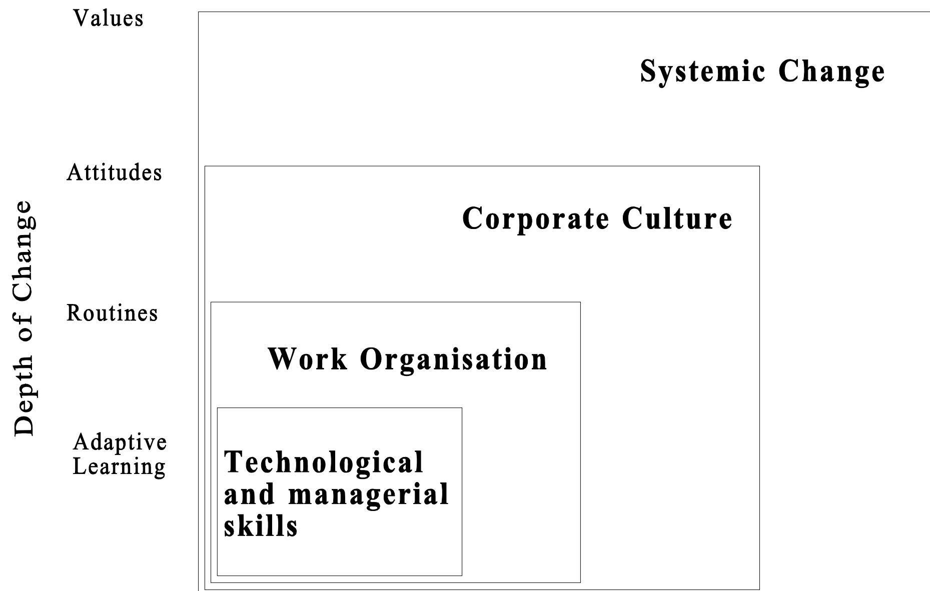
8 Similar arguments have been made by Heidenreich (1993), Aderholt et al. (1994), Puffer (1995) and Michailova (1997).

9 Aniszewska (1997) found in case studies in Poland that change of organisational culture did not reach the shop-floor because of, among other, a lack of information, overly positive self-assessment prior to privatisation and frustration over the lack of appreciation of the (technical) skills of the workforce.

Figure 4: Depth of Post-Acquisition Restructuring



firm was organized around the central plan, and employees were given incentives that encouraged fulfilment of plan targets. As the manager-quote (section 3) illustrates, employees in a market economy are expected to act in constant awareness of the costs and benefits of their activities. In addition, corporate culture has to promote continuous innovation and improvement. The central-planning regime established routines which were stable, as dissent was discouraged and innovation was slow. A market economy does not permit such stability. To stay ahead in a constantly changing industry, firms have to generate innovations continuously, 'mutations' in the terminology of evolution, which generate more productive routines.

The change of corporate culture thus affects not only what individuals do in the firm, but how they do it, and how their activity is motivated, coordinated and assessed. In other words, agents not only have to learn new skills, but they have to change their routines, their attitudes and possibly their values.

6. Managing Deep Restructuring during Systemic Transformation

The challenge for post-acquisition management in transition economies is to facilitate the simultaneous corporate and systemic change. Our case observations suggest that the systemic aspect of enterprise restructuring prolongs the time period of the post-acquisition integration processes (figure 4). This can be explained by the deeper nature of change affecting groups and individuals. However, this need not be so.

The 'plan-desertion' has led to an almost complete break-down of the rationality underlying patterns of behaviour. Therefore, the willingness to accept something new is unusually high, as observed notably

in the Danisco case. Some forces in the environment, e.g. exposure to Western marketing, are supporting changes of routines and attitudes. The ongoing process of cultural evolution may in fact *facilitate* changes in work organization and skills. Post-acquisition management thus may be able to accelerate the process by integrating changes at societal level into its management development programs, and by directly addressing routines and attitudes identified as inhibiting the new organization.

At the same time, strategic management has to acknowledge that it does not operate in a history-free space. The new organization has to acknowledge local roots, or risk severe internal frictions. For instance, shop-floor workers often possess job-specific skills which provide a solid basis to acquire latest manufacturing know-how. Lack of recognition of these skills by the investors, has been a source of resentment by the local work force.

To overcome the discrepancy between Eastern and Western organizations, new solutions may be superior for the post-socialist environment than the superimposition of routines that have been developed elsewhere. Therefore, the experimentation with new ideas and organizational forms should be encouraged at early stages of this evolutionary process (Kogut 1996). New approaches may reach an better synergy between the experience of the multinational investor and the local firm. They may reduce not-invented-here type frictions and make the change process more sustainable.

In this post-acquisition process, training and communication are essential. Training in Eastern Europe should emphasize the transfer of tacit knowledge through on the job training, practical demonstration by Western co-workers, and, if feasible, training on a comparable job in the home country of the parent firm. Such practical experience will raise the cognitive horizon of employees and thus enable them to imitate successful pattern of activity of their Western colleagues.

Finally, effective communication between the new leadership and local employees is needed to convey the basic concepts of the aspired corporate culture (cf. Hasplagh and Jemison 1991). In the case firms, incidents of insufficient interaction, misunderstandings over basic concepts, and language barriers affected communication between the new leadership and the local workforce.[10] this reinforced barriers to the implementation of change.

In conclusion, transformation management requires both sensitivity to the local history and a vision for the future. Miracles may be impossible, but many successful businesses across Eastern Europe, such as Rockwool or Danisco, illustrate the potential of the region.

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[10] see Bjerg Møller (1996) for details on this aspect.

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