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PRESENT TRENDS IN THE FIELD OF BUYING FAST MOVING CONSUMER GOODS IN THE MODERN RETAIL SECTOR IN ROMANIA

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Abstract: The goal of the paper is to investigate the strategic trends in acquisitions in the dynamic field of retailing on the Romanian market. The main objectives are to identify the most relevant changes in the area of acquisitions, as well as their essence and impact on both retailers and suppliers of fast moving consumer goods. The major trends include the adjustment of the buying groups and centrals, the setting-up of logistic platforms and the development of the relationships between suppliers and large modern retailers. This topic is studied within the framework of the ascending evolution of modern retail formats, specifically the expansion of the large international retail chains of hypermarkets and supermarkets that are present in Romania.

Keywords: buying groups and centrals, logistic platforms, relationships, fast moving consumer goods

JEL Codes: M30, M31, M39

INTRODUCTION

The competitiveness of the modern retail formats is a reality reflected by sales and determined by a business model that differs from that of traditional retailing. The buying structures and policies contribute to the accession of the large international retail chains. Hereinafter, several major trends in acquisitions at the level of the large modern retailers existing in Romania are analyzed.

1. RETAIL DYNAMICS IN ROMANIA

The Romanian retail market of fast moving consumer goods (FMCG) is an outstanding case in Central and Eastern Europe (CEE). In 2010, it was the most dynamic market in the region. In 2010, the FMCG retail sales reached Euro 16 billion. During the period 2001-2010, the market increased steadily with an 8.5% CAGR. From 2000 to 2010, Romania registered the highest increase of the retail sales in the CEE region, respectively 123% (Ciobanu, 2011).

The analysts of Oxford Economics estimate a 5% CAGR during the period 2010-2020 (Crăciun, 2011), as a result of the ascending trend of purchasing power, aggressive development of modern trade and shifts in consumption behavior. These factors will lead to a forecasted growth of 62% of the total FMCG retail market value, compared to 57% in Poland, 48% in Czech Republic and 46% in Hungary.

According to the specialists at Contrast Management Consulting, Romania still provides a lot of opportunities for the expansion of modern trade. A thorough analysis – based on indicators such as the consumer purchasing power, the gap compared to developed countries (such as Austria, Czech Republic, Hungary, Poland) and the average price of the land – leads to the conclusion that Romania has a potential for the development of a retail surface of sq.m. 830,000, out of which sq.m. 100,000 in Bucharest (Crăciun, 2011).
For 2011, the total forecasted investment in the modern retail sector is Euro 500 million (Mihai, 2011). Tens of new stores will be developed in Romania. In 2011, the most dynamic players will be Cora, Carrefour, Kaufland, Mic.ro and Mac.ro. For example, Cora Romania has already invested approximately Euro 50 million during the period 2009-2010. Carrefour plans to open two stores in 2011, in Bucharest and Botoșani respectively. The Carrefour hypermarket from Bucharest will be located in the Colosseum commercial center that will be the largest in Europe (based on an investment of Euro 350 million).

The forecasted growth is very likely to be achieved. A supporting argument is the growth in the number of modern retail stores registered in Romania in 2010. According to the research company Nielsen Romania, in 2010, approximately 100 stores (hypermarkets, supermarkets and discount stores) were set up (Mediafax, 2011). More specifically, the number of modern stores increased from 548 units to 642 units at the end of 2010. Consequently, the hypermarkets, supermarkets and discount stores represented 48% of the total retail sales in 2010, compared to 41% in 2009.

This ascending trend of modern trade was achieved on a general background of decrease in the universe of retail outlets. In 2010, a total number of 88,042 stores existed in Romania, compared to 90,372 in 2008. The descending trend was due to traditional trade. During 2008-2010, the number of kiosks declined from 4,514 to 3,130 and the number of average-size stores from 30,781 to 27,993 (The Nielsen Company, 2011).

The FMCG retail market is in an early growth stage. This is shown by the fragmented character of the market. The top five retailers – Kaufland, Carrefour, Real, Penny Market and Plus – have a cumulated market share of only 22% (Vaschi, 2011). Consequently, there is still room for new entrants.

The ascending evolution of sales and investments in modern trade in Romania as well as the potential opportunities provided to new entrants underline the importance of exploring the characteristics and strategies of the modern trade and their impact upon the companies involved. The major trends analyzed hereinafter are the following: adaptation of buying groups and centrals, setting-up logistic platforms/warehouses and development of relationships between suppliers and large retailers.

2. ADAPTATION OF BUYING GROUPS AND CENTRALS

At present, in the European developed countries, the FMCG retail market reached maturity, fact reflected by the slower market growth and fiercer competition. In the developed markets, many retailers have created buying groups to trade larger volumes at lower prices, in order to maintain their competitiveness.

In essence, a buying group is an organization that acts on behalf of stores that belong to many different retail operators (Varley, 2005). There are buying groups that play a wholesale function at international scale and have offices around the world providing cost economies to retailers. A buying central is a contractual structure that offers services to several affiliates such as retailers, wholesalers and other enterprises (Bernard and Salviac, 2008). The main functions accomplished by a buying central are the study and design of the product portfolio, the identification and negotiation with suppliers, the provision of promotion services to affiliates. The goal of such organizations is to generate cost economies due mainly to economies of scale obtained through consolidated buying.

The local small operators from CEE face ever increasing competition from large international retail chains. They tempted to become members of buying groups such as CBA, Spolem, Coop Jednota, EMD Markant Cz, Coop Hungary etc.

The buying groups have a strong negotiating position in the relationships with suppliers. Their turnover exceeds those achieved individually by the major global players. For example, the members of the Coopernic alliance have a turnover larger than Carrefour (Riverain and Walton,
In addition, five of the top ten European retailers are rather buying groups than individual companies. They buy large quantities at convenient prices. The profitability is significantly higher per SKU compared to that of the individual retailers due to the limited range of traded product categories. Research achieved by IGD revealed supplier skepticism relative to the ability of the buying groups to generate benefits for them (Riverain and Walton, 2011). The reaction of suppliers is strongly negative and consists in granting no price concessions and even in refraining from concluding contracts with buying groups.

On this European background, in Romania, the large international retail chains have modified their strategies relative to the acquisitions of FMCGs and to the buying centrals. One significant example is the German retailer Metro Group. Within the framework of the Shape 2012 program initiated in January 2009, Metro Group Buying (MGB) was dismantled. This change impacted all the Metro subsidiaries around the world, including the subsidiary from Romania. As a consequence, each store format within the Metro Group had to administer its own acquisition department. Thus, in Romania, the negotiations with suppliers were conducted separately by the buying departments of Metro Cash & Carry, division of the Metro Group, and of real-, Hypermarket.

In 2011, the changes in the buying strategy initiated in 2009 still continue. For example, Metro Cash & Carry intends to consolidate the relationships with the small food producers (Ionescu, 2011a). Starting with 2012, the retailer will intensify direct collaboration with the suppliers of ultra-fresh products such as fruits, vegetables, fish and meat, in order to diversify the assortment, to improve quality and prices. This two-stage program aims to establish 13 central buying locations - five locations in the first stage and eight locations in a second stage. Each center will coordinate the acquisition of specific product categories. Metro Cash & Carry considers that contract conclusion will be easier for the small producers, in the absence of intermediaries.

The Metro Group will decide in 2011 if the Real Division of hypermarkets will be sold or will remain within the group (Ionescu, 2011b). Even though the sales achieved by Real have increased in 2010 compared to 2009, the division does not represent an “evolution engine” for the Metro Group. Consequently, Real has concluded a partnership with the German buying group Markant, in order to obtain a cost advantage through the acquisition of larger volumes. The turnover achieved in this partnership will represent approximately Euro 30 billion.

Similarly, the buying central Provera of the French-Belgian retail group Louis Delhaize underwent changes on the Romanian market. The central served the Cora and Profi retail chains. In 2008, the turnover of Provera reached Euro 300 million in Romania (Popescu, 2009). In 2009, the Profi stores were bought by Enterprise Investors. As a result, only the hypermarket chain Cora remained to be served by Provera and to sell the private brand Winny. In 2010, the retail group Louis Delhaize decided to reorganize the buying activities. Until 2009, Provera bought own private brand separately from manufacturer brands. Since 2010, the purchase of national brands and own private brands are under the responsibility of four general directors each in charge of a specific product category: drinks and alcoholic beverages, dairy and frozen products, grocery products and fresh produce. The main advantage for the group is a better perspective of the entire category and of the situation at the shelf level.

While the international retailers reorganize and dismantle their buying structures, the most recently launched chain Mic.ro benefits from the support of a buying central. This central of the Mercadia Group will serve both Mic.ro and Macro. At the same time, several Macro stores will become logistic hubs for Mic.ro. Until the end of 2011, the Mic.ro network of convenience stores will consist of 2,000 outlets and the Macro network will include 100 stores.

The evolution of the buying groups and buying centrals reveals the following aspects: (i) in Romania, the buying structures of the international retail chains are reorganized due to the shifts in the buying strategies set at the group headquarters; (ii) the buying groups and centrals that successfully performed years ago, at present must be adjusted to fit the dynamic market realities; (iii) the reorganization effort aims to provide a better perspective of product categories.
and direct relationships with the small suppliers; (iv) centralized buying structures may still be profitable (fact demonstrated by the new market entrants); (v) major benefits are the negotiation of more convenient prices, the diversification of the assortment and the increase in product quality.

3. THE SET-UP OF LOGISTIC PLATFORMS

Most international key accounts – such as Metro, Rewe, Kaufland, Profi, Mega Image, Minimax – have invested in distribution platforms in order to facilitate the deliveries from suppliers and the deliveries to own retail stores. Metro Cash & Carry intends to channel all the deliveries from suppliers through the logistic platform, until the end of 2011.

An example of international key account that invested substantially in distribution centers in Romania is Carrefour. In 2007, Carrefour rented sq.m. 45,000 (out of which refrigerated space for fresh products sq.m. 4,000) in the Cefin Logistic Park which is part of the Europolis network of distribution centers. The value of the five-year contract was Euro 15 million. The distribution center of Carrefour is operated by the logistic firm Norbert Dentressangle. In 2009, Carrefour added a new distribution center. This center is located in Bacia (Hunedoara county) within the Transylvania Logistic Center. The rented surface amounts to sq.m. 20,000 out of which sq.m. 2,450 for fruits and vegetables. The platform facilitates deliveries to the Carrefour hypermarkets and supermarkets from Transylvania, Banat and Oltenia. The logistic partner of Carrefour is the international operator DHL Delamode Romania.

Another example is the supermarket chain Mega Image which is part of the Delhaize Group. In 2010, the retail sales of Mega Image reached one billion Euros. In the same year, the company launched “Romanian tastes” - its first private brand exclusively dedicated to Romanian products. Mega Image has invested Euro 35 million to build a new sq.m. 45,000 logistic center at Popești Leordeni. The deliveries from suppliers will be channeled through the platform between June and October 2011 (Ionescu, 2011 c).

For suppliers, the main advantages of the direct deliveries to platforms are the following: (i) lower costs compared to the situation when deliveries are made to each store of the retail chain; (ii) national expansion without own fixed investments; (iii) better storage conditions compared to the usual warehouses; (iv) existence of backup inventory and the low occurrence of out-of-stock situations etc. For the retailer chain, the major advantages are: (i) more efficient inventory management; (ii) lower labor costs due to the decrease in the reception personnel; (iii) the possibility that stores order a minimal quantity (such as a single pallet).

In practice, platforms also have several drawbacks from the suppliers’ perspective (Nicolae and Illoviceanu, 2011). Among these limitations range the following: (i) the difficulties met in transport optimization due to the deduction of quantities delivered to the distribution center; (ii) the lack of direct information about the market in the absence of contacts with the retail outlet personnel; (iii) risk of out-of-stocks at store level due to the low visibility of sales; (iv) significant variability in the size of weekly orders (for example from 4% to 500%); (v) long time intervals for unloading the transportation vehicles; (vi) late deliveries to stores because the orders are placed late by the outlets; (vii) long itineraries of the orders placed by stores; (viii) ever smaller order volumes due to the addition of new platforms by retail chains; (ix) high value of the tax to be paid by suppliers for the deliveries to the platforms.

Several recommendations may be underlined based on the experience acquired by the suppliers on the Romanian market. An in-depth perspective of the sales at the store level and of the inventories existing on the logistic platform may better protect suppliers from the bullwhip effect that appears due to the information disruption within the communication channel between supplier and final customer. At the same time, a platform setting a tax based on costs that are competitive compared to those of third-party logistic providers will attract suppliers to a higher extent than the present practices of charging an average percentage of the platform costs.
4. RELATIONSHIPS BETWEEN SUPPLIERS AND LARGE INTERNATIONAL RETAILERS

The relationships between suppliers and the modern international retailers are multi-faceted. Conflicts intermingle with intentions of cooperation.

On one side, the fresh produce market witnessed a deep conflict between the international retail chains and the Romanian producers during recent years. Based on the strong negotiation power, the international key accounts have set difficult terms in the contracts with these producers. From the tax for shelf space and entry in one or more stores to the tax for store refurbishment or promotional catalogs, suppliers had to pay substantial amounts of money. Thus, the modern trade has a dual character being both the access “portal” to the mass market and a cost challenge for the Romanian less powerful producers.

On the other side, the FMCG retail market in Romania is marked by several cooperation projects between suppliers and modern retailers. For example, Carrefour succeeded in establishing three distinct quality networks. In 2008, the first quality network was created for pork meat, together with the company Marex from Brăila. In 2010, a quality network for fresh fish with Romavet and one for carrots with Big Land Company were implemented. In the near future, potatoes and apples will be the focus of distinct quality networks. The products are 100% Romanian, the producers comply with clear requirements and the quality is periodically controlled by an independent and accredited body. These cooperation projects allow the traceability for the specific food products. All products sold under the logo comply with the quality and food security requirements. The logo is also a warranty that no genetically modified organisms or other unhealthy ingredients are included in the products.

Another example of cooperation program is the one developed by real-, Hypermarket. The company initiated - in partnership with local authorities from Oradea - the program “Produceţi româneşte, vindem româneşte” aimed at informing and supporting the local producers in order to sell traditional Romanian products through the real-, Hypermarket chain.

CONCLUSIONS

The buying of fast moving consumer goods by the modern retail trade in Romania is marked by significant shifts. The changes are generated by both external factors and the specific features of the local market.

Firstly, the organizational structures of the international key accounts involved in FMCG buying undergo many changes initiated in the countries of origin. The buying groups and centrals have to adapt to the local market evolution. Secondly, the logistic infrastructures acquire an increasing importance. The distribution centers / platforms facilitate the flow of goods towards the final consumers. However, they are not spared of limitations. Thirdly, the relationships within the supply chain are multi-faceted and have a dual character generated by a mixture between conflict and cooperation. Nevertheless, the international key accounts set the rules of the game for less powerful local producers from Romania.

The development of real partnerships among the members of the supply chains may enhance both the profitability of Romanian producers and of the international modern retailers. Finally, such partnerships will favorably impact the value created and delivered to consumers and may ultimately foster their loyalty.

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MULTINATIONAL CORPORATIONS AND RISK MITIGATION IN TODAY’S GLOBAL ECONOMY

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Abstract: Today’s global economy has led to the expansion of the activity of multinational corporations in areas that include a vast economic potential for business development but also to tremendous geopolitical uncertainties. Understanding the geopolitical tendencies as well as the social changes and their associated risks are priorities of the international business environment. A new approach is required to evaluate the exposure to several risk areas and to develop associated strategies. In order to maintain the role of a global player, a corporation must not only survive the economic crises, but also the geopolitical impacts.

Keywords: multinational corporations, risks, geopolitics

INTRODUCTION

Multinational corporations are present in at least 65 high-risk classified countries and investments of more than EUR 100 billions are recorded in almost 50 states classified with a high level of corruption, based on the Corruption Perception Index, according to Transparency International. Although the international economy is falling since 2008 and continues this tendency over the last years, direct foreign investments in the emerging markets grew, while showing a decrease in developed countries, in accordance with the UN World Investment Report 2009: Transnational Corporations, Agricultural Production and Development.

The markets’ maturity forced the companies to expand beyond the boundaries of the developed world, with stable economies, in areas of much higher risks than to what they are accustomed. We have areas which represent a vast economic potential for economic development but also tremendous political uncertainties, including areas with major conflicts, which are not at all insignificant, from the Middle East up to Central Asia, India and Asia.

From the point of view of their capacity to actively mitigate risks, corporations have a high-level of exposure. The corporate environment seeks to apply new patterns and instruments for the understanding of geopolitical and political tendencies, as well as of social changes and associated risks for the international business environment. After the terrorist attacks on September 11th 2001 in New York, commercial strategy included the geopolitical insecurity as a new component of the corporate decision making process.

THE NEW CONTEXT OF THE GLOBAL ECONOMY

Economic globalization has forced political leaders to adjust the harshness of a continuous market and the international Memoranda and Treaties concluded within the last years have confirmed the desire to maintain an open global market, despite the existing economic crisis. The G-20 Summit in Washington D.C. on Financial Markets and the World Economy, on
November 2008, confirmed the political will for a free world economy. Their declaration stated that “within the next 12 months, we will refrain from raising new barriers to investment or to trade in goods and services, imposing new export restrictions, or implementing measures to stimulate exports.” This commitment was reaffirmed at the G-20 Summit in London, held on 2 April 2009, where leaders committed to “minimize any negative impact on trade and investment of our domestic policy actions including fiscal policy and action in support of the financial sector.” They further pledged: “We will not retreat into financial protectionism, particularly [through] measures that constrain worldwide capital flows, especially to developing countries.”

The rhythm of international political events forced the corporation management to adapt in order to confront the consequences of connections between geopolitics and performances in the business environment. A first step was made in 1990, when the collapse of communism lead to the abrogation of the borders of many national economies and opened a new development stage for multinational corporations, followed by a less certain era of geopolitical changes, requiring profound evaluations of geopolitical risks, essential for a continuous business success.

Today, people talk about an extremely fluid, unsecure and unpredictable world after September 11th. In this context, geopolitical risk has a clear importance for the business environment: it is about the risk potential of an international political conflict to threaten the financial and operational stability of companies worldwide. In order to develop a mechanism for risk decrease, the management of multinational corporations must understand the specific nature of the relationship between corporate globalization and geopolitics, it must identify locations with risk potential for corporations and their activities and adopt forecasting instruments which can consolidate their business, from the point of view of threats associated to conflicts and terrorism. In this process, measures taken by the management of multinational corporations are crucial.

The end of the Cold War encountered an enormous expansion of international business, since corporations have been given the opportunity to expand on economies in transition and on emerging markets. In the ’90s, it was thought that free markets and a liberalist economic program can generate more stable geopolitical relationships. The decrease of conflict level between states during this period delivered a geopolitical context, too, which allowed for a powerful consolidation of industries along with the international expansion of corporations. The global economy gained a special status; corporations encountered almost no political and social constraints at all. But, the expanded international presence of trade companies and the complexity evolution of the geopolitical context have increased exposure to conflicts and violence. Multinational corporations became obvious targets of attacks and their vulnerability increased since strategies were based on the assumption of fundamental stable geopolitical relationships.

In this context, the term global player gains a new significance: if prior reference was exclusively made to an economic player, this describes now a company which became a political player too. In order to maintain the global player role, a company must be able to survive not only the economic crises, but also the associated geopolitical impacts.

GLOBALIZATION AND NEW RISKS

Globalization implies a series of concrete rationales such as the quality of governments, mainly of governments of developing countries which adapted slowly to the efficiency requirements for the enhancement of the presence of the companies. Therefore, traditional political risks, such as corruption and expropriation are still applicable. Further, reference is made to the existence of some important factors beyond the governing authorities. The growth of economic and political activities beyond the governments’ control or without its knowledge is translated as an increase of the vulnerability within the globalization networks.

Based on the Quadrennial Defense Review Globalization Report issued by US Department of Defense in February 2010 “Globalization has transformed the process of technological
innovation while lowering entry barriers for a wider range of actors to acquire advanced technologies. As technological innovation and global information flows accelerate, non-state actors will continue to gain influence and capabilities that, during the past century, remained largely the purview of states.”

Advanced technology has represented a huge advantage for businesses, but also has brought with it risks. Technologies facilitating international corporate activity also allow illicit interactions and the sudden occurrence of threats. Corporations are therefore being forced to seek solutions for the consolidation of systems and structures against a specific threat such as cyber attacks. And based on the Eurasia Group - Top Risks 2011 Report there is a political impact behind this risk: “The growing and high-stakes conflict between government supported economics entities and multinational corporations are provided serious home court advantage for state capitalists (cyber attacks for profit). China is by far the biggest concern here, and combined with Beijing-supported ingenuous innovation, this probably is the most important line of conflict between states and corporations globally”

The most significant risks are related to manufacturing capacity, communications and usage of information, essential for a country’s national security from several points of view, from the electronic government to the evaluation of information conflicts and the control of transnational crime organizations. Since platforms and infrastructure of business and crime overlap, risks regarding security are always present and corporations can therefore be negatively affected by the expansion of technological know-how.

First Annual Cost of Cyber Crime Study conducted by Ponemon Institute and released in 2010, entailed seven months of research and visits to each of 45 organizations. The participating midsize and large organizations (from 500 to more than 105,000 employees) represent a mix of industries and government agencies. Researchers talked to IT security personnel, as well as network, forensics, and management staff, to determine the costs of responding to and mitigating cybercrime attacks. The $3.8 million annual cybercrime tally represents an average; organizations reported from a low of $1 million to a high of $52 million per year, according to the study. The $3.8 million average cost represents not what companies or governments might routinely spend each year on say, antivirus software, but the direct cost of coping with the attacks. Types of cybercrime reported include: stealing intellectual property, confiscating online bank accounts, distributing viruses and other malware, posting confidential business information on the Internet, and disrupting a company’s infrastructure. Ponemon representatives say those organizations that had invested in defensive technologies, including security information event management, and had a chief information security officer on board, appeared to be better prepared to respond and took less time to remediate problems. But they add that only about 40% could be considered to have invested in this way.

Other threats address the transportation and international trade fields. Global dependency on key transportation systems (by sea, air or land) increases constantly, and disruptions of the supply chain mostly affects multinational corporations. These threats have major implications on the increase of business insurance costs, leading to the increase of security measures applied to companies of all sizes. An example is the situation in the Aden Gulf, one of the most frequently used naval routes, as ships prefer to cross the Indian Ocean area towards Suez Channel, especially since the second option is to bypass the Cape of Good Hope, a much lengthier and more expensive alternative. The cost of a kidnapping and ransom policy increased by 15 times over the past 5 years, which affects naval transporters whose ships cross the Aden Gulf, an area with significant exposure to piracy, according to a report drafted by AON Risk Services. Approximately 70% of the transporters have such policies, especially for situations similar to the one in the Aden Gulf, especially since there are further “hot” areas on the globe such as the Gulf of Guinea in the immediate vicinity of Nigeria and Malaccan Bay in Indonesia.

Thus, a new approach is required for a detailed understanding and approach to risks. Such a framework must evaluate the exposure to several risk areas and should develop related
strategies. These risks are related to the presence on emerging and unstable markets. These are the traditional areas with political risk, which include the threat of war, terrorism or organized crime. Another risk area is related to the supply and transportation chain. Such risk is associated with the disruption and blockage within unsecure trans-border operational relations. The volatility of this market is a characteristic of today’s economy and geopolitical conflicts have a strong impact on the market’s evolution. With regards to capital risk, it is influenced by political impacts that may cause the sudden loss of the investment flow in an industry branch. The know-how and the intellectual capital can be compromised by risks associated with erroneous information, incorrect communication and cybernetic security.

The presence of such risks may persuade companies to acquire insurance policies. However, insurance does not represent a general solution. Although insurance policies are important mechanisms for the mitigation of risk real costs, the vast nature of risks requires the companies to gather a better understanding of the perspective of geopolitical risk for operation and market insurance purposes.

ASSESSING POLITICAL RISK IN THE GLOBAL ECONOMY

![Image of Global Political Risk Index (GPRl) - Eurasia Group’s report January 2010](image)

The integration of political variables into strategic planning is not an easy task; there are no capacities for a perfect pattern that may predict the cycles of an interdependent economy, much less a global economy overshadowed by geopolitical risk. While traditional risk analysis is focusing on geography, risk today surpasses geographical constrains. Risks associated with the distribution of powerful and potential lethal technologies that represent the origin of today’s numerous commercial risks. Thus, the transnational nature of businesses and risk means that
the geopolitical analysis must take into consideration local, national, regional and international dimensions. Companies use more and more planning techniques for scenarios and services in order to develop in advance responses to unpredictable events and circumstances. In an extremely unsecure era, planning scenarios means that companies must be ready for all possible results and the implementation of flexible strategies throughout the entire future risk and situations spectrum will be possible.

Planning and forecasting scenarios are essential not only for the prediction and confrontation of risks, but only for gathering data and information pertaining to geopolitical tendencies. Within industries, corporations have the mutual interest to understand these tendencies in order to ensure a stable market environment. Usually, corporations do not dispose of proper dependencies. Within industries, corporations have the mutual interest to understand these tendencies for gathering data and information pertaining to geopolitical tendencies a company needs and the available information that it can collect and use.

However, there are examples of risk analysis instruments that are offering early warnings with regard to critical tendencies and a possibility to measure a country’s capacity to face the political, economic, security and social impacts, such as, for instance, The Global Political Risk Index (GPRI). GPRI is a composite of 20 indicators measuring a country’s vulnerability to crises on a scale of 0-100. Higher figures indicate greater stability. Developed by Eurasia Group’s experts in domestic and transitional politics and economics, the GPRI provides an early warning system intended to anticipate critical trends and provide a measure for the capacity of a country’s political regime to withstand political, social, security, and economic shocks. The GPRI was previously identified as the Deutsche Bank Eurasia Group Stability Index (DESIX) and Lehman Brothers
LEGSI index. Clear and concise analysis accompanies the index to illustrate what events impacted each country’s stability rating and make forecasts for the coming month. The GPRI is calculated on a monthly schedule to allow for considered, rather than reactive, analysis on important developments in emerging markets. It places everyday occurrences into a larger context of comparative state stability.

Figure 1 shows the countries having the Global Political Risk Index (GPRI) lower than 80 for January 2010. Highly stable countries (those with an index number at, or higher than, 80) possess all or most of the following characteristics: efficient state institutions, government effectiveness (high degree of political institutionalization), high degree of political legitimacy among the population, sound economic performance and policies, absence of significant anti-state opposition, rare instances of political violence, low level of social, ethnic, or religious tensions and infrequent occurrence of humanitarian emergencies and capacity to mitigate natural disasters. Under the circumstances, the accurate assessment and positioning of the country risk is essential for a company’s decision-making system.

EFFECTIVE MANAGEMENT OF POLITICAL RISKS

Completed in 2010, MIGA (World Bank Group) - EIU Political Risk Survey of 60 multinational enterprises’ executives assessed how political risks feature among the factors that constrain investment plans and how these risks are being mitigated. Based on this survey, types of political risk of most concern to investors when investing in developing countries are:

- Breach of contract by a host government,
- Regulatory changes,
- Transfer and convertibility restrictions,
- Non-honoring of sovereign guarantees/ debt default,
- Civil disturbance,
- Expropriation,
- Terrorism and War.

The survey spots that the risks arising from government intervention (breach of contract and adverse regulatory changes) weigh more heavily on these decisions than on those associated with political violence (Figure 2).

On the other hand the occurrence of losses itself appears to have a moderate impact on risk perception. Most respondents do not consider political risks to be very high in their host
countries, although some of them have experienced losses caused by political risks in one or more of their investment destinations over the past three years. These losses were mostly due to breach of contract and adverse regulatory changes (Figure 3).

Based on EIU Political Risk Survey the majority (95 percent) of investors surveyed for this report actively manage political risk (Figure 4).

Risk mitigation includes:

- Non-contractual mitigation strategies like engagement with local governments, communities, and nongovernmental organizations as well as joint ventures with local enterprises and operational hedging (e.g., setting up multiple plants to spread risk);
- Contractual risk-mitigation tools such as political risk insurance and credit default swaps.

In order to mitigate these risks, the majority of investors prefer non-contractual strategies. Engagement with local governments such as maintaining an open dialogue and good relationships and joint ventures with local enterprises were seen as the most effective tools to mitigate the risks of adverse government interventions. Some 63 percent of respondents evaluate and monitor the level of political risk in their investment destinations through internal risk analysis or risk analysis performed by external consultants. Only 32 percent of the respondents currently use contractual risk-mitigation tools, including political risk insurance and credit default swaps (21 percent).

The proportion of investors who considered that there was no effective mitigation tool against political violence was also significantly higher than for any other risk but they consider as important the monitoring and the use of the risk analyzing tools for these kind of risks. An important portion of the companies use political risk insurance as an effective risk mitigation tool. The non-contractual mitigation strategies as engagement with the local public entities and establishing joint ventures are the most effective for risks mitigation in majority of the cases (Figure 5).

Risk evaluation should become a priority for the management of multinational corporations, which must adapt now to the rhythm of changes within the business environment and to acquire a geopolitical overview. Management should routinely identify and evaluate the risk to achievement of business objectives. This would include the regular assessment of the significance and the likelihood of possible risks to arise and a prioritization program should be established. Higher priority items are those risks judged to be both significant and having a high likelihood of occurrence - those which might have a real impact on the company and which need a strategic rethinking, such as market failures and political impacts. These risks are judged to be prime threats to the management and should be addressed at their source. Those risks judged to be significant but with a lower level of likelihood should be detected as early as possible and monitored on a regular basis. Those risks judged to be insignificant, but with a high likelihood of occurrence should also be monitored closely. Risks judged to be insignificant with a low level of occurrence would likely not demand close attention.

Being aware of risk scenarios must not be restrained to a global approach and to similar solutions, but it shall take into account local, national and regional characteristics. Analyzing the geopolitical factors we reach the conclusion that there are no risk patterns and corporate management should consider personalized solutions which take into consideration the main relevant elements for the risk factor analysis applied to the local conditions. If scenarios and associated risk forecasts are correspondingly understood, major advantages for the development of business may result.

Rather than strategies of reaction to threats, there are active strategies based on the idea that companies are political actors. As a matter of fact, the private sector, by setting market standards, has a considerable impact on the political and decision-making process. This means that corporate activities do affect the shareholders as well as the actors on the political scene because of their impact on different interests in public areas, such as labor force, environment or intellectual property rights. Even without being directly politically involved, companies can encourage the governments’ actions to prevent conflicts or can contribute with resources to the
efforts for re-building economies affected by conflicts, in order to ensure their functioning. Ultimately, government and corporate interests converge for setting up a proper economic environment for business development.

CONCLUSION

Corporations recognize that the effective management of business risk is critical to the success of business. Management should routinely identify and evaluate the risk to achieve business objectives. This would include the regular assessment of both the significance and the likelihood of occurrence of the risks arising. Corporations would seek to resolve important risks by mitigating, avoiding or accepting the risk. Mitigating includes various types of insurances, hedging, and other techniques. Avoiding a risk means conducting business in such a way so as to bypass the risk either partially or completely. Otherwise, some business risks must be accepted as a cost of doing business.

Risk management has to be embedded in all management systems and business processes and should be an integral part of the Company’s internal control processes. As part of the process the identification and the management of risk has to include all managers and staff throughout the company. A key objective of risk management is the development of a comprehensive risk management framework to ensure that risks are being managed in an efficient, effective, and economic manner. The framework will include risk management standards and risk assessment criteria.

Risk evaluation becomes a priority for the management of multinational corporations, which must adapt to the rhythm of the business environment changes and must have an overview on the geopolitical situation. If scenarios and associated risk perspectives are understood adequately, major advantages in business performance may rise.

The maturity of markets has forced companies to expand beyond the boundaries of developed countries with stable economies, into areas with much higher risks than they were used to deal with.

Globalization, along with opportunities, brings along difficult challenges. In periods of economic turmoil, there’s a greater likelihood of political and economic discontent, which amplifies political risks. With growing political instability and the expanding political risk universe, it is important for organizations to perform thorough country-risk assessments while expanding their operations and protecting their existing global operations.

From an operational point of view, political stability at regional, national and local level contributes in a decisive manner to investment decisions. The risk level is mainly determined by the economic and political environment developments in the host country. Under the circumstances, the development of the country risk assessment methodology will be based, through a complex indicators system, on the analysis of economic and political components in a very strong correlation. Another issue arises due to the frequent political or economic changes. In this context it was noted that not all economic or political standing deteriorations in the host country are immediately reflected onto the country risk.

Political variables must be integrated into the strategic planning. The transnational characteristic of businesses, as well as the one of risks, means that the geopolitical analysis must include local, regional and international dimensions. Instruments for the analysis of risks do exist, offering warnings referring to critical tendencies and offering a possibility to measure the country’s capacity to face political, economic, security and social impacts.

The majority of corporations actively manage political risk. Risk mitigation includes different strategies adapted for local cases to a global approach and they take into account local, national and regional characteristics. Corporations use a wide range of risk-mitigation techniques to manage political risks. Risk management includes assessing the level of risk through internal analysis and the use of external consultants and implement mitigation strategies that can be non-contractual strategies like engagement with local governments, communities, and non-governmental organizations as well as joint ventures with local enterprises and contractual risk-mitigation tools such as insurance policies and credit default swaps. Also, active strategies do exist, based on the idea that companies are political and social actors setting market standards.
with a considerable impact on the political decision-making process.

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BEST PRACTICES IN LEADING POST-MERGER BUSINESS INTEGRATION

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Abstract: Mergers and acquisitions (M&A) have been an essential element in the arsenal of corporate strategies for growth and optimization of shareholder wealth for centuries. In addition, in a global economic downturn – particularly of the breadth and depth that has characterized the start of the 21st century – corporations have shown a consistent tendency to mostly adopt defensive strategies of cost management, preservation of market share, and protection of asset liquidity. The juxtaposition of these two dominant trends is the fuel for a common post-downturn phenomenon: a surge in M&A activity. Companies with excessive cash and a thirst for restoring growth seek to capitalize on the many diverse opportunities created by a renewed global economy, one that is often fully re-structured with different customer dynamics, business models, and competition profiles. Given the additional backdrop of numerous recent studies over the last few decades which have concluded that most business combinations actually fail to deliver the results expected, this paper examines “lessons learned” from past M&A implementation in general and outlines best leadership practices for optimizing the outcomes of a strategic business combination in a post-recession 21st century global marketplace.

Keywords: mergers, acquisitions, post-merger best practices, leadership

JEL Codes: G34, L19, M14, M19

INTRODUCTION

In his article “Not all M&As Are Alike – and That Matters” (Harvard Business Review, March 2001), Joseph L. Bower identifies five reasons why companies engage in combining their business operations:

- Consolidation, usually in response to an over-capacitated or otherwise mature industry/market segment.
- "Roll-up" of competitors in a geographically fragmented industry.
- Launch of new products or entry into new markets (buy vs. make).
- As a substitute for R&D investment / risk.
- "Industry convergence:" Exploitation of eroding industry boundaries to create new ones.
This taxonomy, and many others like it, point to a well-accepted reality: the drivers for mergers and acquisitions (M&A) are universal, transcending all business sectors, geographies, business size, etc. And, by their very nature, they have persisted in both the best and worst of times.

Business conditions associated with prolonged global recessions – as experienced in an unprecedented way in the last few years – have proven to create an even greater focus on M&A as a targeted strategy for growth and wealth creation for equity owners. On the one hand, the M&A is quite literally the path to recession survival for some businesses which elect to pursue economies of scale by joining forces with competitors or diversifying their target markets in areas aligned with their core competencies. But, in a more subtle way, recessions invite a plethora of defensive tactics that ironically result in cash accumulation – the institutional version of “saving for a rainy day.” The result of this latter phenomenon is a spike in M&A activity in post-recession recovering global economy driven by the confluence of buyers with cash and sellers with lower than usual valuations.

Leaders understandably are in the forefront of deciding what M&A opportunities exist in their recovering competitive landscape. But, to truly optimize shareholder wealth creation in this environment, a focus on the implementation of business combinations has never been more important, particularly in a 21st century customer/consumer climate dominated by unprecedented choice, low incidence of customer loyalty, radical shifts in long-standing business models, etc. The global business “graveyard” is littered with well-conceived business combinations poorly implemented.

This paper will outline what researchers of post-merger M&A activity have learned about what can dilute the attainment of transaction objectives associated with business combinations, and what best practices have emerged to mitigate the causal factors behind this dilution.

THE POST-MERGER INTEGRATION SCORECARD

Failure to Perform

Post-merger integration results are universally recognized as less than what was intended or expected. This malady has plagued the post-merger landscape ever since the topic has been studied. Following are a sample of some of the findings cited from studies conducted as far back as 1997:

• “In a recent 10-year study of 340 major acquisitions, Mercer Management Consulting, Inc. found that total shareholder returns for 57% of the merged concerns lagged behind their industry averages three years after the transactions.” [Wall St. Journal, February 14, 1997]

• “Studies by McKinsey & Company and Coopers & Lybrand LLP report that 70% of all strategic alliances fail or fall short of expectations. The American Management Association reports that only about 15% of mergers and acquisitions achieve their financial objectives, as measured by share value, return on investment, and profitability.” [HR Magazine, April 1997]

• “An exhaustive analysis of hundreds of deals made in the first half of the 1990s led Business Week to conclude that... of 150 deals valued at $500 million each or more, about half actually destroyed shareholder value.” [Five Frogs on a Log, Mark L. Feldman & Michael F. Spratt, 1999]

• According to a study of 34 companies active in mergers, “... more mergers fail due to inadequacies in post-merger integration rather than to any fundamental failure of strategic concept.” [Booz-Allen & Hamilton, 1999]

• “While target firm shareholders generally enjoy positive short-term returns, investors in bidding firms frequently experience share price underperformance in the months following acquisition, with negligible overall wealth gains for portfolio holders
Internally, managers of acquiring firms report that only 56% of their acquisitions can be considered successful against the original objectives set for them (Schoenberg, in press). Meanwhile, target firm executives experience considerable acculturative stress and, on average, almost 70% depart in the five years following completion (Krug and Aguilera, 2005). “[“30 Years of Mergers and Acquisitions Research: Recent Advances and Future Opportunities,” Susan Cartwright & Richard Schoenberg, British Journal of Management, 2006]

• In 2007, The Hay Group and La Sorbonne conducted interviews with 200 senior European business leaders who have experienced a major merger or acquisition in the past three years. In their report, they concluded that “… only nine percent of European business leaders considered their deal to have achieved its original objective.” [The Hay Group, 2007]

In 2000, Johnson & Johnson (J&J), a 125-year-old global company which has been active on the M&A stage for many years, conducted a major study of M&A activity under the auspices of its Ortho McNeil Division. As reported by Rutgers University researchers Schuler & Jackson (“HR Issues and Activities in Mergers and Acquisitions,” Randall Schuler & Susan Jackson, European Management Journal, 2001), the J&J study found that, “when poor integration occurs,

• Productivity drops 50%;
• Leadership attrition soars 47% within three years;
• Employee satisfaction drops 14%
• High-tech mergers fail to deliver desired results at the rate of 90%;
• Employees report that they feel management cares more about financials than product quality or people at the rate of 80%.”

Of course, there are many factors that have contributed to the above dismal reports and analyses, including some very basic missteps such as poor or hasty due diligence regarding the financial integrity of the acquired entity, paying the wrong price for the acquired enterprise, and simply bad timing. However, when the causal factors are examined, the culprit is rarely the financial or strategic integrity of the transaction, but rather a myriad of factors related to the manner in which human capital is managed before and after the transaction is consummated. To quote Cartwright and Schoenberg (British Journal of Management, 2006), “An emergent and growing field of enquiry has been directed at the cultural dynamics of M&As and the emotional and behavioural response of the employees involved. This literature, with its diverse origins in the psychology, organizational behavior, and human resources management disciplines, has sought to explain M&A underperformance in terms of the cumulative dysfunctional impact of the event itself, its associated uncertainty, and the subsequent process of integration have on individual organizational members.”

Because implementation has been so often identified as the stage during which unmet expectations and, in some cases, broken promises (to stakeholders) are most visible, much has been written about a) the critical success factors for successful M&A-related implementation; and, as a counterpoint, b) the reasons why M&A-related implementation processes do not produce desired result. Focusing on the latter, we examined findings and conclusions from various sources and compiled the following list of the ten most cited reasons for implementation failures:

• Exclusion of workplace “culture” in the due diligence phase of the transaction.
• Ineffective and poorly timed communication with all stakeholders.
• Poorly conceived and/or executed tactics for retention of key employees.
• Private agendas of controlling executives or stakeholders (vs. “strategic integrity”).
• Weak and/or hastily executed planning.
• Management denial of the potential negative impact on all employees.
• Inattention to the loss of employee productivity throughout the process.
• Over-zealous attention to internal issues (vs. to customers and competitors).
• Visible lack of alignment of the post-transaction senior management team.
• Lack of clear ownership of the success of the integration process.

As mentioned earlier, there are indeed many other factors associated with individual cases. For example, some combining organizations grossly underestimate the cost of post-transaction activities required to effect a merger, and find themselves having to reverse the process to maintain viability. Some combinations yield revenue and customer losses (for the combined organization) at levels that were never anticipated; the combining organizations simply overestimate the loyalty of their key customers after-the-fact. A specific example of this was the history of mergers of the so-called “Big 8” accounting firms in the 1980s and 1990s. During the transition to four global leaders today, several of these surviving firms experienced significant losses of client organizations that simply opted to switch to a “second tier” firm now more similar to the pre-merger entity with which they had a long relationship.

Despite the fact that the long history of M&A activity throughout the world has produced sub-optimal results, in many different ways, there appears to be strong consensus that the most debilitating issues are related to people – choices and actions related to who stays, who goes, who is given more or less responsibility, how individual job responsibilities change, how employee compensation and incentive-related processes change, etc. Even the negative effects of customer or market share churn prompted by M&A activity are most often mitigated by the people who remain during the implementation phase and their collective motivation to engineer a successful merger.

**Driving M&A Implementation Success**

Of course, there are always examples of M&A activity where the business objectives on which the activity is predicated are met or exceeded. In the research report mentioned earlier, Schuler & Jackson comment on M&A successes: “Perhaps not surprisingly, some of the major reasons for success in mergers and acquisitions include:

• (Effective) leadership;
• Well-thought-out goals and objectives;
• Due diligence in both hard and soft issues;
• Well-managed M&A teams;
• Successful learning from previous experiences;
• Planning for the combination and solidification steps completed early;
• Key talent retained; and
• Extensive and timely communications to all stakeholders.”

The researchers go on to point out how these actions corroborate with other studies of M&A success, including numerous studies by the global consulting firm Watson Wyatt, who they cite as advocating 1) almost always allocating more time for due diligence than originally expected; 2) starting the integration process as soon as possible and getting HR involved early; 3) working diligently on alignment of post-merger expectations of both parties; 4) confronting difficult human resources issues early in the process; and 5) changing integration managers quickly if they fail to adapt.

As with the diagnoses of failure, successes have also been studied extensively, and the overwhelming theme in these studies is that the critical factors embodied in the success stories are – like with failures – almost all related to “people issues.” Reinforcing this conclusion, the well-respected consulting firm Towers Watson has consistently tracked the effectiveness of M&A for many years in order to help their clients better understand what is needed to assure post-merger success. In their most recent study released in 2010 ("M&A Culture and Integration Issues," Towers Watson, 2010), they surveyed more than 400 business and HR executives in 2009 and concluded:
Companies that judged their merger deals as successful focused more heavily and more effectively on change management and communication, in addition to other traditional people issues.

These same organizations are also more apt to emphasize strategic people management – e.g., influencing leader behavior – during the deal.

Successful organizations are more likely than their peers to measure key people elements of the deal.

Many other sources of post-merger analyses and surveys support the notion that best practices for post-merger integration of well-conceived business combinations must give priority attention to the management of the human assets that all parties bring to the table. To quote McKenzie and Salvador ("The Case for Cultural Renewal," An Issue Paper from Right Management Consultants, 1999), “Tasked with the complexity of fostering growth, controlling costs, enhancing stakeholder value, and delighting customers, it is easy for executives to lose sight of the first link in their company’s value chain – their organization’s workforce. After all, it is people who make a business operational, who truly serve customers, who bring the organization to life. Employees who are committed to the company’s success are an enormous strategic asset, one not always fully utilized.”

**LINKING POST-MERGER IMPLEMENTATION SUCCESS TO HUMAN CAPITAL**

As already noted, M&A activity is expected to rise dramatically in a post-recession global economy, particularly given the breadth and depth of the recent financial challenges with have affected virtually all elements of commerce, government, and philanthropy worldwide. In addition, recent research into the persistent failures of M&A strategies and tactics to produce the level of synergy anticipated continues to put ineffective management of human capital issues at the center of the causal factor landscape. More than ever, leaders should take note of the power of attentiveness to best practices directed squarely at the workforces who are expected to deliver the results on which the M&A activity is predicated.

In examining the research on best practices, five practices tend to dominate the many “lessons learned” findings, conclusions, and recommendations.

1. **Incorporate organizational and workplace culture into the due diligence process.**

The global business community has grown accustomed to measuring their performance and competitiveness using a host of metrics, both financial and non-financial. There is no debate that most of these well-accepted metrics, e.g., profit, balance sheet ratios, market share, customer retention, etc., are indeed leading indicators of goal attainment and stockholder wealth creation. However, the field of organizational effectiveness – mostly unmeasured except for the broad categories of employee satisfaction, productivity, and turnover – is largely ignored in the realm of performance measurement or monitoring.

Organizational effectiveness is an elusive thing to measure, and yet many leaders of organizations often point to their workplace culture as a competitive plus. It is not our purpose here to posture what the term culture, in this context, actually means, but it is clear from most of the research on the subject of M&A effectiveness (to deliver results), culture clash is frequently pointed out to be a dominant spoiler. Some of the more frequently mentioned cases of this include Daimler & Chrysler, Disney & Pixar, and Time Warner & AOL. The expectations of employees in these former independent companies as to how they would be treated after the merger transaction was consummated were simply not met, even in the case of the company which is essentially the pseudo-acquirer.

In making organizational culture an integral part of the due diligence process, leaders should:

- Insist that a discussion on similarities and differences in organizational culture takes
place at the earliest phases of merger exploration and throughout the ensuing processes.
• Take ownership of identifying differences (in organizational culture) and orchestrating a process for rectifying or minimizing these differences.
• Include organizational culture issues in all employee communications.
• Put systems/processes in place to monitor post-merger change initiatives that impact post-merger organizational culture.

2. **Determine degree of integration appropriate to realize desired business objectives**

The decision to acquire another organization is typically initiated for one of five major reasons or drivers previously identified earlier in this paper. Each of the five major drivers implies post merger strategies necessary to realize the desired benefits of the deal. For example, consolidation indicates a goal to improve current performance. With this goal, reducing costs in targeted areas such as redundant back office operations, overlapping product lines or excess locations is the primary focus of the post merger integration. Delta Air Lines’ acquisition of Northwest, for example, resulted in several hub locations being eliminated, along with staff and equipment.

Some acquisitions return the most value when they are largely left to operate independent of the acquirer. Disney acquired Pixar in order to acquire creative product, the equivalent of R&D in many businesses. Disney understood the significant cultural and organizational differences between itself and Pixar and determined that integration of Pixar would risk the loss of the very talent it sought to acquire.

In determining the appropriate degree of post merger integration, leaders should:
• Assess the full “costs” of integration and what resources, processes, customer value propositions or financial models, if any, need to be integrated in order to optimize deal value.
• Consider the risks of integrating more elements of the combined businesses than is necessary to optimize deal value.
• Determine which post integration model is appropriate to the situation as quickly as possible. Speed is a critical element of integration success. Not quickly identifying a PMI high level strategy will affect all subsequent decision making. Any actions or communications made without such a clear strategy risk being premature or ineffective and therefore detrimental to optimizing deal value and objectives.

3. **Communicate with key stakeholders - employees**

An acquisition might be considered the highest order situation calling for change management. Following an acquisition, all stakeholders, including employees, are hungry for information. Each stakeholder group wants to know how will the acquisition affect and will they be better or worse off as a result.

GE used a formula in the nineties to promote understanding of the change process: Q X A = E. That is, the quality of a change strategy or initiative times the acceptance of that strategy or initiative is equal to/determines the effectiveness of the strategy or initiative. Many organizations underestimate the need for communications about the impact of the merger. Some organizations, including GE and Cisco, have developed extensive post merger integration processes including communications to quickly inform and engage employees from the time of the M&A announcement. While employees may not necessarily seeing the changes as directly benefitting them, acceptance builds when they believe there is an open dialogue regarding change and, as a result, few surprises.

Effective practices here include:
• “Town hall” meetings which provide a setting for senior leaders and employees to discuss questions and answers related to the merger/acquisition.
4. **Identify and retain key personnel.**

Just as the necessary conditions for the success of an enterprise include some rather mundane notions such as having adequate cash to fund operations, the ultimate success of a business combination, or at least the optimization of that success, is totally dependent on "key" personnel.

Of course, the definition of "key" in this context varies widely, and some personnel who are clearly in this preferred group (for retention) are replicated in the global talent pool and are theoretically or practically substitutable. But loss of incumbent personnel who are targeted for retention is tantamount to loss of "corporate memory" and expediency – two precious commodities that the talent pool cannot replace. Even the most qualified substitute for a key player will not have the advantage of experience on-the-job and will need some time to assimilate in his/her new role. This is also true of existing employees promoted to positions vacated by employees that the merging companies would have preferred to retain.

Leaders often, and quite naturally, engage in discussions about key personnel early in any merger, including the selection process emanating from the duplication of positions resulting from the merger, which naturally creates the opportunity for the selected candidate to be securely retained via face-to-face discussions leading to negotiations, if necessary, and ultimate affirmation. The critical, and often overlooked, need is to be proactive in avoiding the unintended departure of incumbents whose positions are not being changed or challenged (because of merger-related "competition").

- Good management practices in this area include:
  - Reaching consensus on what leadership positions in the post-merger organization are most critical to its success.
  - Establishing common tactics (i.e., those acceptable to the top leaders of both/all entities) for assessing management talent and for implementing these assessments in a timely manner.
  - Quickly making choices ("who goes, who stays") and having a backup plan for key positions.
  - Establishing a common tactical plan for solidifying the retention of talent (retention bonuses, stock option plans, etc.) and for fairly treating persons being asked to depart (severance payments, non-compete agreements, etc).

5. **Allocate qualified and credible human resources to lead integration teams – and give these leaders the time and authority to act.**

Realizing the synergies expected through Merger and Acquisition requires the establishment of a dedicated integration team. This team should be selected early in the process. The integration team can build the necessary relationships between the two companies. Typically, the integration team will be composed of a corporate level sponsor, a senior member of the HR department and a representative from each of the companies’ operational units. There also should be members selected from the company being acquired. These individuals should be forward thinkers, respected in the organization and capable of gaining the support of others in the organizations. In the past, many integration teams have failed due to lack of respect for these individuals.

The integration team should be established at an early stage, preferably as soon as possible after signing the merger agreement. These roles are highly visible in the organization and
the roles of the team need to be established early. In order for the integration team to be successful, the leaders of the organization should give them the direction and the strategic vision for the new company, communicate to the team why they were selected, the importance of their role, and describe to them the expectations and results expected from their work on the team.

The effective ways to ensure the integration teams are successful would include:

• Provide the team members support so they will not focus on their regular positions - the integration project should be their primary goal
• Build a schedule of what should be done and when
• Establish teams to work on how each function and business unit will be combined (organization structure, job design, staffing levels, compensation, benefits, downsizing, benefit plans, etc.)
• Establish performance measures to ensure the team stays on track and accomplishes their objectives.
• Guide the team to quickly react on key ideas and decisions, focusing on major concerns such as long term profit, cost management, product and competitive strategy
• Implement a campaign to communicate the integration teams’ role, progress, and success to the entire organization and external stakeholders

CONCLUSIONS

In conclusion, this paper has described why the majority of Mergers and Acquisitions often fail because the financial aspects of the merger take precedent over the human capital side. It is important to keep in mind as we come out of this current recession when M&A activity starts to gain momentum to not lose sight of the Five Best Practices described above. Often companies believe that they will do it the right way and not fail as others have in these non-financial areas. The fact remains that most Mergers and Acquisitions occur for one of the five reasons mentioned at the beginning of the paper, all of which are based on financial objectives. The human capital areas are often secondary in importance.

The major lesson that can be learned from this research is to keep the people issues at the forefront of the merger and to follow the best practices outlined in order to be successful.

1. Incorporate organizational and workplace culture into the due diligence process.
2. Determine degree of integration appropriate to realize desired business objectives
3. Communicate with key stakeholders - employees
4. Identify and retain key personnel.
5. Allocate qualified and credible human resources to lead integration teams – and give these leaders the time and authority to act.

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IS ETHICAL DECISION MAKING ON SHORT-TERM EARNINGS MANAGEMENT IMPACTED BY THE ECONOMIC CRISIS?

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Abstract: A corporate culture of ethics requires all levels of employees to believe that the organization wants to act ethically in all it does. Enforcing ethical behavior in the business environment has become a priority, since the misbehavior of some top management representatives became public in the big scandals of the last 10 years. The prior experiences helped many top executives realize they must promote this culture through their own behavior. The authors of the paper use the results of a pilot study to analyze the opinions of Romanian Executive MBA students that are managers in their companies about the ethical behavior in some financial decisions with effect on short-term profit in the crisis and recovery context. It is a continuation, from another perspective, of a study the authors initiated in 2008. Here, the authors looked into the clusters of results during the years 2009-2011, when Romania was confronted with the economic crisis, and compared the conclusions with those of the previous study, that used data from economic growth.

Keywords: ethics, ethical decision making, management of short-term earnings

INTRODUCTION

Our perceptions of whether we do “what’s right” depend on such things as the situation, the time frame, the expectations of others, and whether we are face-to-face with the object of our actions. And we are much poorer judges of the “righteousness” of our decisions than those observing us. In other words, “ethics is subjective.”

The time of crisis showed more accurately than ever that moral systems – seen as behaviors, attitudes and decisions – cannot be regulated. In the free market frame, especially in downturn conditions, ethics takes sometimes a back seat (Kirk, 2008). The best a business school can do is talk about the importance of an ethical conduct and use all the available ways to disseminate messages of improving the ethical behavior expected from the free market adherents: students, teachers, alumni, citizens, consumers, producers, marketers, professionals, businesses, corporations, institutions, nations, societies, politicians, governments, law enforcement officials, scientists, judges, etc.

The authors of this paper have continued a study initiated in 2008 (Dumitrescu, Firică, Manaicu, 2008), where they surveyed and analyzed managers’ opinions about the ethics of several financial and accounting procedures in short-term earnings management. The procedures scrutinized were: changing or manipulating operating decisions or procedures to reduce/increase earnings; changing or manipulating accounting methods when the change to earnings is small/large; deferring discretionary expenditures into the next accounting period to meet the
quarterly/yearly budget target; selling excess assets to realize a profit; ordering overtime work at end-year to ship as much as possible; offering special credit terms; make large restructuring changes to reduce the future reporting costs.

In 2008, the crisis was impacting the business environment. Since then, brutal changes occurred in the worldwide economic environment. The evolution of the GDP shows the huge impact these changes had on the economic situation in Romania (Figure 1) and the strong pressures that the managers of companies acting in Romania had to face.

![GDP growth rate -in percentage](image)

Source: National Institute of Statistics

**Figure 1. Romania, GDP growth rate**

The authors analyzed the perception of the managers about the most effective measures dealing with the recovery process (Dumitrescu, Firică, Manaicu, 2010). The current paper gives more insight into the evolution of ethical behavior in Romania and is a complement to the conclusions of the 2008 study, reflecting the managers’ perspectives on the same decisions in the new economic context.

**THE GOAL OF THE STUDY**

The authors aligned with the initiative of the Institute for Business Administration in Bucharest (IBAB) to survey students’ opinions about general managerial practices. An already published result (Dumitrescu, Firică, Manaicu, 2008) monitored the evolution of the students’ opinions year by year from 2005 to 2008 on the ethical nature of financial-accounting procedures of the short-term earnings management. The study revealed some statistically significant differences between the students in 2008 and those in the previous years. Here, we continue this approach by using basically the same questionnaire, anonymously, in English.

The present paper aims to:
- Investigate the extent to which the economic conditions created ethical issues for managers with respect to short-term earnings management, as well as establish whether or not there was a change between 2009 and 2011;
- Compare our current results (for 2009-2011) with prior research findings (for 2005-2008), by testing the differences between the managers’ perception of several ethical issues of short-term earnings management, during the economic stability, and the crisis-recovery period, respectively.

**THE WORKING TOOL**

The study continued at IBAB between 2009 and 2011 is based on a questionnaire administered to the managers who are Executive MBA students. Given the managerial position of the majority of the students surveyed, middle level managers are under scrutiny in the current paper. New identification items have been added to the previous version of the questionnaire: industry
and gender. The questionnaire is a tool of comparison and control, and can help revise the most important decision and practical managerial aspects made through the debate of a case study (Simons, Sapir, Reinbergs, 1998). The working tool measures ethical perceptions and contains ten items regarding the procedures, the practices and the most important decisions related to the short-term earnings management. The decisions fall into four categories: changing or manipulating operating decisions or procedures (2 items); changing or manipulating accounting methods (2 items); deferring discretionary expenditures into the next accounting period (2 items); increasing short-term earnings by different methods to meet a budget target (4 items).

The accounting process can diverge from the underlying actual process of the firm. The divergence we are pointing in the paper is not related to the accounting standards or human limitation. We are referring to the perverted incentive of a certain group of stakeholders of the firm whose actions harm the interest of the other stakeholders by focusing on the most often used methods for managing short term profit.

The ten items of the questionnaire require the respondents to assess the behavior suggested by choosing one answer out of three:

- Ethical
- Questionable or minor infraction
- Unethical or serious infraction.

It is difficult to draw a general conclusion about the ethical or non-ethical behavior involved in a decision making process, because each situation should be seen against its specific backdrop – the business environment, the common practices, the organizational culture, the legal frame. However, our study has brought to light some significant aspects regarding the dynamics of the managers’ perception of the ethical business behavior.

THE RESPONDENTS

The respondents are students in the second semester of the EMBA Program, at IBAB. The topics of the session where the questionnaire was administered were: ethics, the internal control system, the performance targeting system, the payment and motivation system, the forecast and the short term earnings management, the risk management. Besides, at the time when the questionnaire was run, at the beginning of the course of Financial Management, the manager-students had already attended the Financial and Managerial Accounting course.

The number of respondents in each year is presented in Figure 2. We must mention that in 2010 and 2011 the number of the surveyed students diminished, given the reduced enrolment during these years, in direct relation with the contraction of the business education market. However, the response rate was high: out of the total number of students enrolled in the first year, 86% in 2009, 90% in 2010, and 91% in 2011 participated in the survey.

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of respondents</th>
<th>The proportion of the respondents in the students enrolled</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>59</td>
<td>86%</td>
</tr>
<tr>
<td>2010</td>
<td>18</td>
<td>90%</td>
</tr>
<tr>
<td>2011</td>
<td>20</td>
<td>91%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>154</strong></td>
<td><strong>–</strong></td>
</tr>
</tbody>
</table>

*Figure 2. The number and percentage of respondents in 2009-2011*

The structure by industries of the EMBA program respondents’ companies is presented in Figure 3. The percentage of respondents coming from highly regulated and highly compliant industries (such as Pharma, IT, Banking, Chemical industry) is on average 39%, the highest being in 2011 (45%) and the lowest in 2010 (30%).
Regarding the average age of participants there are not important differences between the three years. However, the highest average is in 2010 and 2011 (36 years) and the lowest is in 2009 (34 years) (Figure 4a). Looking at the respondents by gender, one can notice that in 2009 the structure is almost balanced, while in 2010 and 2011 it is deeply unbalanced, with 25/75% in 2010 and 35/65% in 2011 (Figure 4b). The average number of years of working experience is largely the same each year. The average managerial experience is 6 years in 2009, 6.8 years in 2010 and 8 years in 2011 (Figure 4c).

**Figure 3. The respondents by industry, 2009-2011**

The analysis of the results is made on two levels.
A) The longitudinal analysis of the three assessment clusters by each question.
B) The comparison of the current findings with our prior research.
The main conclusions at the level of analysis A) are:

1) Managing Short-Term Earnings by changing or manipulating operating decisions or procedures
   a) When the result is to reduce earnings
   b) When the result is to increase earnings

The results are briefly shown in the Figure 5.

In 2009, 53% of the respondents assessed that changing or manipulating operating decisions or procedures is a questionable or minor infraction, whatever the impact on the short term profit – to reduce or to increase it. A comparatively small proportion of respondents assessed the decisions as major infraction (25%), while 22% considered it ethical. It is significant that the same distribution holds for situations 1a and 1b, i.e. for reduced and increased earnings, respectively.

In 2011, 50% of the respondents assessed that whatever the impact on the short term profit, changing the operating decisions and procedures is unethical, major infraction. The rest of 50% expressed different assessments in connection with the impact of the decision on the short term profit: when the decisions reduced the short term profits, 35% assessed them as minor infractions, and 15% as ethical. When the decisions increased the short term profit, 35% assessed them as ethical, and 15% as minor infractions.

In 2010, the respondents assessed differently the decisions related to changing or manipulating the operating decisions, given the impact on the short term earnings: when the decisions decreased the profit, the assessment was for 47% minor infraction, for 35% ethical, and for 18% major infraction.

When the decisions targeted to increase the profit, 41% of the students assessed the behavior as ethical, 35% as minor infraction and 24% as major infraction.

Thus, the participants in 2011 were stricter (tended to view this item as less ethical).

2) Managing Short-Term Earnings by changing or manipulating accounting methods
   a) When the change to earnings is small
   b) When the change to earnings is large
As shown in the Figure 6, in all the three years and whatever the impact on the short-term profit, a large majority of students assessed the decisions as unethical or major infraction. The decisions were considered ethical by a very small proportion of respondents.

It is interesting that in 2010 the decisions regarding changing or manipulating the accounting methods with small impact on the short term profit were assessed by 39% as minor infraction, by 39% as unethical, and by 22% as ethical. The respondents in 2011 tend to be stricter when considering the ethicality of this procedure.

3) Managing Short-Term Earnings by deferring discretionary expenditures into the following accounting period

a) To meet an interim quarterly budget
b) To meet an annual budget target at year-end target

The results are briefly shown in the Figure 7.

The assessments of students on this group of decisions clearly show a different perception of the impact of deferring charges in order to meet a quarterly versus a year-end budget target.

In 2009 and 2011, the impact of deferring discretionary expenditures into the following accounting period in order to meet the quarterly budget is seen as a minor ethical infraction, but, in 2010, it is assessed by a large number of respondents (63%) as ethical.

The decisions of deferring discretionary expenditures into the following accounting pe-
period to meet the year end budget target is seen mainly in 2009 as a minor infraction, in 2010 as ethical and in 2011, by a large majority (60%), as unethical.

These results are consistent with the conclusion of a study (Mergenthaler, Rajgopal, Srinivasan, 2008) that finds evidence that failure to meet quarterly earnings benchmarks is associated with lower bonus and equity grants and higher probability of forced dismissal for both CEO and CFO.

4) Increasing Short-Term Earnings to meet a budget target

The breakdown of the response structure is shown in the Figures 8a, 8b, 8c, 8d.

a) By selling excess assets and gaining a profit

![Figure 8a. Question 4a](image)

b) By ordering overtime work at year-end to ship as much as possible

![Figure 8b. Question 4b](image)

c) By offering customers special credit terms to accept delivery without the obligation to pay until the following year

![Figure 8c. Question 4c](image)
d) By making large restructuring changes that reduce future reported costs

In all the three years the highest number of respondents assessed that these four decisions to increase the short term profit in order to meet the budget target are ethical.

However, some differences should be mentioned:

a) Selling excess assets for profit is assessed as ethical by the highest number of respondents (71%) in 2010 and as unethical, major infraction by 32% of respondents in 2011.

b) Ordering overtime work at year-end to ship as much as possible was assessed as ethical behavior by the highest number of respondents (59% in 2009, 50% in 2010, and 45% in 2011) and only a small proportion of respondents regarded it as unethical (13%, 11%, 15% respectively).

c) Offering customers special credit terms to accept delivery without the obligation to pay until the following year is assessed as ethical by 50% of respondents in 2010, and as unethical, major infraction by 40% of respondents in 2011.

d) Making large restructuring changes that reduce future reported costs is seen as an ethical decision by 78% of respondents in 2010, only by 43% in 2009, and by 60% in 2011. These results are consistent with the conclusions of our research regarding the managers’ perception about the most effective measures to cope with the crisis (Dumitrescu, Firică, Manaicu, 2010). A small proportion of students think this action is a major infraction.

Here are the main elements and conclusions of the analysis at the second level, B):

Based on the prior research described at point A, we make the following hypothesis: due to crisis conditions, the Romanian managers’ perception of the ethical principles in the years 2009, 2010, and 2011 changed significantly when compared with the time span 2005-2008, since the economic conditions altered considerably. To test this hypothesis, four samples were considered:

– Sample 1 comprised 293 students in 2005-2008 with aggregated answers on a 4-year time span;
– Sample 2 comprised 59 students in 2009;
– Sample 3 comprised 18 students in 2010;
– Sample 4 comprised 20 students in 2011.

First, for each of the ten practices, we computed the aggregated frequency distributions of responses of sample 1 (Figure 9). In the adopted methodology, the sample 1 is considered the controlling group while the samples 2, 3, and 4 are the experimental groups. Then, we compared the frequency distributions of samples 2, 3, and 4 of each item with those aggregated of sample 1.
The three answer options to each item (ethical, questionable or minor infraction, and unethical or serious infraction) were considered exhaustive categories and require the application of a test for the equality of proportions with specified values – those from the controlling sample. The results of the comparison are presented in the Annex. At 0.05 significance, we found the following results:

In 2009, the students had almost the same opinion as the controlling group 1 about the ethicality of actions, except item 4c: “increase the short term earnings to meet a budget target by offering customers special credit terms to accept delivery without obligation to pay until the following year”. Students in 2010 judge somewhat differently the ten items proposed by the questionnaire, but only three items reveal a statistically significant difference of structure of responses: 3a, 3b, and 4d. Thus, students in 2010 seem to consider to a much larger extent “deferring discretionary expenditure into next accounting period to meet an interim quarterly and year-end target” an ethical procedure. The same conclusion is available for the action 4d: “increase the short term earnings to meet a budget target by making large restructuring charges that reduce future reported costs”. The proportion of students who considered it ethical almost doubled in 2010. The distribution of students in 2011 differs in four out of the ten items of the questionnaire, compared with 2005-2008.

<table>
<thead>
<tr>
<th>Item</th>
<th>Ethical</th>
<th>Questionable or minor infraction</th>
<th>Unethical, or serious infraction</th>
</tr>
</thead>
<tbody>
<tr>
<td>1a</td>
<td>0.303</td>
<td>0.441</td>
<td>0.255</td>
</tr>
<tr>
<td>1b</td>
<td>0.303</td>
<td>0.303</td>
<td>0.393</td>
</tr>
<tr>
<td>2a</td>
<td>0.096</td>
<td>0.443</td>
<td>0.460</td>
</tr>
<tr>
<td>2b</td>
<td>0.072</td>
<td>0.203</td>
<td>0.725</td>
</tr>
<tr>
<td>3a</td>
<td>0.277</td>
<td>0.476</td>
<td>0.247</td>
</tr>
<tr>
<td>3b</td>
<td>0.173</td>
<td>0.363</td>
<td>0.464</td>
</tr>
<tr>
<td>4a</td>
<td>0.608</td>
<td>0.265</td>
<td>0.127</td>
</tr>
<tr>
<td>4b</td>
<td>0.543</td>
<td>0.372</td>
<td>0.085</td>
</tr>
<tr>
<td>4c</td>
<td>0.488</td>
<td>0.430</td>
<td>0.082</td>
</tr>
<tr>
<td>4d</td>
<td>0.410</td>
<td>0.358</td>
<td>0.232</td>
</tr>
</tbody>
</table>

Figure 9. The aggregated frequency distribution of the ten items of the questionnaire during the period 2005-2008 (sample 1)

Our study revealed that the number of criteria that had statistically different frequency distributions, compared with 2005-2008, is increasing year by year.

CONCLUSIONS

Our research can be considered as aligned with the research direction opened in 1990 by Bruns and Merchant (1990) regarding the morality of short term earnings management. In this respect, the results of our research are consistent with those of Giacomino and Bellovary (2006). The most important findings of the current study are:

– as anticipated, the economic crisis created ethical issues for the students enrolled in the Executive MBA program that are managers in their companies; our study shows that there is evidence of an attitude change (stricter view) regarding the ethics of short-term earnings management, more visible in 2011;
– the number of practices that had statistically different frequency distributions, compared with 2005-2008, increased year by year in the period 2009-2011, affected by the economic crisis in Romania. However, this change is not as extensive as we hypothesized;
none of the ten practices were assessed unanimously as either ethical, or totally unethical practices;
the results indicate that the direction of the impact of the decision (increase or decrease in short-term profit) alter the basis for judgment on the 3-option scale. The reduction of earnings or smaller effects were assessed as more acceptable than the increase of earnings and larger impact;
the reporting period (quarterly or year-end) affected significantly the answers: decisions were rated less acceptable if they affected year-end results;
our students need more exposure and understanding of the methods used to manage earnings.

REFERENCES


Merhentaler R., Rajgopal S., Srinivasan S., [2008]. CEO and CFO career consequences to missing quarterly earnings Benchmarks HBS, working paper series, 09-014


Exhibit 1: The results of the equality of proportions with the \( x^2 \) test

The notations below on item 1a) were introduced:

<table>
<thead>
<tr>
<th>The theoretical proportions of the sample 2, 3, or 4</th>
<th>1a) is ethical</th>
<th>1a) is questionable or a minor infraction</th>
<th>1a) is unethical, or a serious infraction</th>
</tr>
</thead>
<tbody>
<tr>
<td>The specified proportions from the sample 1</td>
<td>( \pi_1 )</td>
<td>( \pi_2 )</td>
<td>( \pi_3 )</td>
</tr>
<tr>
<td>( \pi_1^0 = 0.303 )</td>
<td>( \pi_2^0 = 0.441 )</td>
<td>( \pi_3^0 = 0.255 )</td>
<td></td>
</tr>
</tbody>
</table>

The null hypothesis was tested: \( H_0: \pi_1 = \pi_1^0, \pi_2 = \pi_2^0, \pi_3 = \pi_3^0 \) against the alternative

\( H_1: \) at least one of the equalities does not hold.

Using the appropriate test procedure and the 0.05 level of significance, we conclude:

<table>
<thead>
<tr>
<th>Item</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>1a</td>
<td>Do not reject ( H_0 )</td>
<td>Do not reject ( H_0 )</td>
<td>Reject ( H_0 )</td>
</tr>
<tr>
<td>1b</td>
<td>Do not reject ( H_0 )</td>
<td>Do not reject ( H_0 )</td>
<td>Do not reject ( H_0 )</td>
</tr>
<tr>
<td>2a</td>
<td>Do not reject ( H_0 )</td>
<td>Do not reject ( H_0 )</td>
<td>Reject ( H_0 )</td>
</tr>
<tr>
<td>2b</td>
<td>Do not reject ( H_0 )</td>
<td>Do not reject ( H_0 )</td>
<td>Do not reject ( H_0 )</td>
</tr>
<tr>
<td>3a</td>
<td>Do not reject ( H_0 )</td>
<td>Reject ( H_0 )</td>
<td>Do not reject ( H_0 )</td>
</tr>
<tr>
<td>3b</td>
<td>Do not reject ( H_0 )</td>
<td>Reject ( H_0 )</td>
<td>Do not reject ( H_0 )</td>
</tr>
<tr>
<td>4a</td>
<td>Do not reject ( H_0 )</td>
<td>Do not reject ( H_0 )</td>
<td>Reject ( H_0 )</td>
</tr>
<tr>
<td>4b</td>
<td>Do not reject ( H_0 )</td>
<td>Do not reject ( H_0 )</td>
<td>Do not reject ( H_0 )</td>
</tr>
<tr>
<td>4c</td>
<td>Reject ( H_0 )</td>
<td>Do not reject ( H_0 )</td>
<td>Reject ( H_0 )</td>
</tr>
<tr>
<td>4d</td>
<td>Do not reject ( H_0 )</td>
<td>Reject ( H_0 )</td>
<td>Do not reject ( H_0 )</td>
</tr>
</tbody>
</table>
COMPETENCY DEVELOPMENT FOR TRANSFORMATIONAL LEADERSHIP

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Abstract: The paperwork attempts to understand and further explain the competencies one needs to personally develop in order to be able to reach the transformational leadership stature from a mere transactional one, along to observing the highs and lows of each type of leadership and highlighting their impact in the day-to-day business, with examples from banking, pharmaceuticals, telecommunications, electronics and IT industries.

Keywords: Transformational Leadership; Transactional Leadership; Training and Development; Management Competency

JEL Codes: M1; M5; J24

Existing Transformational Development Competencies – A Testimonial of a Follower

Motto: I must follow the people. Am I not their leader?
Benjamin Disraeli

Dear Authors,
I understand that you plan to write a paper on transformational and transactional leadership. Allow me to share with you my thoughts on the matters.

Looking back at my early career compared to the stage I find myself nowadays, I realize that most of my intuitive observations made back then can now be explained in a more structured and logical way. I remember the times when I was classifying my hierarchical managers in two categories: the “quiet” ones and the “active” ones.

The “quiet” ones:
- were managing the unit the same way every day;
- they avoided to involve themselves in big projects;
- I could often hear them saying “Why did you stick your nose where you didn’t belong?
It’s not our business to get involved”;
- they opposed or showed resistance to any type of change;
- they were not able to provide a decent answer to any of the professional questions asked or they were simply turning the discussion toward a different topic till somebody around was finally, releasing an opinion;
- last but not least, their time was eaten-up by a huge amount of routine.

On the contrary, the “active” ones:
- were coming to actually see what was one doing; they wanted to understand the kind
of job performed by their subordinates;
- were always prompting ideas;
- initiated the most important and complex projects;
- were inspirational, always interested in new approaches and ready to support or offer explanations;
- have many times destroyed the well established status-quo of many other bosses around exposing incompetence;
- did hate any unproductive routine.

I believe that my intuitive segmentation in “active” and “quiet” managers needs to get in depth by assessing their managerial effectiveness. A further compare-and-contrast drill of a transactional leader and a transformational leader might be worthwhile, indeed.

A Follower

**TRANSFORMATIONAL OR TRANSACTIONAL – THIS IS THE QUESTION!**

Leadership is the ability of using a no coercive influence to direct and coordinate the activities of group members toward goal accomplishment. Leadership involves neither force nor coercion. A manager who relies on force to direct subordinates’ behaviors is not exercising leadership. Leaders instead rely on their traits and skills, behavior in relations with their subordinates and on their capacity to understand and adapt to a specific context. (Zorlentan, Mincu, 2006)

Martin has cited Burns and then Kuhnert and Lewis who were suggesting that in 1978 and 1987 respectively there are two types of management activity, each demanding different skills (Martin, 2005):

1. Transactional. This includes the allocation of work, making routine decisions, monitoring performance and interacting with other functions, departments and teams within the organization.
2. Transformational. This is about having the skills and personal qualities to be able to recognize the need for change and the adequate course of action to cope with change.

Robbins and Judge cited Bass who identified in 1990 the characteristics of both types of leader (**Exhibit 1 – Transformational and Transactional Leadership Momentum**), suggesting that transactional leadership represents rather a restrainer to change, fostering a climate of mediocrity. (Robbins, Judge, 2010)

By contrast, transformational leaders can produce higher performance when dealing with uncertainty and change. The transformational leader is a catalyst of change, takes charge as change agent, is audacious in risk taking, believes in team members, does the utmost to empower others, is able to dream and share it with others. Transformational leadership makes bold, unexpected and innovative moves to adapt organization effectively to the dynamic and turbulent environment. In this endeavor, they may alter the management methods and processes to serve the customers, the product portfolio and technologies. Transformational leaders are capable of having a profound and extraordinary effect on their followers. (Robbins, Judge, 2010) They earn the trust of followers, build confidence among their team members by helping them increase their competence and performance, while giving freedom to take initiative, hence achieving higher acceptance of objectives among subordinates. Transformational leaders play a role model for their people and inspire them to perform above and beyond the call of duty. (Kreitner, 1995)

Unlike transformational leaders, the transactional leaders are focusing to achieve the repetitive and routine activities. They are highly efficient in a static environment, in an organization that may manufacture and sell a stable product portfolio, with same methods and technologies. These kinds of leaders guide or motivate their followers to achieve the established goals by clarifying role and task requirements. Transactional leadership involves daily exchanges between leaders and subordinates in the areas of reward allocation, monitoring deviations from
rules and standards and taking corrective action, as well as providing the direction and support for task achievement. (Schermerhorn, 1996; Schermerhorn, Hunt, Osborn, 1995)

The major issue highlighted through this model is that most leaders are required to engage in both transactional and transformational leadership as part of their responsibilities. If leaders tend to one “type” then it will be difficult for them to achieve an effective performance across the full range of their responsibilities. Transactional and transformational leadership are not opposing approaches to getting things done; they complement each other, but that does not mean they are equally important. Transformational leadership builds on top of transactional leadership and produces levels of follower effort and performance that go beyond what would occur with transactional approach alone. The reverse is not true. An effective transactional leader with poorly developed transformational competencies will likely only be a mediocre leader. The best leaders are transactional and transformational. (Robbins, Judge, 2010)

The role for businesses is widely recognized when it comes to leadership development and on-the-job training through the corporate programs aiming to develop the company’s own human resources with special headline for programs targeting the developmental needs of the management teams. The challenges the CEOs have reported in recruiting and retaining talent reflect the strategic and geographical changes afoot for many companies. Companies are taking the long view on addressing talent and management needs in every market where they operate. The CEOs consider that they need to foster the capacity of the organization to attract, retain and manage talent. This does not depend currently on the compensation packages, but rather on the CEO and executive teams’ ability to create a sense of belonging to an organization that offers a long-term relationship and a professional development opportunity for the talent, for the company’s human capital. Global deployments are a first step to address shortages as company footprints change, but many CEOs know they need to nurture local talent management in the long run. Any idea that a centralized headquarters can effectively dictate to far-flung operations in increasingly important markets is disappearing. Many of today’s multinationals want to give independence to local managers that understand the local culture and know how to do business, to get closer to those markets, to build the next generation of leadership fully competent to take their companies to the next level. (PricewaterhouseCoopers-Report, 2011, p.15, 17) Moreover, the risk management capabilities at all levels of management have become nowadays a critical option into developing management teams. 69% of CEOs surveyed in Romania are looking at allocating more senior attention to risk management, 50% formally incorporating risk scenarios into strategic planning, 46% at allocating more board meetings attention to risk management. (PricewaterhouseCoopers Findings, 2011, p.10) Therefore, the profile of the manager nowadays has been enriched and new personal developmental needs are ripe to be approached to successfully adapt to complex economic and business challenges.

**“BECOMING THE LEADER” CHARTER**

In the attempt to define the complex process one has to go through until becomes a real leader, Figure 1 summarizes the most important transformational milestones.

![Figure 1](image-url)
In **stage I**, the individual has the passion and willingness to learn. **Stage II** does position the individual fully convinced about the bright perspective of his/her professional choice and ready to show what he/she is able to do. As the level of experience and qualification rise, the individual starts to develop competencies and intuition; as the **stage III** ends, business vision starts to shape up. This is the phase where luck or favorable circumstances get into the picture – it is the “turning point”. If one is not lucky to be discovered and promoted, by a hierarchical superior then his/her motivation will gradually lose pace and the lack of interest may easily install. This is a moment when a large majority of employees decides to change their professional orientation. Favorable circumstances proved to play a lesser role, immaterially weighting in this probability game versus luck. Going forward, in the **stage IV**, we will see that luck actually represents the emerging of a visionary leader, meaning a transformational leader. Luck has been there, while the individual’s vision has helped her/him to become the Leader.

**We have a leader. What do we do with her/him and what is she/he doing with us?** The fact that there are so many debates about leadership suggests that there is no magic formula for the best way to lead. The economic and financial landscape has changed dramatically in the last three years and topics like managing risks, finding new ways of protecting own capital or raising it and foreseeing various threats the companies may face, have become common subjects of discussion. Due to the increased level of risks within the business environment nowadays, some leaders prefer not to change anything within the existing business model or organization. They struggle to maintain the same way of doing business and show no flexibility. Moreover, they even penalize any attempt of change coming their way. They are the transactional leaders. They are more worried about their own well being and intellectual comfort than about progress and improvement. They will do the same thing every day without complaining. They will neither offer help nor raise obstacles in front of those who have initiatives. They will simply not get involved and they will postpone each requested meeting, until the interested parties will give up in a classical “laissez-faire” approach. They do not have enough strength or determination to initiate improvement. The maximum risk a transactional leader is going to take is the delegation of responsibilities and some networking. To whom and how are they delegating? Whom do they choose to network with? Mostly to people they are comfortable to deal with, to persons raising no difficulties in the day-to-day activity, or sharing the same views in terms of professional goals.

Transactional leaders need to demonstrate their character, their competence and their influence in order to have their management style accepted. Otherwise, they will be continuously challenged and will face difficulties in imposing their points of view. Delegating responsibility or authority does not solve a transactional leader’s low points. Managers must control their direct reports because if they will rely too much on their formal authority without effectively checking the outcome, they will soon realize they achieved a false victory. In face of a difficult or unexpected obstacle, the subordinates may tend to hide the problem not wanting to look like they were unable to solve it. How would they manage to solve it, may indeed represent an issue, if controls are not put in place.

Managers must focus on networking, not only on good and old friendships. As a manager moves into a leadership role, his or her network must reorient toward a strategic form of networking, beyond the personal and operational networks possessed. If a leader focuses only on one-on-one relationships, he/she most likely will neglect the collective power of a group to improve individual performance and commitment. (Ibarra, Hunter, 2007) Unfortunately, transactional leaders are hardly able to develop themselves a flair for opportunity to initiate change or improvement or to spot the right persons to get things done by self-involving to mentor, coach or assist them.

The quest from a functional manager or a transactional leader to a business manager or a transformational leader means to look at adding important competencies (Kaplan, 2007):

(a) **Vision and priorities**
- how often do I communicate a vision for my business?
- have I identified and communicated three to five key priorities to achieve that vision?
- if asked, would my employees be able to articulate the vision and priorities?

(b) Managing time
- how am I spending my time?
- does it match my key priorities?
- how are my subordinates spending their time?
- does that match the key priorities for the business?

c) Feedback
- do I give people timely and direct feedback that they can act upon?
- do I have at least five junior subordinates who will tell me things I may not want to hear but need to hear?

d) Succession planning
- have I - at least in my mind, picked up one or more potential successors?
- am I coaching them and giving them challenging assignments?
- have I become a decision bottleneck?

e) Evaluation and alignment
- is the business model of my company still aligned with the key success factors for the business?
- if I had to design again my business would I do it the same way? Alternatively, would I do it differently?

(f) Leading under pressure
- what type of events creates pressure for me?
- how do I behave under pressure?
- what signals am I sending to my subordinates?
- are these signals helpful or are they undermining the success of the business?

g) Staying true to yourself
- is my leadership style comfortable?
- do I assert myself sufficiently or I have become tentative?
- am I politically correct in excess?
- does the worry for my next bonus or promotion cause me to hesitate to express my views?

The set of questions mentioned above and the ability “to smell” a good business have determined a well-known bank’s CEO operating on the Romanian market to consider initiating a new line of business. The bank was a reputable financial institution whose activity was focusing on offering financial services to large, well-established corporate clients. The CEO considered that it was time for the bank to diversify its client portfolio, through launching Consumer Banking business, in order to be able to offer full range of services to the corporate clients and to their employees. When the senior management team was told about his intentions, several Board members thought it would be a brilliant opportunity for a corporate bank. Some others showed reluctance considering that the bank was about to “jump” in “the unknown” - there was no competency in the Consumer business, locally, with the entire banking industry at its dawn with respect to financing individuals. Eventually, the Consumer Banking business was launched and it was a total success – a success driven by the CEO’s inspirational leadership, with his vision, courage, total support in terms of training and development, networking with relevant experts from within the international group the local bank was part of, and who could spread knowledge and personal involvement. As a genuine transformational leader, he did create a vision, convince his followers to pursue for it and implement immediately.
TO BE “LEADERSHIP COMPETENT” IN TELECOMMUNICATIONS, ELECTRONICS AND IT

The next data and findings are the result of a consulting project initiated in 2005-2009 that has encompassed over 100 senior and middle managers from several international telecommunications, electronics and IT companies operating on the Romanian market - voice and data services, telecommunication wholesale, software development, IT solutions and services, electronics, computer and copying equipment import and distribution. The project aimed to evaluate the level of leadership competencies and subsequently, identify the competencies that need further development so that the management team is able to cope well with very competitive industries, as are telecommunications, electronics and IT industries for the last fifteen years in Romania. The fierce competition, the continuous strive for profitability improvement through cost reduction and quality management endeavors, Lean Six Sigma included, have determined significant change of roles for the managers, supervisors and employees with respect to equipping them with a wider range of skills - including more interaction with customers and suppliers, greater challenges, higher uncertainty, increased responsibilities. (Mincu, 2010)

The “Win-Win!” Program as dubbed internally did employ an instrument1 based on a set of managerial competencies applicable to all management layers. Being “leadership competent” in the understanding of the instrument was to possess, put to work and give visibility to three facets of a competency: knowledge, skills and attitude. Sometimes, we are possessing broad knowledge and we are highly skilled in specific domains and projects but we fail due to a neutral or negative attitude. Sometimes, we are passionately keen to accomplish a breakthrough, but we lack the necessary knowledge, structure, information or we are simply clumsy at new starts – most likely, we might deliver an average performance at best.

The instrument has brought forward about 50 management competencies, out of which several has been selected by the top management as essential competencies expected to three-fold (knowledge-skills-attitude) equip the leadership positions, as follows:

- displaying management competencies such as “recruiting talent”, “managing people’s performance”, “managing through systems and technology”, “customer focus”, “effective decision making”, as well as “planning”, “quality management” and “time management” – describing active management by exception and contingent reward.

This expresses the expectation of the organization that the job incumbent will perform as effective transactional leader, regardless leadership job in the hierarchy.

- individualized consideration through competencies of “developing people”, “delegation”; intellectual stimulation through “effective problem solving”, “creativity and innovation”; inspirational motivation through “motivating people”, “dealing with risk and uncertainty”, “delivering effective presentations”; idealized influence through “ethical and authentic”, “possessing vision” and “building teams”.

The expectation of the organization was that the job incumbent would be an effective and active transformational leader, regardless leadership job in the hierarchy.

Within the Win-Win!” endeavor, each manager performed a self-evaluation against the same set of essential competencies. His/her direct superior evaluated him/her based on the same benchmarking grid. A one-on-one feedback session took place between the two parties, resulting into an agreement of competencies that would need to undergo further development. The following trends of leadership developmental needs were identified [Exhibit 2 – Development Status of “Win-Win!” Leadership Competencies in Various Industries]:

- most of the essential competencies equipping an effective transactional leadership were well developed at the entire group of executives under evaluation, with the exception of “quality management” and “time management”;

- several essential competencies of an effective and active transformational leadership appeared well developed: “effective problem solving”, “creativity and innovation”, “ethical and authentic”, “delegation”. Yet, most of the other competencies would need
significant progress and development: “motivating people”, “dealing with risk and uncertainty”, “possessing vision”, “building teams”, “developing people”, “delivering effective presentations”.

The diagnosis of the developmental needs for the leaders in the telecommunications, electronics and IT companies was followed by the agreement of personal development plans, customized to personal needs but covering the essential leadership competencies as well. Various forms of training and development - in class, online, coaching and mentoring, business plan development, exposure to special projects, exchange programs etc - were included in each manager’s plan for the six to twelve months following the diagnosis and agreement.

LEADERSHIP COMPETENCIES IN PHARMACEUTICALS

Another “Win-Win!” consulting project has been completed in 2010 for a Romanian vertically integrated group of pharmaceutical private companies (import and distribution of drugs, food supplements and natural products, pharmacy and high-end products retail chains). Included in the endeavor were over 170 senior, middle and first line managers. The project has targeted to evaluate the level of leadership competencies and subsequently, identify the competencies that need further development so that the management team is able to cope well with a strictly regulated, competitive and high personnel turnover industry as is pharmaceuticals for the last ten years in Romania.

The top management has selected the following essential “Win-Win!” competencies to equip the leadership positions:

• “recruiting talent”, “managing people’s performance”, “customer focus”, “effective decision making”, as well as “planning”, “organizing work”, “negotiation” and “time management” – describing an active management by exception and contingent reward. This expresses the expectation of the organization the job incumbent would need to be an effective transactional leader.

• individualized consideration through competencies of “developing people”, “composure” and “delegation”; intellectual stimulation through “effective problem solving”, “managing process”; inspirational motivation through “motivating people”, “dealing with risk and uncertainty”, “delivering effective presentations”; idealized influence through “ethical and authentic”, “possessing vision” and “building teams”.

The expectation of the organization was that the job incumbent should be an effective and active transformational leader.

The “Win-Win!” process of self-evaluation - direct manager’s evaluation – feedback – consensus of a personal development plan revealed the following trends of the management team’s developmental needs in the pharmaceutical companies ([Exhibit 2 – Development Status of “Win-Win!” Leadership Competencies in Various Industries]):

• most of the essential competencies equipping an effective transactional leadership were well developed at the group of executives under evaluation, except “recruiting talent”, “effective decision making”, “managing people’s performance” and “time management”;

• essential competencies of “effective problem solving” and “ethical and authentic” appeared well developed at the level of effective and active transformational leadership. Yet, most of the other competencies need significant progress and development: “developing people”, “delegation”, “motivating people”, “managing process”, “dealing with risk and uncertainty”, “possessing vision”, “delivering effective presentations”, “building teams”.

Strategic Agility: Accountable Leadership in Action
BEYOND TRANSACTIONAL LEADERSHIP, REACH TRANSFORMATIONAL LEADERSHIP

A leader’s work is never done. Once becoming a leader, the last and the most important test is to share the learning with the next generation of leaders. This last task fails in most cases; this last test actually needs to begin long before a leader is ready to leave the stage.

With this remark, the paperwork would like to conclude by emphasizing the main competencies a transactional leader has: is able to manage during quiet and less turbulent economic times, with great challenges when asked to lead their companies and teams through turbulent or critical economic periods; apply basic management competencies that do not reach the impact of the advanced leadership competencies such as mentoring, coaching or sharing knowledge; first line and middle management people have all chances to become effective transactional leaders, while in higher hierarchical leadership positions would rather fail lacking the competencies to inspire and direct teams and companies. Examples from several industries in Romania are demonstrating that companies in Romania enjoy a good development level of transactional leadership competencies, yet those are not offering enough agility to mitigate the current economic turbulence.

By contrast, the transformational leaders need to possess the competencies to drive the organization and its people to a better future and beyond expectations: will always have the courage to take the most difficult decisions to mitigate risk and uncertainty, with remarkable results; his/her creativity bursts during tough and stressful economic periods when their capabilities appear to “explode”; will be ready to share knowledge with those intellectually and emotionally close to him/her, fighting stupidity, incompetence and self-sufficiency. The leadership teams in Romania still have to complete a complex journey to build the necessary transformational leadership competencies, with active focus on people management competencies - as the examples from various industries have shown.

And as Kenneth W. Freeman said, it takes a well-managed ego to help a successor become, in the best case, an even better leader than you are.

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1 Based on the philosophy of Career Architect created by Mike Lombardo and Bob Eichinger in the early 1990s; for more details, consult Using the Career Architect to Assess and Develop Leadership Competencies, http://acumen-international.com/site/acumen/files/articles/Using%20the%20Career%20Architect%20to%20Assess%20and%20Develop%20Leadership.pdf

Exhibit 1 – Transformational and Transactional Leadership Momentum (Robbins, Judge, 2010)

<table>
<thead>
<tr>
<th>Transformational leader</th>
<th>The most effective and active</th>
</tr>
</thead>
<tbody>
<tr>
<td>Idealized influence</td>
<td>Provides vision and sense of mission, instills pride, gains respect and trust</td>
</tr>
<tr>
<td>Inspirational motivation</td>
<td>Communicates high expectations, uses symbols to focus efforts, expresses important purposes in simple ways</td>
</tr>
<tr>
<td>Intellectual stimulation</td>
<td>Promotes intelligence, rationality, and careful problem solving</td>
</tr>
<tr>
<td>Individualized considera</td>
<td>Gives personal attention, treats each employee individually, coaches, advises</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Transactional leader</th>
<th>Ineffective and passive</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contingent reward</td>
<td>Contracts exchange of rewards for effort, promises rewards for good performance, recognizes accomplishments</td>
</tr>
<tr>
<td>Management by exception (active)</td>
<td>Watches and searches for deviations from rules and standards, takes corrective action</td>
</tr>
<tr>
<td>Management by exception (passive)</td>
<td>Intervenes only if standards are not met</td>
</tr>
<tr>
<td>Laissez-faire</td>
<td>Abdicates responsibilities, avoids making decisions</td>
</tr>
</tbody>
</table>

Source: (Bass, 1990)

Exhibit 2 – Development Status of “Win-Win!” Leadership Competencies in Various Industries

<table>
<thead>
<tr>
<th>Essential leadership competency</th>
<th>Telecommunications, Electronics and IT (100 managers surveyed)</th>
<th>Pharmaceuticals (170 managers surveyed)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Recruiting talent</td>
<td>25% managers to develop</td>
<td>75% managers to develop</td>
</tr>
<tr>
<td>Managing people’s performance</td>
<td>30% managers to develop</td>
<td>65% managers to develop</td>
</tr>
<tr>
<td>Managing through systems and technology</td>
<td>25% managers to develop</td>
<td></td>
</tr>
<tr>
<td>Customer focus</td>
<td>20% managers to develop</td>
<td>15% managers to develop</td>
</tr>
<tr>
<td>Effective decision making</td>
<td>35% managers to develop</td>
<td>50% managers to develop</td>
</tr>
<tr>
<td>Planning</td>
<td>30% managers to develop</td>
<td>35% managers to develop</td>
</tr>
<tr>
<td>Organizing work</td>
<td></td>
<td>35% managers to develop</td>
</tr>
<tr>
<td>Negotiation</td>
<td></td>
<td>25% managers to develop</td>
</tr>
<tr>
<td>Quality management</td>
<td>60% managers to develop</td>
<td></td>
</tr>
<tr>
<td>Time management</td>
<td>85% managers to develop</td>
<td>65% managers to develop</td>
</tr>
<tr>
<td>Developing people</td>
<td>50% managers to develop</td>
<td>75% managers to develop</td>
</tr>
<tr>
<td>Composure</td>
<td></td>
<td>35% managers to develop</td>
</tr>
<tr>
<td>Delegation</td>
<td>20% managers to develop</td>
<td>70% managers to develop</td>
</tr>
<tr>
<td>Effective problem solving</td>
<td>10% managers to develop</td>
<td>15% managers to develop</td>
</tr>
<tr>
<td>Creativity and innovation</td>
<td>20% managers to develop</td>
<td></td>
</tr>
<tr>
<td>Managing process</td>
<td></td>
<td>50% managers to develop</td>
</tr>
<tr>
<td>Motivating people</td>
<td>55% managers to develop</td>
<td>60% managers to develop</td>
</tr>
<tr>
<td>Dealing with risk and uncertainty</td>
<td>50% managers to develop</td>
<td>65% managers to develop</td>
</tr>
<tr>
<td>Delivering effective presentations</td>
<td>70% managers to develop</td>
<td>80% managers to develop</td>
</tr>
<tr>
<td>Ethical and authentic</td>
<td>10% managers to develop</td>
<td>7% managers to develop</td>
</tr>
<tr>
<td>Possessing vision</td>
<td>65% managers to develop</td>
<td>75% managers to develop</td>
</tr>
<tr>
<td>Building teams</td>
<td>55% managers to develop</td>
<td>50% managers to develop</td>
</tr>
</tbody>
</table>
CRISIS MANAGEMENT FROM THE PERSPECTIVE OF STATE AID POLICY

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Abstract: The importance of the competition protection policy has been always questioned during economic crises. The main argument against antitrust enforcement was that it delays the economic recovery. This paper is focused on state aid policy in European Union. It presents the temporary relaxation of the rules, the results of their enforcement and concludes with an evaluation of the European approach in this field.

Keywords: competition policy, economic crisis, state aid policy

JEL Codes: L4, L5

INTRODUCTION

Motto: Whilst vital state aid to the financial sector has been permitted under specially adapted, crisis-specific rules, state aid to the non financial sector has remained broadly stable, and a positive aspect is that, in these circumstances, Member States have continued to re-orient State subsidies to research, environmental protection and other general-interest objectives, which create growth and jobs.”

Joaquin Almunia, European Commission Vice-President in charge of competition policy

There is already a truism to say that the recent financial and economic crisis has been the most severe after the Great Depression of 1930s in the past century. Therefore, the question on how decision-makers have dealt differently today than 70 years ago is perfectly reasonable. However, at this point, we may remember what the former China’s Prime Minister, Zhou Enlai, answered in the 1970s to a question about the impact of the French revolution (1789): “Too early to say”. Obviously, it is too early for a full checkup of the lessons that derive from the recent crisis.

But there are at least two conclusions that may be drawn at this moment about the different approaches during past and present crises. The first is that antitrust policy was not put aside as it happened during past crises. In the past, during both economic crises and wars, times of severe national anxiety, antitrust has taken a back seat to other political and regulatory objectives. Antitrust enforcement has often been a political luxury good, consumed only during periods of relative peace and prosperity (Crane, 2010). Opinions have prevailed that antitrust enforcement is a “luxury good,” meaning that, while it may be afforded in good economic times, it must be relaxed in bad economic times or that antitrust enforcement is “so yesterday,” meaning that, while it could be accommodated while Western economies flourished, it cannot be tolerated anymore in times of globalization (Lasserre, 2010).

It didn’t happen this time. The former EU competition commissioner, Neelie Kroes, mentioned: “Throughout those first weeks after the collapse of Lehman Brothers, the Commission faced great pressure to set aside the competition rules on State aid, in order to allow EU Member
States freedom to implement financial sector rescue measures as they saw fit. This scenario, we believed, would be the first step towards repeating a Great Depression. To avoid this fate we set out to argue the case for continued application of not only state aid control but all competition rules. We promoted this as the way to maintain a level playing field in the EU and avoid large-scale movements of funds between Member States by investors in search of the highest level of protection. In other words, we wanted to stop a subsidy war” (Kroes, 2010).

The second main difference from the 20th century Great Depression was in the efforts of the governments to coordinate between themselves and not to act independently. We refer here to global coordination in the framework of G20 or international organizations like IMF and OECD, trans-Atlantic coordination between US and European Union, or coordination inside the EU. However, we are aware about the fact that there have been a lot of different opinions and approaches, like, for instance, the debate between US and EU about the moment and strategy of exit from the governmental support programs.

The global management of the crisis includes measures taken at several different levels, involving different sectors. The first level is the international support for countries in difficulties. Ireland or Greece is the best example, but not the only one. Romania has been a beneficiary of such a help. The interventions of the Federal Reserve or the European Central Bank in order to provide liquidity on the markets are another one. Direct support for the banking system and for companies in the ‘real’ economy is the third level.

Support does not come without conditionalities and changes in the rules. As a result, there will be changes in the control of fiscal policies inside EU and in the regulation of the banking system. On the other hand, there will not hopefully be changes in the European rules on state aid control. This paper is focused on the current situation of state aid rules inside the European Union and on their future developments.

**APPROACH OF THE EUROPEAN UNION**

In 2008/2009, the European Commission put in place a temporary State aid framework to enable Member States to deal with financial problems in the banking system, as well as support access to finance for firms in the other sectors of the economy. This framework, which was tightened as part of an exit strategy in July and December 2010, is in place until the end of 2011. The next table summarizes these measures:

<table>
<thead>
<tr>
<th>Measure.</th>
<th>Date of enforcement</th>
</tr>
</thead>
<tbody>
<tr>
<td>The application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis</td>
<td>13 October 2008</td>
</tr>
<tr>
<td>The recapitalization of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition</td>
<td>5 December 2008</td>
</tr>
<tr>
<td>Communication from the Commission on the Treatment of Impaired Assets in the Community Banking Sector</td>
<td>25 February 2009</td>
</tr>
<tr>
<td>Temporary framework for State aid measures to support access to finance in the current financial and economic crisis</td>
<td>17 December 2008</td>
</tr>
<tr>
<td>The return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules</td>
<td>23 July 2009</td>
</tr>
<tr>
<td>Communication from the Commission on the application of State aid rules to support measures in favor of banks in the context of the financial crisis</td>
<td>1 January 2011</td>
</tr>
</tbody>
</table>

*Source: European Commission*
The guidance was based on EC Treaty rules allowing for aid to remedy a serious disturbance in the economy of a Member State (Article 87.3.b of the EC Treaty). These measures were thought to help Member States to put in place coordinated concrete measures to restore confidence in financial markets. EU state aid rules require that measures taken do not give rise to disproportionate distortions of competition, for example by discriminating against financial institutions based in other Member States and/or allowing beneficiary banks to unfairly attract new additional business solely as a result of the government support. Other requirements include that measures must be limited in time and foresee adequate contributions from the private sector. Support schemes such as guarantees or recapitalization schemes could be cleared by the Commission very quickly if they fulfilled conditions which guarantee that they are well-targeted and proportionate to the objective of stabilizing financial markets and contain certain safeguards against unnecessary negative effects on competition. The specific conditions included:

- Non-discriminatory access in order to protect the functioning of the Single Market by making sure that eligibility for a support scheme is not based on nationality.
- State commitments to be limited in time in such a way that it is ensured that support can be provided as long as it is necessary to cope with the current turmoil in financial markets but will be reviewed and adjusted or terminated as soon as improved market conditions so permit.
- State support to be clearly defined and limited in scope to what is necessary to address the acute crisis in financial markets while excluding unjustified benefits for shareholders of financial institutions at the taxpayer’s expense.
- An appropriate contribution of the private sector by way of an adequate remuneration for the introduction of general support schemes (such as a guarantee scheme) and the coverage by the private sector of at least a significant part of the cost of assistance granted.
- Sufficient behavioral rules for beneficiaries that prevent an abuse of state support, like for example expansion and aggressive market strategies on the back of a state guarantee.
- An appropriate follow-up by structural adjustment measures for the financial sector as a whole and/or by restructuring individual financial institutions that had to rely on state intervention.8

At the same time, the measures distinguished between banks that are fundamentally sound and receive temporary support to enhance the stability of financial markets and foster undisturbed access to credit for citizens and companies on the one hand, and distressed banks whose business model has brought about a risk of insolvency on the other hand. State support for distressed banks implies a greater risk of competition distortions, therefore safeguards must be stricter and a thorough restructuring is necessary.

In particular, the guidance established principles for the pricing of state capital injections into fundamentally sound banks based on base rates set by central banks to which a risk premium was added that has to reflect the risk profile of each beneficiary bank, the type of capital used and the level of safeguards accompanying the recapitalization to avoid abuse of the public funding. Riskier banks will have to pay a higher rate of remuneration. The pricing mechanism needed to carry a sufficient incentive to keep the duration of state involvement to a minimum, for example through a remuneration rate that increases over time.

Banks in distress that faced a risk of insolvency should in principle be required to pay more for state support and to observe stricter safeguards. The use of state capital for such banks can be accepted only on the condition of a far-reaching restructuring restoring their long-term viability, including where appropriate a change in management and in corporate governance.

Member States had the possibility of creating schemes for recapitalization that are open to all banks if the rate of remuneration is set at a predetermined level which ensures an appropriate overall return over time.9
The design of the asset relief schemes, be it asset purchase, insurance, swap, guarantee or hybrid models had to observe several principles as well:  

- full transparency and disclosure of impairments, which had to be done prior to government intervention;  
- coordinated approach to the identification of assets eligible for asset relief measures through development of eligible categories of assets ("baskets");  
- coordinated approach to valuation of assets ex-ante, based on common principles such as valuation based on real economic value (rather than market value), implemented by independent experts and certified by bank supervisors,  
- validation by the Commission of the valuation of the assets, in the framework of the State aid procedures on the basis of uniform assessment criteria;  
- adequate burden-sharing of the costs related to impaired asset between the shareholders, the creditors and the State;  
- adequate remuneration for the State, at least equivalent to the remuneration of State capital;  
- coverage of the losses incurred from the valuation of the assets at real-economic-value by the bank benefiting from the scheme;  
- aligning incentives for banks to participate in asset relief with public policy objectives, through an enrolment window limited to six months during which the banks would be able to come forward with impaired assets;  
- management of assets subject to relief so as to avoid conflicts of interests;  
- appropriate restructuring including measures to remedy competition distortion, following a case by case assessment and taking into account the total aid received through recapitalization, guarantees or asset relief, with a view to the long-term viability and normal functioning of the European banking industry.

After addressing the problems in the financial sector, the Commission targeted the ‘real’ economy as well, by temporarily relaxing existing state aid conditionalities. The aim was to ensure sufficient bank lending to companies, to allow companies with liquidity problems due to the crisis to benefit from temporary relief through a limited grant and to encourage companies to continue investing into a sustainable future, including the development of green products. The measures that the Member States could grant to companies had in view:

- a lump sum of aid up to €500,000 per company for the next two years, to relieve them from current difficulties;  
- state guarantees for loans at a reduced premium;  
- subsidized loans, in particular for the production of green products (meeting environmental protection standards early or going beyond such standards);  
- risk capital aid up to €2.5 million per SME per year (instead of the current €1.5 million) in cases where at least 30% (instead of the current 50%) of the investment cost comes from private investors.

Under the existing state aid control rules, companies which got an initial rescue aid were obliged to present a restructuring/liquidation plan in a period of six months. For the financial sector, this was limited to distressed banks, i.e. banks that, in particular, received support above 2% of their risk-weighed assets. As a result, the Commission explained, in July 2009, its approach to assessing restructuring aid given by Member States to banks. The approach was based on three fundamental principles: i) aided banks must be made viable in the long term without further state support, ii) aided banks and their owners must carry a fair burden of the restructuring costs and iii) measures must be taken to limit distortions of competition in the Single Market. As a result, banks had to stress test their business. This required a diagnosis of the bank’s strengths and weaknesses, which may lead to revisiting the business model of the bank, disclosing and dealing with impaired assets, withdrawing from loss making activities or even considering absorption by
a viable competitor or orderly winding up. This approach made clear that aided banks and their capital holders must bear adequate responsibility for their past behavior and contribute to the restructuring of the bank as much as possible with their own resources. This required in particular that the state is correctly remunerated for the aid it gives. Where this is not possible immediately due to market circumstances, such burden-sharing will be required at a later stage. Measures to limit distortions of competition resulting from the state aid to banks have also been included. Such distortions were perceived to come from prolonging the bank’s inadequate or excessively risky past behavior and/or from maintaining its market presence to the detriment of competitors. Large state support may require some adjustments including structural measures, such as divestitures (which can be spread over a number of years in the current crisis), or behavioral measures, such as constraints on acquisitions or on aggressive pricing and marketing strategies funded by state aid.12

Finally, at the end of 2010, the European Commission has agreed to prolong into 2011 its state aid crisis framework subject to modified conditions to continue with a gradual phasing-out.13 The Temporary Framework to support businesses access to finance maintained those measures that address ongoing market failures. But firms in difficulty have been excluded from the scope of the Temporary Framework to ensure an appropriate restructuring of the economy.

As to the financial sector, starting with 1st January 2011, every bank requiring state support in the form of capital or impaired asset measures had to submit a restructuring plan (and not only those which received support above 2% of their risk-weighted assets). On the other hand, the prolonged Temporary Framework maintained several measures facilitating the access to finance, especially for SMEs, i.e. subsidized state guarantees and subsidized loans, inter alia for green products. In these areas, the market was considered not yet able to entirely meet small companies’ financing needs. The introduction of stricter conditions for those measures was thought to facilitate a gradual return to normal state aid rules while limiting the impact of their prolonged application on competition. This included that for large firms working capital loans were excluded from the application of the Temporary Framework and that firms in difficulty can no longer benefit from the Framework.

ENFORCEMENT RESULTS

According to data from European Commission, between 2008 and September 2010, €4,588.9 billion of aid was made available to financial institutions. However, the amount of public support actually used in 2009 was much lower and stood at € 1,106.6 billion. For 2008, it was € 957 billion.

| Table 2. Maximum approved crisis-related amount of aid to the financial sector |
|---------------------------------|-----------------|
| **Schemes**                     | **Approved value 2008-2010** |
| for guarantees                  | 3,478.96        |
| for recapitalization measures   | 3026.28         |
| for asset relief interventions  | 348.64          |
| for liquidity measures other than guarantee schemes | 62.17 |
| **Ad hoc interventions in favor of individual financial institutions** | 41.87 |
| for guarantees                  | 1109.94         |
| for recapitalization measures   | 458.97          |
| for asset relief interventions  | 197.44          |
| for liquidity measures other than guarantee schemes | 339.63 |
| **TOTAL**                       | 4588.90         |

Source: European Commission.
The bulk (76%) of this support came in the form of State loans or guarantees to maintain interbank financing which would only have an impact on public finances, if they were called upon, whereas recapitalization represents 12% and impaired asset relief 9%. Excluding the crisis-related support, total aid remained relatively stable at €d continued to re-focus on less distortive horizontal objectives such as aid for research and innovation, protection of the environment and support to SMEs.\textsuperscript{14}

Obviously, there are large differences between countries. Almost 90% of the approved amounts have been registered in 8 countries, representing most of the largest and richest Member States of the European Union. On the other hand, 5 countries did not make any decision to support the financial sector: Bulgaria, Czech Republic, Estonia, Malta and Romania. Their banking sectors were probably less sophisticated and, as a result, did not get involved in the kind of financial operations that created so much trouble in the current crisis. However, one question remains unanswered: would several of these countries have the financial resources to intervene if their banks were in trouble? The answer is not difficult to imagine, if someone would compare the size of Romania’s GDP, for instance (a little bit above 100 billion Euros), with the amount of money made available by the 8 above mentioned countries (around 4 trillion Euros). The approved amounts have been huge, but they have not been unlimited and discrimination between national banks and foreign banks has been avoided due to the control of the European Commission (Nicolaides and Rusu, 2010).

<table>
<thead>
<tr>
<th>Country</th>
<th>No. of measures</th>
<th>Type of measures</th>
<th>Approved amounts 2008-2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>United Kingdom</td>
<td>9</td>
<td>Rescue aid, guarantees, recapitalization, working capital guarantee scheme, restructuring, impaired asset relief, liquidation aid</td>
<td>850.30</td>
</tr>
<tr>
<td>Ireland</td>
<td>19</td>
<td>Guarantees, recapitalization, impaired assets relief scheme, rescue, restructuring</td>
<td>723.31</td>
</tr>
<tr>
<td>Denmark</td>
<td>7</td>
<td>Rescue aid, liquidation aid, guarantees, recapitalization, fund for winding up of banks</td>
<td>599.66</td>
</tr>
<tr>
<td>Germany</td>
<td>25</td>
<td>Restructuring aid, rescue aid, guarantees, recapitalization, capital injection, asset relief scheme, refinancing of export credits</td>
<td>592.23</td>
</tr>
<tr>
<td>France</td>
<td>3</td>
<td>Refinancing, recapitalization, capital injection</td>
<td>351.10</td>
</tr>
<tr>
<td>Spain</td>
<td>5</td>
<td>Fund for acquisition of financial assets, guarantee scheme, restructuring aid, recapitalization scheme</td>
<td>334.27</td>
</tr>
<tr>
<td>Belgium</td>
<td>12</td>
<td>Guarantees, restructuring, capital injections, asset relief</td>
<td>328.59</td>
</tr>
<tr>
<td>Netherlands</td>
<td>11</td>
<td>Guarantees, capital injection, illiquid assets facilities, restructuring, recapitalization</td>
<td>323.60</td>
</tr>
<tr>
<td>Sweden</td>
<td>4</td>
<td>Guarantees, rescue aid, recapitalization, restructuring aid</td>
<td>161.56</td>
</tr>
<tr>
<td>Austria</td>
<td>6</td>
<td>Guarantees, recapitalization, restructuring</td>
<td>91.70</td>
</tr>
<tr>
<td>Greece</td>
<td>2</td>
<td>Guarantees, recapitalization</td>
<td>78.00</td>
</tr>
<tr>
<td>Finland</td>
<td>3</td>
<td>Capital injections, guarantee scheme</td>
<td>54.00</td>
</tr>
<tr>
<td>Portugal</td>
<td>4</td>
<td>Guarantee, recapitalization, recovery of illegal state aid (Banco Privado Portugues)</td>
<td>20.45</td>
</tr>
<tr>
<td>Italy</td>
<td>2</td>
<td>Guarantees, recapitalization</td>
<td>20.00</td>
</tr>
<tr>
<td>Slovenia</td>
<td>3</td>
<td>Guarantee scheme, liquidity scheme, rescue recapitalization</td>
<td>12.00</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>1</td>
<td>Restructuring aid</td>
<td>11.59</td>
</tr>
<tr>
<td>Hungary</td>
<td>3</td>
<td>Guarantees, recapitalization, mortgage support scheme, liquidity support scheme</td>
<td>10.33</td>
</tr>
</tbody>
</table>
The case of Banco Privado Portugues (BPP) is an interesting one. BPP received a state-guaranteed loan of 450 million Euros from six other banks in December 2008. Initially, the Commission approved the loan as a rescue aid on the condition that a restructuring plan of the bank will be presented in six months. As the plan was not presented and the Bank of Portugal initiated the liquidation procedure for BPP, the Commission decided that the aid was illegal and incompatible with the Single Market. As a result, Portugal has to recover from BPP the loan that it repaid to the creditors in execution of the guarantee plus the difference between the price the bank should have paid for the guarantee and the lower fee actually paid, including accrued interest.15

The next figure shows the share of state aid in the GDP of the European Union. There is a clear decreasing trend in the state aid when not including crisis measures and the level is quite low (less than 1%). However, when crisis measures are included, the level rises abruptly to more than 3.5% of GDP.

![Figure 1. State Aid in EU](image)

Companies in the ‘real’ economy benefitted from the provisions of the Temporary Framework, which involved an increased de minimis aid (from €200,000 to €500,000), state guarantees at a reduced premium rate, subsidized loans or an increase in the size of risk-capital aid.

**CONCLUSIONS AND RECOMMENDATIONS**

There were three options regarding the EU rules on state aid control for the financial sector and for the ‘real’ economy in the context of the crisis: (i) relinquish; (ii) not to change and (iii) temporarily relax them.

There is quite a consensus regarding the correct approach of the European Commission when temporarily relaxing the rules, mainly for the banking sector. The European Commission has been praised for taking a series of swift decisions granting survival packages to distressed financial institutions while insisting, first, that they be devised in the least distortive way; second, that their features be sufficiently consistent so as to preserve a level-playing field throughout
the European market; and, third, that the aid granted be monitored and reimbursed as soon as market conditions allowed for the distressed institution’s recovery (Lasserre, 2011).

It was a pragmatic decision to adapt state aid rules to the new circumstances, instead of completely putting them aside for the time of the crisis. A more restrictive approach and a rigorous application of the state aid rules would have prevented Member States from acting quickly and, therefore, would have led Member States to ignore them (Jaeger, 2010). In other words, decision-makers didn’t forget the potential negative long-term effects on social welfare and and resisted to renounce to state aid control rules in order to avoid short-term costs.

State aid policy has played an important role during the financial crisis. It has allowed Member States to support, initially, financial institutions and then the real economy, while at the same time striving to prevent excessive distortion to competition and disruption to the flow of resources between Member States. Putting aside the rules in this area would have raised enormous problems during the period after the crisis, in which Member States will return to the original regime of state aid (Nicolaides and Rusu, 2010).

However, there have been huge differences between countries as regards the size of the aid. Nobody can say at this moment that distortions of competition have been kept to the minimum. However, when speaking about state aids, we are referring to national and not to European money. Therefore, these differences reflect the disparities between the financial strength of the countries and they are not the result of the legal framework. On the contrary, the existing rules put a cap on the size of the aid, making it not to be unlimited. Therefore, in our opinion, countries lacking strong financial resources, like Romania, should always be in favor of maintaining the existing framework for state aid control in European Union.

Finally, a comment about the current debate on microeconomic theories. There are many voices arguing that the theory of free markets and their self-regulation has been discredited. In our opinion, the current crisis has been generated by weaknesses in the system of regulating and supervising the financial sector and not in the functioning of “real” economy. So, microeconomic theories continue to be valid, but their conclusions should be better enforced. Therefore, changes are necessary in the monitoring of the banking sector in order to avoid the danger of having to deal with a “too big to fail” financial sector and are not necessary in the current international mechanism of protection of competition. And, in a globalized world and an inter-twinned financial system, changes should be made globally, through an intense co-operation between countries.

REFERENCES


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PROFESSIONAL LEadership AND PERSONAL FLEXIBILITY:
THE ROMANIAN CHALLENGE

Melvyn L. Fein, Ph.D.
Kennesaw State University, S.U.A. (2011)

Abstract: Romania provides an interesting example of the transition from a command economy to a market-based one. This has presented serious challenges to those who hope to lead this change. If they are to be successful, they must become more professionalized than was permitted under the former regime. In order to achieve this, however, they must become “self-motivated experts” in leadership, who cultivate emotional maturity, self-knowledge, other-knowledge, and negotiation skills. While these attributes were discouraged by the coercive tactics of the communist era, only if they are sufficiently developed can future leaders flexibly overcome the obstacles thrown up by their past.

THE CENTRALIZED PRECURSOR

As we move toward a more extensively techno-commercial world, the challenges become more professionalized in nature. This is true of all societies that strive to be economically advanced, but it presents a greater challenge where market-based institutions have been suppressed. This includes nations such as Romania that have only recently emerged from under Soviet domination. As they seek greater freedom and prosperity, their citizens must make difficult commercial and communal adjustments. This is especially so for those who provide leadership.

During the first part of the twentieth century it was assumed that centralized command structures were more efficient than decentralized ones. Thinkers such as Max Weber and Fredrick Taylor argued that bureaucracy and scientific management held the keys to greater productivity. By placing responsibility at the apex of organizations, the resultant strategies would be more rational. Because the people at the top were more talented, but had broader views of what was required, they made the best planners. It was therefore up to their subordinates to follow their directions. Only this would ensure that the appropriate products were produced with the least waste of time or resources.

In fact, experience has proved otherwise. In command economies, whether on the national or organizational level, over-centralization has been disastrous. Most noticeably in places influenced by communist ideology, it has led to economic stagnation and political despotism. In the absence of market forces and lower-level discretion, foolish choices have been made, and enforced, despite evidence that they were not generating the expected results. Moreover, far from the best and the brightest making the soundest judgments, power, not expertise, dominated the planning process.

As if this were not bad enough, in places like Romania the failure of these strategies left a residue behind. Instead of people being able to discard the old and substitute the new, they have been handicapped by sterile habits that linger on. Rather than act with the boldness and collegiality that decentralization requires, their psyches continue to respond to threats grounded in the past. Instead of becoming “self-motivated experts” who can take initiative and rebound from mistakes, many have yet to acquire the personal qualities needed for self-direction and mutually respectful collaboration.
THE PROFESSIONALIZED PARADIGM

Historically professionalism was restricted to a few occupations. Physicians, lawyers, and clergymen formed its core. Indeed, they were thought to possess a divine calling. As such, they were regarded as special. Only a relatively few persons qualified, and, in the case of physicians and attorneys, were allowed to supervise their own activities.

Ordinary persons, on the other hand, were thought lazy. They conformed to Douglas Macgregor's Theory X, which held that rigorous management was required to keep a majority of them productive. Theory X is usually associated with capitalism. It has been argued that only market-based economies exploit workers. In contrast, because socialist ownership is widely dispersed, everyone is thought motivated to work harder. In fact, actual command economies lodge discretion in party apparatchiks, not ordinary workers. The latter are treated as industrial tools to be manipulated at the discretion of their superiors. As a consequence, during the heyday of communism, they joked that they pretended to work, while their bosses pretended to pay them.

A professionalized paradigm, in contrast, distributes responsibility into many more hands. It assumes that a far larger number of workers are capable of self-motivated expertise. Not just bosses, managers, or traditional professionals, but nurses, police officers, accountants, salespersons, machine operators, construction workers, and bus drivers are all believed capable of making competent decisions. Often aware of things their bosses are not, if permitted to make necessary adjustments, they both prevent mistakes and promote efficiency.

This is also true of lower level managers. In advanced industrial nations, such as the United States, upwards of ten percent of all employees have managerial responsibilities. The nature of the work performed is frequently so complex that its effective coordination requires local supervision. This must therefore be exercised with intelligence and flexibility. To achieve this, local leaders must be self-directed. They must be the kinds of persons who are skilled at making decisions and who are personally motivated to make them. If not, they are apt to wait for someone else to tell them what to do, with the consequence that things go terribly wrong.

If the above is true, professionalized managers have become more valuable than previously. No longer will a peasant or proletarian mentality do because those geared to doing stereotyped jobs in a stereotyped manner cannot possibly keep up with accelerating changes.

THE CHALLENGES OF PROFESSIONALIZED LEADERSHIP

Professionalized leadership is not easy. Being a “self-motivated expert” in guiding others requires more than vaunted ambition. It also requires technical skills. Less well understood, however, are the personal aspects of professionalized leadership. To be self-motivated in directing others entails more than a desire for power. What is needed as well is an ability to inspire teamwork. Effective leaders know how to stir others to action. They are able to recognize the abilities others bring to the endeavor and know how to encourage them to apply these.

Professionalized leaders must likewise fine-tune their interventions. Put another way, they must be flexible and responsive. As circumstances change, they must be able to modify their input to fit the new conditions. If they cannot, they will make unnecessary mistakes. This puts a premium on personal flexibility. It is what enables leaders to keep up with fast-moving events. Rigidity, in contrast, quickly reaches its expiration date.

A self-motivated expertise therefore implies flexibility. Nevertheless, personal flexibility does not come easily to everyone. It is especially difficult for individuals socialized in rigid politico-economic institutions. Initiative having been discouraged because it was dangerous, they feel more secure when refusing to take risks. This has been so in the former Soviet Union, where modernization has been gradual and incomplete. It is less so in Romania because its command economy was imposed from the outside. Nonetheless the scars of social coercion do not heal easily. They continue to make themselves felt in the personal lives of individuals whose conscious aspirations are stymied by impulses they neither perceive nor understand.
Among the largely unrecognized areas relevant for developing professional flexibility are: 1) emotional maturity, 2) self knowledge, 3) other knowledge, and 4) negotiation skills. None of these, however, is acquired by memorizing textbook formulae. All require a personal emersion in change processes that can be difficult for those unfamiliar with them.

**EMOTIONAL MATURITY**

We humans are emotional creatures. Our feelings are important tools for achieving personal and interpersonal goals. Nevertheless, if improperly utilized, they can betray us. In order to be functional, they must be socialized. They need to be tamed in a manner that enables them to succeed. Daniel Goleman referred to this capacity as EQ, i.e., as an “emotional quotient.” He argues that while IQ can get people jobs, it is EQ that enables them to succeed.

Another way to interpret this capacity is as “emotional maturity.” We are all born with a capacity to feel emotions. Nevertheless childhood affects must be modified as we become adults. If they are not, their intensity tends to be misplaced. Thus, anger becomes rage and fear becomes terror. As most people know, angry children frequently throw tantrums. They strike out at those who frustrate them. In this, they are apt to alienate the very persons from whom they seek aid. As a result, instead of achieving what they desire, they initiate unconstructive conflicts.

Unsocialized fear has similarly dire consequences. Fear helps us deal with dangers. It does this by initiating a fight/flight response. In this, we either run away from a threat or stand and attempt to overcome it. Unfortunately when fear is very intense, these reactions produce panic. Terrified people run into the arms of greater dangers, while if they turn to face a threat, fight back with blind violence. Thus, rather than plan adequate defensive strategies, they impulsively lash out in a manner that makes them more vulnerable. It is therefore imperative that children learn how to handle their fears.

Sadly, in societies that have endured political and economic repression extensive coercion tends to generate fear and anger. Regimes that punish people for exercising initiative intentionally produce fear. One of their chief means of seeking compliance is intimidation. If they can frighten people into running away, they will not have deal with their resistance. Or if subordinates stand and fight, they do so in a disorganized and injudicious manner that is easily defeated. Repression similarly generates anger. Yet unsocialized anger is equally debilitating. People who are childishly enraged do not calculate how best to overcome their frustrations. Apt to plunge straight ahead irrespective of the odds, they too are more effortlessly vanquished.

In nations, such as Romania, with long histories of violence and repression, stable emotional responses are less likely to have been broadly inculcated. The upshot is that emotional insecurities instilled over millennia tend to discourage emotional maturity. Many people learn that it is better not to take chances than court destruction. This attitude is passed down from parent to child such that ordinary individuals become cautious. Unsure of the consequences of too much audacity, they keep novel ideas to themselves. Nor do people trust those outside their family circles. Rather than open themselves to betrayal, they do not organize the sorts of alliances necessary for large-scale projects.

So what is to done? The first thing to realize is that Romanians, as a people, are no more immature than others. What we are dealing with here is a cultural artifact that generates its behavioral equivalent. The accumulated fears and rages of generations past create social responses that mimic personal insecurities. Unfortunately, national memories can be very long. Too many tragedies produce a shared vigilance that warns against too much boldness.

What then are potential leaders to do? How are they to achieve the emotional flexibility necessary to take calculated risks? First, they must understand their own impulses, as fashioned by social factors over which they had limited control. Nonetheless, most of us do not brood over personal feelings. We do not so much analyze as experience them. Still, those whose impulses are out of synch with their opportunities have to be introspective. They need to be in tune with
their fears and disappointments. Only in this way can they judge whether apparent dangers are as perilous as they seem.

All this is made more difficult by the fact that emotions are not as malleable as cognitive thoughts. Fears do not disappear just because dangers fade. They tend to hang on until we are completely certain that a menace has departed forever. Until that happens – which can take years – deep-seated trepidations linger.

Anger too tends to be persistent. Even after we ostensibly achieve our desires, it can motivate punitive responses. Intense anger is blind, which means that it does not always realize it has accomplished its mission. Sometimes years go by before a deep-seated fury subsides. In the meantime, it can prompt us to treat friends as if they were enemies and enemies as friends.

The fundamental secret to emotional maturity is thus time. It takes time to adjust to feelings that are too strong to be easily controlled. If this sounds tangential to the concerns of professionalized leaders, it must be remembered that the most important instrument managers have is themselves. If they are to be the sorts of person others follow, they must begin here.

The second key to personal flexibility is self-knowledge. Since at least the ancient Greeks, people have been advised to know themselves. Indeed, doing so has been described as the beginning of wisdom. This is because an awareness of who we are is the starting point for our interactions with others. Whether we are leading or following, competing or cooperating, reciprocal relationships commence with ourselves. This means that whether we win or lose depends on how we compare with others. More specifically how do our strengths and weaknesses stack up against theirs? This often determines how we will work together and if our collaboration will be successful.

Most people realize that self-assessments can be difficult. In part, this is because many of us are uncomfortable admitting our limitations. While we are cognizant of our imperfections, we fear that our weaknesses are so substantial as to preclude significant social accomplishments. As a result, we frequently fool ourselves about our liabilities. These may be suppressed much as we censor uncomfortable emotions. Nevertheless, no matter how successful our denials, these restrictions influence the outcomes of our actions. They do not disappear merely because we divert our attention. This difficulty comes to the fore when we decide how to apply our abilities. If we choose to pursue directions where we are weak, we are less likely to succeed than if we concentrate on areas where we are strong. This makes it imperative to be honest with ourselves. To do otherwise is nothing less than a form of self-sabotage.

Looking our weaknesses in the face, however, takes courage. It requires the realization that even though we have them, this does not preclude genuine strong points. Indeed, because many of us secretly fear that others will out-do us, we keep our failings under wraps. This makes sense in the public arena where advertising one’s limitations invites exploitation. It makes less sense when privately evaluating our assets. It must also be remembered that others are engaging in impression management. Because they too have weaknesses they choose to conceal, we may, in fact, compare more favorably than we suppose.

This said, an even greater problem is incorrectly appraising one’s strengths. It might be supposed that most of us inflate our assets so as to balance our weaknesses, but this is often not the case. Frequently our strengths frighten us as much as our disabilities. This is so because they too can get us in trouble. If our weaknesses tempt others to exploit us, our strengths scare some into launching preemptive attacks. Because they too want to be winners, they hope to disable us before our assets overshadow theirs.

This tendency is particularly important when people have been subjected to coercive environments. Clearly, the more oppressive the circumstances, the more rational to conceal one’s abilities. This is surely the situation under repressive political and economic conditions. Now that
the Romanian revolution is two decades old, people can look back and recognize that this was
the way of things under the communist regime. Because many of those in power were far from
the best and brightest, those with greater abilities threatened them. Thus, talented people –
frequently intellectuals – bore the brunt of their despotic tactics.

The response to such potential subjugation is often to keep one’s strengths private. Yet
these must be recognized just as much as one’s weaknesses. If personal limitations are to be
avoided when making tactical decisions, strengths need to be utilized because they can provide
an edge both in competing and cooperating with others.

Among the personal factors that must also be understood are our innermost motiva-
tions. Not everyone wants the same things. Yes, we all share some basic needs. Thus, we all require
food, clothing, and shelter. Even so, while some people want to become rich, others do not. Likewise some crave social attention, whereas others shun it. Much of this has to do with our
temperamental differences, but a great deal is determined by how we were raised.

In the case of Romania, having survived repression, the foremost goal of many individ uals
is to ensure that they endure its revival. If so, this underlying motive colors their personal de-
cisions in a host of situations. This includes potential leaders. They too once had to find ways to
avoid serious harm. As a consequence, as long as they remain unaware of the springs of their
action, they may make commercial and administrative decisions that have little to do with
achieving success in here-and-now dealings.

KNOWLEDGE OF OTHERS

As noted above, working with people is an interactive process. Would-be leaders must
understand that they are immersed in a sea of divergent humanity. If they hope to lead others in
flourishing enterprises, they must be flexible enough to modify their understandings of them.
Genuinely professionalized managers must be motivated to look into the souls of individuals
different from themselves. Despite our common humanity, people are not alike in every respect.
To be expert in dealing with them therefore requires an ability to make accurate distinctions. Only
this can enable someone in a position of leadership to recognize the strengths others bring to the
table, as well as what is needed to motivate them to do a good job.

Just as is the case with the self, understanding others begins with correctly assessing
their strengths and weaknesses. It also requires insights into their personal and cultural motives.
And yet to assess these properly, it is crucial to realize they may be quite complex. Not only are
individual lives enormously complicated, so are our shared cultural histories. So many things
happen to us individually and collectively, that it is foolish to suppose we all respond the same
way. This belief, however, this is one of the legacies of communist ideology. It is based on a social
psychology that may generously be described as naïve. The notion that all members of the
bourgeoisie are infinitely corrupt is a fantasy. Likewise, dismissing them as parasites is political
nonsense easily disproved by the greater productivity of capitalist societies.

Equally fatuous are depictions of proletarians as public-spirited individuals uniformly
oppressed by their masters. Marxist theoreticians sincerely believe that government ownership of
the means of production will eliminate selfish impulses. In the end, not only will the state wither
away, but ordinary workers will produce according to their abilities and take only in accord with
their needs. Rewarding people for their efforts will therefore be unnecessary, as will discouraging
greed. Except that experience demonstrates this is a fantasy.

By the same token, portraying those who organize communal efforts under collectivist
regimes as relentlessly rational technocrats is to be blind to the actualities. Much as in other so-
cieties, those who aspire to social power in socialist governments tend to be ambitious. Many so
want to acquire power that they resort to unfair strategies to get it. But in so doing, common
sense is frequently jettisoned.
One of the most important tasks of leaders is to delegate responsibilities. No one, no matter how smart, can know everything. Nor can the most energetic of bosses be everywhere. Other people must consequently be depended upon to shoulder part of the load. Except not everyone is equally capable of performing every task. Talents and ambitions are not uniformly distributed. It is therefore essential to make distinctions.

Even devotees of Taylorism (i.e., scientific management) perceived a need to match individual abilities to specific responsibilities. This is why they placed so much faith in psychological and vocational testing. But differentiating between individuals is frequently a personal activity. Good leaders must therefore also be good judges of character and ability.

Some contemporary social theorists condemn being judgmental as immoral. They instead recommend unconditional positive regard. This, however, is patent gibberish. Quite the contrary, professionalized leaders must make accurate judgments and provide individualized support. Both the good and the bad must be recognized for what they are. Effective leaders cannot, in the manner of orthodox Marxists, divide humanity into heroes and villains. They require more subtle and contextualized appraisals. They also require more compassion. Limitations must be accepted, not rationalized. People must be allowed their foibles, while simultaneously being encouraged to overcome them.

**NEgotiation Skills**

To repeat an essential point, professionalized leaders work *with* people. This may sound obvious, but it must be distinguished from working *on* people. In the past – certainly before the human relations model became prominent – it was assumed that managers operated in an impersonal environment. They simply made appropriate decisions and then imposed them on others. This was conceived of as an emotionally detached and supremely rational activity. The goal was to be objectively accurate so as to be optimally efficient.

This sort of dispassionate methodology has been associated with corporate capitalism, but is even more appropriate to understanding command economies. While business owners applied efficiency experts to increase profits, centralized planners sought to be even more efficient in their choices. They assumed that if they calculated all of the variables operative in an economy, they would arrive at an equation that optimized the available resources – including the human ones. They would then issue directives that if followed would result a higher standards of living for everyone. In this, the technocrats would control production, but because they were controlled by facts and logic, everyone would be freed of human despotism.

If this depiction is accurate, then theoretically, at least, Marxist-style economic and political centralization was intended to be rational. Marx, it must be remembered, regarded himself as a scientific socialist. He was convinced his investigations discovered the inevitable trajectory of human history. Industrial societies would eventually be organized as he predicted because there was no reasonable alternative. It was therefore up to the communist cadre to facilitate the transition first to socialism and then communism.

Reality, however, has been different. The early Marxists assumed that resistance to their vision would come from greedy capitalists, but once they were removed, there would be smooth sailing. Workers would embrace the new system and cooperate in establishing it. This, unfortunately, is not what transpired.

Whatever the original intent, in places like Russia and Romania, the mass of citizens were operated on rather than cooperated with. They were told where to work, what methods to use, and which quotas to fulfill. This was not a matter of discussion. Since the experts knew best, others were required to comply – or else. There was, in short, no place for social negotiations. Input from below was not appreciated; hence economic and political leaders did not have to worry about what their subordinates thought. If the latter disagreed with their plans, this did not matter. It was the job of underlings to do as expected. If adjustments had to be made, this was to be
from above, not below.

Nevertheless this sort of intransigent pseudo-rationality proved singularly ineffective. Command economies have not been efficient. The volume and quality of goods produced have been inferior and the level of innovation mediocre. Amazingly, much of what was achieved borrowed heavily from capitalist competitors. Western inventions and techniques were painstakingly copied. Moreover, because interpersonal adjustments were discouraged, these tended to be avoided. A great deal of ingenuity pervaded the system, but this was primarily applied to working around the prescribed arrangements.

Of course, negotiations did exist within socialist regimes. The top leaders clearly made bargains amongst themselves. Nevertheless, they had to do so with care lest a misstep result in political oblivion. This precipitated massive deception and corruption. Far from honest negotiations in which give and take produced solutions from which everyone benefited, meticulously prescribed formulae had to be respected – or at least appear to have been. If this meant that some solutions were off limits, the ensuing rigidities needed to be tolerated. Meanwhile, on a lower level, interpersonal negotiations also took place. But these were even more likely to be defensive. The central goal was to forestall the negative consequences of rampant coercion. If improved productivity occurred, this was a side effect. Of more importance was guarding against attacks by coworkers who were also gaming the system.

With this sort of legacy, formerly communist societies have seen the negotiation skills of ordinary people atrophy. Not surprisingly, those concerned with shielding their flanks care little about problem solving. Nor are they as intent on hammering out communal deals as achieving bargains geared to private needs. Neither is experimentation valued. Since the familiar and stereotyped are safer, these become the norm. For comparable reasons, it is wise to do business with well-known persons. Even in market economies the players develop trusted relationships, but when conditions are insecure these become vital. As a result, collaboration between strangers is difficult, which, in turn, limits personal and organizational options.

Plainly, when such habits become deeply entrenched, they increase the obstacles to taking advantage of opportunities. Worse still, because these leanings are emotionally internalized, they get handed down from one generation to the next. Youngsters born long after the old regime is dismantled find themselves as poorly prepared for flexible negotiations as their parents. Because the misgivings of their elders’ become their own, they too worry less about problem solving and more about protecting themselves.

If this is to change, there must be significant personal and social transformations. Effective negotiation skills must be sought and inculcated. But this is not the same as pursuing technical training. Because good bargains depend on who people are more than on what they know, would-be leaders must be prepared for personal makeovers. Furthermore, these must begin with emotional maturity, self-knowledge, and other – knowledge – hopefully on both sides of potential deals. The more widespread these personal attributes become the greater the chances suitable partnerships can develop. Likewise, the larger the number of persons engaged in personal growth, the more likely their reciprocal relationships will contribute to cultural changes that facilitate successful negotiation patterns.

Competent negotiation skills begin with an appreciation of the need to increase interpersonal trust. If people are to make mutually constructive deals, they must lower their guard so that they can honestly swap resources. Nevertheless, if they are mentally sound, they know cheating and coercion are possible. They will therefore want to be certain their collaborators are motivated to steer clear of both. Unfortunately, it takes time to establish a reputation for integrity. It takes even more time for individuals conditioned to anticipate duplicity to expect reliability from relative strangers. This generally occurs only after many instances of successful interactions. And as for a generalized cultural supposition of trustworthiness, it can take generations to evolve. Only after many individuals come to expect and provide dependability does this become a part of the social landscape.
Effective negotiating is often about problem solving. The objective is to figure out how what is exchanged can benefit both parties. Sometimes this requires creativity. Consequently, it is important to be flexible about what is traded and how. That which was not initially anticipated by the parties can hold the solution to knotty problems. Indeed, if they are open to suggestions, they may discover surprising answers. Success in this almost always demands cool heads. The point is to leave both parties in a better position than before. Only if this is so, will they be willing to make future deals. Similarly, if effective collaboration benefits both, they are more apt to function as allies. Successful leadership is not solely contingent upon one’s own attributes. Personal power is multiplied when it acts in concert with others. Because groups of individuals working cooperatively are almost always more potent than isolates, skill in assembling and influencing coalitions is frequently the key to success.

In the case of Romania, where the communist government did not appreciate independent initiative, these were unpracticed skills. Non-regime alliances were a threat and hence vigorously suppressed. Likewise, ideas originating from outside the dominant circles were discouraged. This meant that most people devoted more energy to staying out of trouble than to negotiating within emergent alliances. Or, if they joined the communist party, they kept their heads down. Most were not as concerned with innovative leadership as access to a reasonably comfortable lifestyle.

**THE ROMANIAN CHALLENGE**

There are many lessons to be learned from the Romanian experience. At the minimum, it indicates that not all potential leaders deal with the same issues. Opportunities take many shapes; sometimes coming in the form of greater obstacles. Remarkably, the efforts and insights needed to overcome these can provide an edge in competition with others who have become self-satisfied. This, however, is contingent on understanding the nature of one’s challenges and perceiving the potential avenues for surmounting them.

The most important Romanian advantage is its people and their ambitions. Even though there has been a brain drain of enormous proportions – with fully ten percent of the population having emigrated elsewhere – the level of education is fairly good. Traditionally, the nation had many world-class schools, and it still does, especially with respect to math and the sciences. But even more important are the attitudes of ordinary Romanians. Despite years, and some might say centuries, of hardship, they remain optimistic and open-spirited. Although a streak of passivity endures, given the communist legacy and the history of oppressed peasantry, this is expectable. The good news is that it can be overcome. Aspirations can be realized, albeit more slowly than many hoped. More people can become active innovators, but only as they gradually realize their dormant strengths. The past demonstrates that underdogs can rise to the top and Romania may provide another example. But much will depend on the leadership that emerges. If it is professionalized, if it is flexible enough to recognize and exploit emergent opportunities, there is not telling the directions that are possible.

**REFERENCES**

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