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# **CAPITALISM FROM BELOW: AN EXPLORATORY ANALYSIS OF SMALL ENTREPRENEURSHIP IN HUNGARY, POLAND, AND ROMANIA**

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## **ABSTRACT**

*The contours of markets and entrepreneurship are shaped by historical and politico-institutional factors. In the case of Central and Eastern Europe, the development of new entrepreneurial classes is a function of communist legacies and post-1989 political processes. Employing survey data from 2000, this article examines how political and institutional conditions influence patterns of recruitment into self-employment and income returns to small entrepreneurship in Hungary, Poland, and Romania. The results of this analysis show that human capital (captured by education) has positive significant effects on becoming a self-employed individual with employees in Hungary and Romania. As compared to other individuals, former socialist “petit bourgeois” (i.e., individuals who were business owners in 1988) are more likely to be small business operators in post-communism. Individuals who held managerial authority positions before 1989 have higher chances to become small business operators in Romania but not in Hungary or Poland. Unemployment seems to function as a push-factor for becoming a small business operator in Hungary and Poland but not in Romania. In Romania, most small entrepreneurs earn significantly more than employees in the state or private sector. Gender, age, and education have significant positive effects on income returns in all of the three countries under scrutiny.*

## **KEYWORDS**

- politics
- markets
- entrepreneurship
- post-communism
- Hungary
- Poland
- Romania

While all roads may lead to Rome, it seems that not all transitions from socialism have led to a Western-style, rational capitalism. Employing nationwide survey data, in this article I examine institutional and individual factors that regulate the rise of small entrepreneurship in Poland, Hungary, and Romania. Different forms of entrepreneurship – from large scale enterprises to small commerce – rely on combinations of different forms of capital, from financial resources to human capital to social capital or network resources.<sup>1</sup> For instance, having significant financial resources and expertise might matter more for starting a large business than for becoming a self-employed individual – an activity that has low entry barriers in terms of financial or human capital. In turn, as I will discuss in the following pages, the type of resources relevant for various forms of post-socialist entrepreneurship is a function of politico-institutional factors.

Against this backdrop, in this article I focus on the following questions: 1) What are the social origins of Polish, Hungarian, and Romanian small entrepreneurs?; 2) What roles do education, financial resources, and cultural capital (or market expertise) play for becoming a self-employed individual in these countries?; 3) What are the income returns to small entrepreneurship (self-employment) in Poland, Hungary, and Romania?

This study is organized as follows: In the first section I will discuss the theoretical arguments that are at the core of my analyses. In the second section, I will present the data and measures employed in this article. In the third section, I will discuss the socio-demographic profiles of small entrepreneurs in these countries, followed by causal-analyses of entry into entrepreneurship in the fourth section. I will then turn to cross-national analyses of income returns to small entrepreneurship. In the last section I will briefly review the main findings of this comparative inquiry.

## 1. Theoretical Background

Although previous sociological analyses have improved our understanding of post-socialism, as Walder<sup>2</sup> rightfully stresses, they have generated more controversy than theoretical convergence. This is because, I contend, many sociological studies in-

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<sup>1</sup> M Granovetter, “Entrepreneurship, Development and the Emergence of Firms”, Unpublished manuscript. Stanford University, Sociology Department, Stanford, 1989; M Granovetter, “The Economic Sociology of Firms and Entrepreneurs” in A Portes (ed.), *The Economic Sociology of Immigration: essays on networks, ethnicity, and entrepreneurship*, Russell Sage Foundation, New York, 1995, pp. 128-165; M Granovetter, “A Theoretical Agenda for Economic Sociology” in M Gullien, R Collins, P England, and M Meyer (eds), *The New Economic Sociology: Developments in an Emerging Field*, Russell Sage Foundation, New York, 2002, pp. 35-59; A Portes, “Social Capital: Its Origins and Applications in Modern Sociology”, *Annual Review of Sociology*, no. 24, 1998, pp. 1-24; A Róna-Tas, “Path Dependence and Capital Theory: Sociology of the Post-Communist Economic Transformation”, *East European Politics and Societies*, no.1, 1998, pp. 107 – 131; D Sandu, “Drumul antreprenorial: Fara incredere dar cu relatii” [The Entrepreneurial Way: Without Trust but with Connections] *Sociologie Românească* [Romanian Sociology], no. 2, 1999, pp. 123-142

<sup>2</sup> A Walder, “Elite Opportunity in Transitional Economies”, *American Sociological Review*, no. 4, 2003, pp. 899-916.

spired by Victor Nee's "market transition theory"<sup>3</sup> have neglected the political and historical aspects involved in the construction of markets in the former communist bloc.

My argument runs as follows: markets are politically shaped through elaborated rules and practices.<sup>4</sup> Consequently, the transition to a market economy depends on the successful creation of new (market-supporting) political and cultural institutions, and the suppression of other (non-market) institutional arrangements. The shaping of markets in post-socialist countries is likely to be influenced by two sets of factors: 1) *the political institutional histories of the communist regimes*; and 2) *the completeness of the political break with the communist past* (i.e., whether the former communists maintained their positions of power after the first free elections).

According to Marx's evolutionary model of history, capitalism would eventually lead to communism. Yet, in an ironical (for Marx) twist of history, whoever becomes a capitalist in Eastern Europe is heavily influenced by the communist past. Thus, I expect to find a more developed entrepreneurial class in countries that, *prior to 1990*, attempted to reform their socialist systems by formally allowing activities in the small, private sector, in the so-called "second economy". Following Lampland and Róna-Tas,<sup>5</sup> I use "second economy" to refer to economic activities organized outside the state sector and *legally* tolerated by socialist regimes. That is, in such countries (e.g. Hungary and Poland), post-socialist small entrepreneurship will be better developed (i.e., both its size and its contribution to the GDP will be greater) than in countries that did not implement reforms during communism.

<sup>3</sup> V Nee, "A Theory of Market Transition", *American Sociological Review*, vol. 54, 1989, pp. 663 – 681; V Nee, "Social Inequalities in Reforming State Socialism: Between Redistribution and Markets in China", *American Sociological Review*, vol.56, 1991, pp. 267 – 282. Nee's theory has stirred a vivid controversy, which culminated in the so-called "market transition debate" in *American Journal of Sociology* in 1996, vol. 101, no. 4. Contributions to the 1996 debate included A Oberschall "The Great Transition: China, Hungary, and Sociology Exit Socialism into the Market" pp. 1028-1041; N Fligstein, "The Economic Sociology of the Transitions from Socialism", pp. 1074-1081; D Stark, "Recombinant Property in East European Capitalism", pp. 993 -1027; I Szélenyi and E Kostello, "The Market Transition Debate: Towards a Synthesis?", pp. 1082 – 1086; A Walder, "Markets and Inequality in Transitional Economies: Towards Testable Theories." pp. 1060-73; V Nee, "The Emergence of Market Society: Changing Mechanisms of Stratification in China", pp. 908-949. Nee's subsequent contributions to this debate include V Nee and R. Matthews. "Market Transition and Societal Transformation in Reforming State Socialism", *Annual Review of Sociology*, no. 22, 1996, pp. 104-156; V Nee and Y Cao "Path Dependent Societal Transformation in Hybrid Mixed Economies", *Theory and Society*, vol. 28, 1999, pp. 799-834. The debate was revived again in 2001 in *American Journal of Sociology*; on this point, see G Eyal, I Szélenyi, and E Townsley, "The Utopia of Postsocialist Theory and the Ironic View of History in Neoclassical Sociology." Review symposium, *American Journal of Sociology (AJS)*, no. 4, 2001, pp. 1121-1128; J Böröcz "Change Rules" Review Symposium, *American Journal of Sociology*, no. 4, 2001, pp. 1152-1168, and other contributions in the same issue of AJS.

<sup>4</sup> K Polanyi, *The Great Transformation: The Political and Economic Origins of Our Time*, Beacon Press, Boston, [1944] 1957

<sup>5</sup> M Lampland, "Pigs, Party Secretaries, and Private Lives in Hungary", *American Ethnologist*, no. 3, 1991, pp. 459-479; A Róna-Tas, "Path Dependence and Capital Theory: Sociology of the Post-Communist Economic Transformation", *East European Politics and Societies*, no.1, 1998, pp. 107 – 131; A Róna-Tas, *The Great Surprise of the Small Transformation: The Demise of Communism and the Rise of the Private Sector in Hungary*, University of Michigan Press, Ann Arbor, 1997.

Secondly, the development of post-socialist entrepreneurship has also been influenced by the completeness of the political break with the past or by what Walder calls “the extensiveness of regime change,” i.e., “the degree to which, prior to or simultaneous with the market onset, Communist Party hierarchies lose their political monopoly and must compete with other organized entities for political power.”<sup>6</sup> Following Walder’s arguments, I contend that in countries that broke sharply with the past through the first free elections, (small) entrepreneurship acts as a foundation for market activities and economic growth. This is because in such countries most of the communist elites lost their posts and the new elites (usually communist-era oppositional forces or newly formed political groups) have implemented comprehensive political and economic reforms. This has also translated into creating institutional frameworks that reward human capital (i.e., education and adequate organizational skills) rather than political capital (i.e., ties to officialdom or membership in communist elite networks) in the newly emerging market economies.

Conversely, in countries that, prior to 1990, did not reform their communist systems and did not break sharply with the past after 1990 (i.e., where most former communists have maintained their posts after the first free elections), entrepreneurship will rely on a personalized logic and will aim at wealth via political protection (see also Gabanyi<sup>7</sup>). Instead of acting as a foundation for a market economy, entrepreneurship will be predatory, rent seeking rather than productive, and will hinder economic growth. Also, in such under-reformed countries (i.e., Romania), the size of the new private sector and its contribution to the GDP will be smaller than in former socialist countries with more reformist political histories.

As regards pre-1989 history, the openness to economic reforms and private businesses was a function of the type of political regime in each of these three countries. After Stalin’s death, the Polish and Hungarian communists changed their leadership-style from the “iron fist” to the “velvet glove.” In the late 1960s and early 1970s, this change of heart translated into several economic reforms and ideological relaxation. Similar reforms were adopted in Romania during the same period. Yet, while the Hungarian and Polish communists stayed (more or less) on the reformist path, the Romanian leadership reversed gears and, after 1971, it started to re-Stalinize the entire country.<sup>8</sup> Romania’s timid economic reforms from the late 1960s were abandoned and Ceausescu’s manner of ruling started to become more and more personalized and unchecked. At the same time (i.e., in the late 1970s and early 1980s), Hungary was openly experimenting with economic liberalization and Poland – despite some reformist attempts – was facing serious social and economic

<sup>6</sup> Walder, 2003, p.901.

<sup>7</sup> A Gabanyi, “The New Business Elite: From Nomenklatura to Oligarchy” in H. Carey (ed.), *Romania since 1989: Politics, Economics, and Society*, Lexington Books, Lanham, 2004, pp. 353-372.

<sup>8</sup> V Tismăneanu, *Reinventing Politics: Eastern Europe from Stalin to Havel*, The Free Press, New York, 1992; V. Tismăneanu, *Stalinism for All Seasons: A Political History of Romanian Communism*, University of California Press, Berkeley, 2003. Tismăneanu’s contributions to the history of Romanian communism are extremely numerous and he is by far the most authoritative voice on this issue.

problems, which culminated with Solidarity's open challenge to the communist regime in the late 1980s.

By the end of 1980s, there were fairly significant differences regarding the political and economic landscapes of these three countries. Politically, to employ Linz and Stepan's concepts,<sup>9</sup> socialist Poland and Hungary in 1988 were "mature post-totalitarian regimes." Yet, the degree of political pluralism and reforms within the party was higher in Hungary than in Poland. Regarding economic reforms, in Hungary the second economy was not only allowed but also encouraged<sup>10</sup> whereas in Poland it was merely tolerated.<sup>11</sup> Romania, on the other hand, was the closest to a totalitarian rule: it had an insignificant opposition and virtually no alternative or parallel (civil) society and a second economy.<sup>12</sup>

Like in other Central and Eastern European countries, Romania's communist regime eventually collapsed. Yet, Ceaușescu's legacies would prove difficult to overcome. In 1990 Romania lagged behind Hungary and Poland in several key economic aspects. Specifically, as compared to Hungary and Poland, Romania had an insignificant private sector, an oversized and non-performing industry, a lower degree of urbanization, higher inflation, and a smaller GDP per capita.<sup>13</sup> In contrast, Hungary, which in 1990 had the longest history of economic reforms in the region, had a relatively well developed service sector, a high degree of urbanization, and a higher GDP per capita. (Notably, in one area, Poland and Romania were comparable and even had an advantage vis-a-vis Hungary: both Poland and Romania were richer in natural resources than Hungary.)

Let us consider next the post-socialist histories of these countries: In both Poland and Hungary, anticommunist forces came to power as a result of the first free elections. Subsequently, these new political forces introduced comprehensive political and economic reforms (albeit in different forms, especially in regard to privatization policies – for a detailed analysis of these policies, see Stark and Bruszt<sup>14</sup>). In Romania, however, the second-tier communists won not only the first but also the second free elections, staying in power from 1990 until 1996. The second-tier communists' approach to political and economic reform was hesitant, fitting the "partial reform" paradigm.<sup>15</sup> That is, the former communists favored a gradualist

<sup>9</sup> J Linz & A. Stepan, *Problems of Democratic Transition and Consolidation: Southern Europe, South America, and Post-Communist Europe*, The Johns Hopkins University Press, Baltimore, 1996

<sup>10</sup> I Kemeny, "The Second Economy in Hungary" in M. Łoś (ed.), *The Second Economy in Marxist States*, Macmillan Press, 1990, London, 1990, pp. 50-68; Linz and Stepan, 1996.

<sup>11</sup> M Łoś, "The Dynamics of the Second Economy in Poland" Pp. 27-49 in M. Łoś (ed.), *The Second Economy in Marxist States*, Macmillan Press, 1990b, London, 1990b, pp. 27-49.

<sup>12</sup> Tismăneanu, 2003; H. Brezinski & P. Petersen, "The Second Economy in Romania" in M. Łoś (ed.), *The Second Economy in Marxist States*, Macmillan Press, 1990, London, 1990, pp. 69-84.

<sup>13</sup> M de Melo et al., "Circumstance and Choice: The Role of Initial Conditions and Policies in Transition Economies.", *World Bank Policy Research Working Paper*, World Bank, Washington, D.C., 1997.

<sup>14</sup> D Stark, & L. Bruszt, *Postsocialist Pathways: Transforming Politics and Property in East Central Europe*, Cambridge University Press, New York, 1998.

<sup>15</sup> T Frye, "The Perils of Polarization: Economic Performance in the Postcommunist World", *World Politics* no.

approach to reform. More importantly, they did so with little discipline (i.e., few if no hard budget constraints were put in place) and without public scrutiny.<sup>16</sup> This has allowed the deposed regime's insiders to gain the facto control over important economic resources<sup>17</sup>; once in control, such insiders have blocked further reforms which would have deprived them of their advantages or rental havens.

By the end of the first decade of political reforms, the World Bank classified Hungary and Poland as “competitive democracies” (i.e., regimes with high levels of civil and political rights). Romania, on the other hand, was among the so-called “concentrated regimes,” along with Russia, Bulgaria, Moldova, or Slovak Republic. Although having multiparty systems and free elections, such regimes have barriers to political participation of certain groups and have a rather haphazard attitude towards civil rights. (For an alternative classification of these regimes, see McFaul<sup>18</sup>.)

The post-1990 political histories of Hungary, Poland, and Romania have translated into different economic outcomes. All of these three countries have gone through economic recession after 1990. Yet, the severity of economic recession has varied significantly among these countries. According to the World Bank<sup>19</sup>, Poland had the shortest and mildest recession, while Romania had a much more serious recession. Specifically, Romania and Poland had 3 years of consecutive economic decline, while Hungary had 6 years. Furthermore, using an index with the GDP in 1989 equal to 100, in 2000 Hungary it was equal to 109, in Poland to 144, and in Romania it was 82.<sup>20</sup> In other words, while Hungary and especially Poland have experienced economic growth over the last decade, in 2000 Romania did not achieve its 1989 economic parameters.

The facts reviewed above lend support to my theoretical arguments regarding the relationship between political institutional histories and economic outcomes in the countries under scrutiny: more reformist communist and post-communist political histories are usually associated with higher growth rates. Furthermore, these institutionalized histories and their specific politico-organizational conditions create contexts in which different paths to entrepreneurship are shaped. These contexts dictate not only “what actors are constituted as legitimate economic participants and how they relate to each other”<sup>21</sup> but also—in the context of this study—the structure of rewards (or income returns) to various forms of capital employed in entrepreneurship.<sup>22</sup>

54, 2002, pp. 308-337; World Bank, *Transition: The First Ten Years. Analysis and Lessons for Eastern Europe and the Former Soviet Union*, World Bank, Washington, D.C., 2002.

<sup>16</sup> D Dăianu, “Fiscal and Monetary Policy.” in H. Carey (ed.), *Romania since 1989: Politics, Economics, and Society*, Lexington Books, Lanham, 2004, pp. 391-418.

<sup>17</sup> Gabanyi, 2004.

<sup>18</sup> M. McFaul, “The Fourth Wave of Democratization and Dictatorship: Noncooperative Transitions in the Postcommunist World.” *World Politics*, Vol. 54, 2002, pp. 212-244.

<sup>19</sup> World Bank, 2002, p.1

<sup>20</sup> World Bank, 2002.

<sup>21</sup> N Biggart & M. Guillén, “Developing Difference: Social Organization and the Rise of the Auto Industries of South Korean, Taiwan, Spain, and Argentina”, *American Sociological Review*, 64, 1999, p. 742

<sup>22</sup> Regarding the larger topic of the institutional specificity of the former communist bloc, on a merrier tone,

In the following pages, employing survey data from Hungary, Poland, and Romania from 2000, I will examine the factors that regulate entry into small entrepreneurship and income returns to small entrepreneurship (self-employment) in each of these countries. Based on my previous discussion regarding the role of political institutional histories for market transition, I expect that in Hungary and Poland – two countries with more reformist histories – the proportion of small entrepreneurs will be higher than in Romania. Secondly, I expect that income returns to being a small entrepreneur will be higher in Hungary and Poland than in Romania. Thirdly, I contend that the longer a country’s history of market reforms, the higher the income returns to education (or human capital). That is, consistent with arguments advanced by Victor Nee’s market transition theory<sup>23</sup>, education will yield higher income returns in Hungary and Poland than in Romania. Fourthly, in all of these three countries, individuals who were small business operators (or self-employed) *prior to* the collapse of communism have higher chances of being entrepreneurs in 2000 than other individuals. This is consistent with arguments advanced by the “capitalism from below” thesis.<sup>24</sup> According to this thesis, compared with other people, individuals who ran small private businesses during socialism are at an advantage during transition because they have the expertise or the cultural capital required to operate successfully in a market environment. Furthermore, I expect that individuals who held positions of managerial authority during communism will be more numerous among entrepreneurs in Romania than in Hungary and Poland.

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let me quote from Adams & Brock’s “*Adam Smith Goes To Moscow: A Dialogue on Radical Reform* (Princeton University Press, Princeton, NJ, 1994). In their fictional account of the meeting between the Prime Minister of an Eastern European country and a Western economic advisor, the latter argues for an unconditional implementation of “shock therapy.” The Eastern European Prime Minister emphasizes the need to take into account the specific conditions in each country: “Consider, for example, that in 1990 according to Moscow’s Center of Public Opinion Studies, 42 percent of the Soviet people believed in telepathy, 57 percent believed in televised cures for afflictions of all sorts, 42 percent believed in astrology, and 35 percent believed in sorcery (...) In the last Czech Elections [in the early 1990s – *my note*] forty parties, coalitions and movements contended for votes, including the ‘Friends of Beer’ and the ‘Independent Erotic Initiative.’ Obviously, this bizarre milieu is a fertile habitat for economic myths and a suspicion of free market ideas imported from the West.” (p. 7) Speaking of myths and their fertile habitat, in the early 2000s, the then ruling political party of Ion Iliescu and Adrian Năstase tried to come up with miraculous (albeit hilarious) solutions to jump-start the Romanian economy. One such solution was the construction of a Dracula theme-park, which, the Năstase cabinet believed, would attract millions of tourists and dollars, and would help balance the national budget. After intense publicity on the project, the Dracula theme-park project was abandoned. For other excellent examples illustrating the trials and tribulations of post-socialist Romania, see K. Verdery, *What Was Socialism, and What Comes Next?*, Princeton University Press, Princeton, 1996.

<sup>23</sup> Nee, 1989.

<sup>24</sup> G Eyal, I Szélenyi, and E. Townsley, *Making Capitalism without Capitalists: The New Ruling Elites in Eastern Europe*, Verso, London, 1998; the initial formulation of the “capitalism from below” thesis is found in I. Szélenyi, *Socialist Entrepreneurs*, University of Wisconsin Press, Madison, 1988.

## 2. Data and Measures

In this chapter, I employ survey data from the 2000 study “Poverty and Social Structure in Transitional Economies” coordinated by Ivan Szelényi.<sup>25</sup> Although his study focuses on poverty, the information included in the questionnaire allows me to outline comparatively the contours of entrepreneurship in Hungary, Poland, and Romania. Szelényi’s study employs nationally representative samples of the adult, noninstitutionalized populations of the three countries mentioned above. The sampling method was random stratified: each sample includes at least 1,000 individuals, ages 15 years and over and the interview method was face-to-face.

Before presenting the measures I will employ, I must, however, comment on the limitations of the survey data described above. First, these samples are *nationally* representative. Thus, it is extremely unlikely that owners of large businesses were interviewed in these surveys. The inherently small number of entrepreneurs included in these or any other nationally representative samples does not allow for detailed statistical inferences regarding this group. Such inferences would require representative samples of the entrepreneurs from the countries under scrutiny.

Secondly, life history data and event history modeling techniques would have been ideal by allowing me to account for the formation of the new entrepreneurial classes in a time-varying way, from 1990 until 2000. My data, however, is almost wholly cross-sectional, reflecting the contours of the entrepreneurial categories in 2000. Yet, the surveys I employ contain information about respondents’ careers before the collapse of the communist regime. This will allow me to identify patterns of recruitment into entrepreneurship and the determinants of income returns to entrepreneurship.

Despite the limitations mentioned above, Szelényi’s data have several important merits. First, given the timing of these surveys (i.e., ten years after the collapse of the communist regimes), my analyses will provide an updated picture (albeit in large strokes) of the new private sector. Studies of post-socialist entrepreneurship in Eastern Europe<sup>26</sup> employ data about individuals’ socio-demographic characteristics before and only *three or four* years after the collapse of the communist regimes. Given that the socialist system was an “economy of shortages,”<sup>27</sup> which neglected demand for consumer goods and services, “this [could have created] large opportunities for the first cohort of entrepreneurs.”<sup>28</sup>

<sup>25</sup> I Szelényi, “Poverty and Social Structure in Transitional Economies. Survey data and methodology documentation”, Yale University: Center for Comparative Social Research, 2000. I am extremely grateful to Ivan Szelényi for allowing me to employ his data.

<sup>26</sup> J Böröcz & A. Róna-Tas, “The Small Leap Forward: The Emergence of New Economic Elites”, *Theory and Society*, no. 24, 1995, pp. 751–781; Róna-Tas, 1994; Eyal et al., 1998; Hanley, 2000a; 2000b.)

<sup>27</sup> J Kornai, *Economics of Shortage*, Elsevier North Holland, New York, 1980.

<sup>28</sup> A Walder, “Privatization and Elite Mobility: Rural China, 1979 – 1996”. Asia/Pacific Research Center *Working Papers Series*, Institute for International Studies, Stanford University, Stanford, 2002b, p.9.



Employing data from 2000 allows me to assess whether the conclusions of previous studies reflect a temporary phase in transition or more general trends regarding the social origins of entrepreneurs and income returns to entrepreneurship. The second merit of the data I employ is that it also includes Romania -- a case that has been less frequently included in comparative sociological analyses of transition.

I present in Table 1 (see next page) the definition and the sample characteristics for the variables employed in the cross-national analyses of entrepreneurship.

*Measures.* To account for entrepreneurship, Szelényi's surveys employ the categories "self-employed with employees" and "self-employed without employees." For reasons of brevity, in the following pages I use "employers" to denote "self-employed with employees" and "self-employed" to denote "self-employed with no employees." To examine patterns of recruitment into entrepreneurship, I will resort to several logistic regressions, employing two dummy variables that capture qualitatively distinct entrepreneurial categories: "Employer (or self-employed with employees)" (1=yes) and "Self-employed (with no employees)" (1=yes).

*Independent Variables.* An individual's *human capital* is measured in years of education. "*Cultural capital for running a private business*" is proxied by a dummy variable indicating whether, in 1988, the respondent was self-employed or not (1=yes). According to Szelényi<sup>29</sup> and Eyal et al.<sup>30</sup>, individuals who were self-employed under state socialism are at an advantage during transition because they already have the cultural capital or the expertise required by a market economy.

Some analysts might contend that becoming an entrepreneur is ultimately a function of an individual's financial resources.<sup>31</sup> To account for this, I capture a respondent's *financial resources* by a subjective indicator of income in 1988. (These surveys did not ask for the actual figures for income in 1988 and this is why I employ this subjective indicator.) The source item asked respondents: "Compared with other families in your country, would you say your family income in 1988 was far below average, below average, average, above average, or far above average?" Other studies<sup>32</sup> treat this question as asking respondents to place their family's income in a quintile of the 1988 income distribution. For technical reasons (e.g., lack of variation in some of the five categories, which yields biased estimates), I recoded this variable as follows: 1 = "(The respondent's family income in 1998 was) Far below and below average"; 2 = "Average"; and 3 = "Above and far above average."

<sup>29</sup> Szelényi, 1988;

<sup>30</sup> Eyal et al., 1998;

<sup>31</sup> A survey of manufacturing firms conducted in medium-size cities in Poland, Romania, Slovakia, Russia, and Ukraine, found that in Romania "own and family financing" was the most important source of financing for starting a business (S. Johnson, J. McMillan, & C. Woodruff, "Entrepreneurs and the ordering of institutional reform: Poland, Slovakia, Romania, Russia, and Ukraine compared", *Economics of Transition*, no. 1, 2000, p. 11).

<sup>32</sup> J Earle, & Z Sakova, "Entrepreneurship from Scratch", Unpublished Manuscript, SITE, Stockholm School of Economics and Central European University, 2000.

Table 1. Sample Characteristics of Employers, Self-employed Individuals, and Employees from Hungary, Poland, and Romania in 2000

Variables	Hungary			Poland			Romania		
	Employer	Self-employed	Employee	Employer	Self-employed	Employee	Employer	Self-employed	Employee
Gender (male=1)	83%	62%	54%	38%	55%	50%	88%	78%	56%
Respondent's average age (in years)	43	42	38	42	42	37	41	44	37
<i>Place of Residence</i>									
Urban (1=yes)	50%	62%	69%	75%	38%	81%	94%	50%	75%
<i>Human Capital</i>									
Average years of education	12	12	11	10	11	12	14	9	12
Median years of education	12	12	10	10	10	12	16	9	12
<i>Position of Authority Before 1988</i>									
R had at least 3 subordinates in 1988	8%	10%	12%	-	3%	6%	25%	17%	7%
<i>Cultural Capital for Running a Business</i>									
R was self-employed in 1988 (1=yes)	16%	21%	1%	12%	42%	1%	-	17%	-
<i>Financial Resources: Family Income in 1988</i>									
Far below and below average	25%	8%	12%	12%	7%	8%	19%	22%	10%
Average	41%	71%	80%	88%	74%	78%	44%	44%	65%
Above and far above average	34%	21%	8%	-	21%	14%	37%	34%	25%
Ever unemployed after 1990 (1=yes)	16%	27%	28%	12%	18%	21%	13%	13%	24%
Average business age (in years)	13	12	- <sup>a</sup>	16	18	- <sup>a</sup>	6	12	- <sup>a</sup>
<i>Business Sector</i>									
Agriculture	8%	23%	8%	24%	65%	3%	-	33%	6%
Industry	25%	8%	34%	-	2%	25%	25%	12%	39%
Trade	42%	15%	15%	38%	15%	17%	38%	22%	1%
Services	25%	54%	43%	38%	18%	65%	37%	33%	46%
Number of cases	12	48	323	8	55	315	16	18	300

\*Source: "Poverty and Social Structure in Transitional Economies" (I. Szelényi, coord., 2000)

Notes: Except where noted, the figures represent percentages;

<sup>a</sup> Not applicable as this variable is calculated only for business owners.

Some authors see self-employment as a less genuine form of entrepreneurship and more as a forced, temporary choice adopted by individuals facing unemployment and poverty (for an informative review of the so-called “refuge from poverty” thesis, see Hanley<sup>33</sup>) To account for this fact, I use the dummy variable “*Ever unemployed after 1988*” indicating whether the respondent was ever unemployed after 1988 but is currently an employee or an entrepreneur.

“*Former position of managerial authority under state socialism*” is captured by a dummy variable indicating whether the respondent had at least 3 subordinates under state socialism. One caveat: Szelényi’s surveys from 2000 did *not* ask respondents whether they were members of the communist party in 1988. Thus, “authority position under state socialism” is *not* the equivalent of the “(communist) cadre (or party official)” variable from other market transition studies.<sup>34</sup> While all cadres enjoyed some sort of authority, not all respondents with positions of authority were cadres. For instance, foremen or heads of department stores often had at least 3 subordinates but this fact did not mean that they were party members, let alone cadres.

Victor Nee deems “cadre” a measure of positional power but one could say that, in the context of market transition, “cadre” also measures a particular form of (an individual’s) social capital or network resources. At the same time, one can reasonably argue that former cadres have considerable organizational experience or managerial skills, accumulated by virtue of their position of authority under state socialism. Similar validity issues can be raised in regard to my variable “authority position under state socialism”; unfortunately, these surveys lack other indicators to further distinguish among the various facts captured by “authority position under state socialism.” In this article, I will interpret this variable as signaling network resources and organizational skills.

### **3. Socio-demographic Profiles of Post-Socialist Entrepreneurs: Results of Bivariate Analyses**

Let me begin by noting the differences in the raw numbers of entrepreneurs across countries as shown in Table 1. As compared to Hungary and Poland, Romania has proportionally a smaller “army” of entrepreneurs – a finding that is consistent with data from other studies.<sup>35</sup> Path dependency theorists would deem this finding unsurprising because socialist Romania did not attempt to reform its economic system and activities in the second economy were forcefully discouraged. But, as I argued before, the absence of reformist policies before 1990 need not necessarily handicap the rise of the private sector during transition.

<sup>33</sup> Hanley, 2000a

<sup>34</sup> See Nee, 1989, 1991, 1996; Róna-Tas, 1994; Walder, 2002a, 2002b, 2002c;

<sup>35</sup> European Bank for Reconstruction and Development (EBRD), *Transition Report 1999*, London, 1999.

While the past does play a role in this story, what has happened after the collapse of the communism, I contend, is equally important. A case in point is the Czech Republic, which, like Romania, did not witness economic reforms in the late 1980s. However, after the downfall of the communist regime, the Czech Republic implemented comprehensive economic reforms and by the mid-1990s had one of the highest per-capita entrepreneurship in the region and a dynamic market economy.<sup>36</sup>

More complex forms of entrepreneurship such as being a small business operator with employees usually require significant resources in terms of human capital.<sup>37</sup> This does seem to be true in both Hungary and especially Romania, where employers tend to be better educated than employees. For example, as shown in Table 1, the median years of education of Romanian employers, i.e., 16 years, indicates that half of them are college graduates. In contrast, the average years of formal schooling of Polish employers is lower than the average years of education of their conational employees. Furthermore, previous studies<sup>38</sup> have shown that self-employment has low entry barriers in terms of formal education. This seems to be true in Poland and Romania, where self-employed individuals tend to be less educated than employees (see Table 1). The opposite is true in Hungary, where both the average and the median years of formal schooling indicate that self-employed individuals are somewhat better educated than employees.

Consider next the controversial issue of former authority figures. As this status was recorded by and recoded from these surveys, individuals who fall into this category are not over-represented among entrepreneurs in either Hungary or Poland. In the Romanian case, however, there is a statistically significant association between being an employer and having had at least 3 subordinates in 1988 ( $\chi^2 = 5.98$ ,  $p < .05$ ). Results of bivariate statistical analyses appear to indicate that, ten years into transition, Romanians who enjoyed some sort of authority in the deposed regime are fairly well represented among the upper strata of small entrepreneurs (i.e., self-employed with employees).

Former socialist entrepreneurs (i.e., individuals who were self-employed in 1988) have a statistically significant presence among the self-employed in all of these three countries. The situation is different for employers: the only statistically significant association between “petit bourgeois in 1988” and “employer in 2000” is recorded in the Hungary ( $\chi^2 = 14.22$ ,  $p < .000$ ).

Further, individuals who have been unemployed after 1988 have a statistically significant presence only among the Hungarian and Polish self-employed ( $\chi^2 = 14.48$ ,  $p < .001$ ; and  $\chi^2 = 21.67$ ,  $p < .001$ , respectively). Regarding material

<sup>36</sup> V Benacek, “Private Entrepreneurship and Small Businesses in the Transformation of the Czech Republic” in G. Grabner and D. Stark (eds.), *Restructuring Networks in Post-Socialism: Legacies, Linkages, and Localities*, Oxford University Press, Oxford, 1997, pp. 209-241; World Bank, 2002.

<sup>37</sup> Eyal et al., 1998.

<sup>38</sup> Róna-Tas, 1994; Hanley, 2000a; Eyal et al., 1998.

resources in 1988, the Romanian and Polish entrepreneurs in these samples did not enjoy significant advantages as compared to employees (i.e., most individuals in both categories had an average monthly income in 1988). The same is true for Hungarian employers but not for self-employed; the latter are mainly recruited from the category of respondents whose income in 1988 was above average ( $\chi^2 = 7.16, p < .05$ ).

Consistent with findings of other studies,<sup>39</sup> in all of these three countries, employers mainly operate in trade and services. The same categories seem to be favored by Hungarian and Romanian self-employed (see also for Hungary, Róna-Tas<sup>40</sup>). In Poland, however, agriculturally self-employed are a majority. This is not surprising taking into account that, in contrast to Hungary and Romania, the majority of Poland's agriculture remained in private hands during state socialism.<sup>41</sup>

#### 4. Entry into Entrepreneurship in Hungary, Poland, and Romania: Results of Causal-Type Analyses

In the previous section I sketched the contours of entrepreneurship in Hungary, Poland, and Romania. Let me now move beyond simple bivariate statistics and employ causal-type analyses to account for the socio-demographic determinants of entry into entrepreneurship. The *dependent (dummy) variables* in the following analyses are “employer (or self-employed with employees) (1=yes)” and “self-employed (without employees) (1=yes).” The list of independent variables includes “respondent's education (in years),” “position of authority under state socialism (1=yes),” “cultural capital for running a business (or whether the respondent was self-employed in 1988 [1=yes]),” “whether the respondent was unemployed after 1988 (1=yes),” and “respondent's financial resources in 1988 (on a 3-point scale).” Control variables are gender (1=male), respondent's age (in years), and place of residence (coded “1” for urbanites and “0” otherwise).

Table 2 presents the results of five causal analyses of entry into entrepreneurship, employing nonlinear models, i.e., logistic regressions. The  $\chi^2$  values are significant at  $p < .01$  in all models, and the fit of each full model shows a significant improvement over a reduced model with control variables. For reasons of brevity, I include in Table 2 only the full models for each entrepreneurial pathway in each country.

<sup>39</sup> D Berkovitz & D. DeJong, “Entrepreneurship and Post-Socialist Growth”, Unpublished manuscript. Department of Economics, University of Pittsburgh, Pittsburgh 2003; Earle and Sakova, 2000.

<sup>40</sup> Róna-Tas, 1997.

<sup>41</sup> Łoś, 1990b; Verdery, 2003; Wedel, 1986

Table 2. Coefficients from the Logistic Regressions of Being an Employer and a Self-Employed Individual on Selected Independent Variables

Independent Variables	Hungary		Poland <sup>a</sup>		Romania	
	Employer	Self-employed	Self-employed	Employer	Self-employed	Self-employed
Gender (male=1)	1.553** (.790)	.261 (.339)	.541 (.318)	1.995* (.801)	1.541* (.636)	
Respondent's age (in years)	-0.14 (.019)	-0.14 (.011)	-.034* (.014)	-.025 (.021)	-.038* (.018)	
<i>Place of Residence</i>						
Urban (1=yes)	-835 (.620)	-.394 (.346)	-1.281*** (.343)	1.214 (1.079)	-.001 (.531)	
<i>Human Capital</i>						
Years of education	.242* (.112)	.259*** (.061)	.152* (.075)	.544*** (.135)	-.244** (.090)	
<i>Position of Authority Under State Socialism</i>						
Respondent had at least 3 subordinates in 1988 (1=yes)	-- <sup>b</sup>	-.135 (.534)	.152 (.846)	.516 (.708)	1.876* (.796)	
<i>Cultural Capital for Running a Business</i>						
R was self-employed in 1988 (1=yes)	1.852* (.882)	3.291*** (.570)	3.410*** (.437)	-- <sup>c</sup>	5.033*** (1.047)	
<i>Financial Resources: Family Income in 1988 (1-3)</i>						
Ever unemployed after 1990 (1=yes)	.134 (.602)	.397 (.319)	.511 (.328)	.019 (.479)	.240 (.462)	
Constant	-- <sup>b</sup>	1.091*** (.395)	1.449*** (.429)	1.086 (.866)	-.196 (1.068)	
-2 log-likelihood	-7.395 (2.032)	-6.322 (1.154)	-4.473 (1.217)	-12.686 (2.404)	-1.952 (1.536)	
$\chi^2$	110.64	305.54	314.50	118.58	147.41	
Degrees of freedom	6	8	8	7	8	

\*Source: "Poverty and Social Structure in Transitional Economies" (I. Szelényi, coord., 2000)

Notes: Each column contains the full model for each entrepreneurial category. The figures represent unstandardized coefficients (standard errors). <sup>a</sup> The extremely small number of Polish employers in the national sample did not allow for meaningful causal-type analyses (see text). <sup>b</sup> Not included in models due to lack of variation in the respective categories; <sup>c</sup> Not included in models due to perfect determination. That is, no Romanian employer was self-employed in 1988; \* p < .05; \*\* p < .01; \*\*\* p < .001

Before discussing the results, I must, however comment on several technical limitations of these analyses. Ideally, I should have employed multinomial logistic models (MNL), which, as compared to binary logistic regressions, have the advantage of simultaneously considering multiple outcomes (i.e., “employers,” “self-employed,” and “employees”). This fact allows meaningful comparisons across categories.<sup>42</sup> Unfortunately, due to the lack of cases (perfect determination) or to lack of variation in the categories of some independent variables, MNL was not a feasible modeling strategy.

Secondly, these samples are nationally representative. Although these samples might accurately reflect the *proportion* of entrepreneurs in the adult population of each country, the actual (small) number of entrepreneurs included in each sample has made some more detailed analyses difficult if not impossible. A case in point is the Polish sample: the extremely low number of self-employed with employees (or employers) does not allow for meaningful causal-type analyses. This is why, for Poland, Table 2 presents only the results of the logistic regression of being a self-employed individual (with no employees) on selected independent variables. Also, the already discussed lack of variation in the categories of some variables led me to exclude them from analysis (see the bottom of Table 2).

Against this background, readers should interpret my analyses as having an *exploratory* character. Put another way, my analyses seek to portray, in large strokes, some of the socio-demographic factors that might play a role in this story of entrepreneurship, ten years into transition. Supplementary analyses using other types of samples (i.e., nationally representative samples of entrepreneurs or, at least, larger national representative samples) are required for further in depth analyses of entrepreneurs.

**Hungary.** Employers in this country are mainly recruited among males (see Table 2). An individual’s financial resources before 1990 and having been unemployed at least once after 1990 have no influence on the chances of being an employer. Other studies<sup>43</sup> found that in the early 1990s, education was one of the major resources for more complex, elite forms of post-socialist entrepreneurship. This also seems to be the case in 2000 as each year of education increases an individual’s chances of being an employer.

Former socialist entrepreneurs have a considerable advantage in operating as employers ten years after the formal demise of Kadar’s regime. This finding is consistent with the “capitalism from below” thesis, which maintains that former socialist entrepreneurs would be well represented among post-socialist businesspeople. This is so because the former socialist petit bourgeois possess, among other things, the cultural capital or a proper understating of how to operate in a market economy. Moreover, this finding attests that, in Hungary, self-employment is a road to upward mobility.

<sup>42</sup> J Scott Long, *Regression Models for Categorical and Limited Dependent Variables*, Sage Publications, London, 1997, p. 150.

<sup>43</sup> Eyal et al., 1998; Róna-Tas, 1994.

My analyses tend to confirm Eyal et al.'s views: Hungarians who enjoyed some sort of authority during communism are not more likely to be employers than other individuals in 2000. However, given the limitations of this type of survey and its measures, readers should exercise some caution in interpreting the results of these analyses.

In Hungary, education plays a significant, positive role not only for being an employer but also for being a self-employed individual. This runs counter to findings of other studies, which, at the dawn of the transition, reported negative effects of education on entry into self-employment.<sup>44</sup> More recent studies of Hungary, however, show that well-educated individuals seem to be attracted to self-employment.<sup>45</sup> For some of these individuals, this might be a temporary strategy to avoid unemployment and cope with poverty. Other people, especially those within the so-called liberal occupations (e.g., law, medicine etc.) might have figured out that, given their educational credentials and skills, they could do better as self-employed individuals than as employees. Moreover, in the 1990s, the Hungarian laws were particularly generous with individuals who registered themselves as self-employed; this generosity translated into tax exemptions for the “new” small business operators.<sup>46</sup>

A decade into the Hungarian transition, former authority figures are no more likely than other respondents to operate as self-employed individuals. Former socialist entrepreneurs are well represented not only among employers but also among the self-employed in 2000, which signals that these people have at least managed to survive as small business operators after the socialism's collapse (for similar results from the early 1990s, see Hanley<sup>47</sup>). Consistent with the predictions of the “refuge from poverty” thesis, unemployment seems to have pushed some individuals to take shelter from neediness in self-employment. Specifically, Hungarians who have been at least once unemployed since 1988 are more likely to become self-employed than individuals who have not experienced unemployment.

**Poland.** As mentioned before, the very small number of employers included in the Polish sample did not allow for meaningful causal analyses. Overall, the Polish story, as told by these surveys, is somewhat similar to the Hungarian one. Unemployment has also forced some Poles to take refuge from economic hardships in self-employment. Like in Hungary, in Poland too, education increases one's chances of entry into self-employment. Furthermore, Poland's former socialist entrepreneurs, like the Hungarian ones, are more likely to be self-employed than

<sup>44</sup> See on this point, Róna-Tas, 1994

<sup>45</sup> I Gábor, “Too Many, Too Small: Small Entrepreneurship in Hungary—Ailing or Prospering?” Pp. 158 – 175 in G Grabner and D Stark (eds.), *Restructuring Networks in Post-Socialism: Legacies, Linkages, and Localities*, edited by Oxford University Press, Oxford, 1997, pp. 158-175; Róna-Tas, 1997.

<sup>46</sup> Róna-Tas, 1997, p. 202.

<sup>47</sup> Hanley, 2000a.



other individuals.<sup>48</sup> Having had at least 3 subordinates in 1988 has no impact on entry into self-employment in 2000.

**Romania.** Like in Hungary, men are more often involved in entrepreneurship than women. As I will discuss in the following chapters, this is likely to reflect the gendered practice of registering firms in the names of the males in the household. However, as I found out during my fieldwork, this statistical fact underestimates the important contribution that women have in running businesses (for similar gendered practices in registering firms, see Yanagisako's study on Italy.<sup>49</sup>)

Human capital, captured here by years of schooling, has positive effects on entry into entrepreneurship as an employer. Like in Hungary, where Eyal et al.<sup>50</sup> predicted that well educated individuals would form the core of more complex forms of entrepreneurship, in Romania too, education is an important resource for operating as an employer in 2000. Yet, Romanians who enjoyed some sort of authority in 1988 are no more likely than others to be employers – a finding to which I will return in the following pages.

Younger people are more likely to follow the avenue of self-employment, which might be the only way out of potential unemployment and poverty. Let me make a brief but necessary detour and illustrate this trajectory of refuge from poverty with the case of Romanian workers formerly employed in such moribund sectors as mining and heavy industry. At the pressures of the World Bank and the International Monetary Fund, in 1998 the then center-right ruling coalition decided to restructure Romania's oversized and unproductive coal mining industry from the Jiu Valley. As trade unions in the mining industry were extremely powerful, the Government attempted to and eventually reached an agreement on how the restructuring would take place. Workers in this industry faced two choices: they could either stay in the industry and be fired subsequently or they could voluntarily leave their jobs with a generous severance pay package (i.e., the so-called "worker 'contract buy-outs'" or *disponibilizare* in Romanian). Each individual who chose the latter was awarded "a lump-sum of twelve to twenty months of pay in addition

<sup>48</sup> Studies on the Polish case arrive at mixed conclusions. On the one hand, it was Poland that Staniszkis used as empirical evidence to formulate the so-called "political capitalism" thesis in the late 1980s. (J. Staniszkis, "Political Capitalism in Poland", *East European Politics and Societies*, no.1, 1991, pp. 127-141.) Yet, as Rona-Tas argues (1998, p. 117), "it is less clear in Staniszkis' account whether political capitalism is a temporary phase that will pass once property relations are established." On the other hand, Eyal et al (1998) maintain that political capitalism thesis does not cut ice in Poland (and Hungary). Employing the same data as Eyal et al (1998), Hanley (2000b) shows that, as compared to other former socialist countries, political capitalism is, indeed, an inaccurate theoretical tool to describe Hungary and Poland. Yet, when comparing these two countries, Hanley (2000b) finds both petit and grand embourgeoisement among nomenklatura members in Hungary but not in Poland, where ex-cadres are "petit as opposed to grand entrepreneurs." This little detour attests that, even when more detailed data about the former elites are available, different authors might arrive at somewhat different conclusions. Again, readers should recall that my samples and measures cannot provide answers to questions regarding the fate of the former nomenklatura in 2000.

<sup>49</sup> S Yanagisako, *Producing Culture and Capital: Family Firms in Italy*, Princeton University Press, Princeton, 2002.

<sup>50</sup> Eyal et. al, 1998.

to regular unemployment benefits.”<sup>51</sup> Notably, at that time, people in the mining industry were among the best-paid Romanian workers. It goes without saying that most miners decided to cash-in their severance pay package.

What happened with them afterwards is an interesting yet sad story. The Romanian Government at that time, with the assistance of international agencies, outlined several programs to encourage these workers to start small businesses. But, as is often the case, foreign-designed aid programs tend to fail when confronted with the reality of countries where such programs are implemented (for other [hilarious] examples of the collusion between foreign experts and the realities of Eastern Europe, see Adams and Brock, and especially Wedel<sup>52</sup>). Foreign advisors and domestic experts alike overlooked the fact that the former mining cities could not survive, let alone prosper, only on the basis of commerce and services. As most ex-coal miners usually opened grocery shops, beauty parlors, auto-repair shops, and especially bars and restaurants, few of them managed to remain in business let alone to prosper. As a result, many former coal miners decided to find their luck elsewhere; some of them moved to other industrial cities, while many others decided to return to their native villages and become farmers.

Turning back to my data and analyses, the negative effect of education on the chances of becoming a small business operator attests that in Romania self-employment has low entry barriers in terms of human capital. Further, as Szelényi<sup>53</sup> would have it, an individual’s “memories of market transactions” or cultural capital are an asset for operating in the private sector in 2000; as compared to other individuals, former Romanian socialist entrepreneurs are at a huge advantage in running a small business, a decade after the collapse of Ceaușescu’s regime.

Romanians who had at least 3 subordinates are more likely to be self-employed in 2000 than other individuals. However, readers should keep in mind that “former managerial authority position” is not the equivalent of the “(communist) cadre” variable. In other words, this finding should not be interpreted as absolute evidence that the former Romanian communist politicians experienced downward mobility into self-employment.

<sup>51</sup> D Kideckel, “A New ‘Cult of Labor’: Stress and Crisis among Romanian Workers”, *Sociologie românească* [Romanian Sociology], no. 1, 2002, p. 143.

<sup>52</sup> Adams & Brock, 1993; J. Wedel, *The Private Poland: An Anthropologist’s Look at Everyday Life*, Facts on File Books, New York, 1986. In her work on land restitution in post-socialist Romania, K. Verdery notes that one reason that made foreign advisors and local politicians unprepared for the unexpected outcomes of Western recipes for reform is that “the very concept of private property was so deeply ideological (...) that no one was able to think clearly about its logistics” (2003, p. 4). She adds that the results of reforms were different from expectations because “all property-making, including our own [in the West – my note], is not a natural but a historical and political process [italics mine]” (K Verdery, *The Vanishing Hectare: Property and Value in Postsocialist Transylvania*, Cornell University Press, Ithaca and London, 2003, p.4). For an illuminating and comprehensive analysis on the collectivization of Romania’s agriculture during communism, see G Kligman & K Verdery, *Peasants under Siege: The Collectivization of Romanian Agriculture, 1949-1962*, Princeton University Press, Princeton, NJ, 2011.

<sup>53</sup> Szelényi, 1988;

## 5. Cross-National Analyses of Income Returns to Small Entrepreneurship

Based on media accounts, personal experiences, and anecdotal evidence regarding the newly rich, most Hungarian, Poles, and Romanians are simultaneously fascinated and outraged by the well-being of the new entrepreneurial classes. During my frequent trips to Romania in 1999 and 2000, I, too, was struck by the huge wealth discrepancies I encountered. The large number of top-of-the-line Mercedeses, Audis, Lexuses, and BMWs cruising the streets of Romanian cities often made me wonder if I was not hallucinating. To my relief, after meeting some Romanian entrepreneurs, I found out that I had not been hallucinating at all. All of the fancy cars I had seen were real, proving that, indeed, it was quite good to be an entrepreneur in post-Ceausescu's Romania.

Yet, after meeting one such BMW owner, I remembered the less glamorous case of a small entrepreneur I interviewed in Romania in 1999: In his early thirties, married, having a small child and being unemployed, he borrowed money from friends and relatives and started a small retail business. Sixteen months later he was near bankruptcy due to the opportunistic behavior of his business partner and – as his spouse put it – their poor understanding of how “a market economy really works in this country.” Eventually, he sold his business shares to his cheating partner and “bought” himself a tourist visa<sup>54</sup> for a Western European country. He eventually made it to the West and, according to news from him, for a while, he illegally lived and worked on a farm in Spain. Later on, he managed to get a residence permit and as a result he was able to find better-paying jobs and to bring his wife to Spain. Although both of them still dream of going back to Romania and opening their own business, they doubt this will happen in the near future.

Admittedly, the stories presented above represent extreme or outlier cases; the majority of Romanian, Hungarian, and Polish (small) entrepreneurs lies in between BMWs' owners and struggling self-employed individuals. Along with many market transition scholars, readers might rightfully wonder how well do most entrepreneurs fare as compared to both their fellows and other people. What are the most and the least rewarding entrepreneurial pathways in different countries? How large are the income differences between entrepreneurs and other individuals and what socio-demographic factors account for such differences?

To answer these questions, I begin by discussing the results of bivariate statistics of income returns to being an entrepreneur and an employee. Income returns to these occupational categories are measured by a respondent's self-

<sup>54</sup> Before 2000, Romanian citizens needed visas to enter the so-called Schengen space (i.e., Western Europe). Romanians who wanted to work abroad did so by obtaining a tourist visa; often times, such visas were secured by bribing – via intermediaries – officials of Western European embassies in Romania. Once in Germany, Spain, Italy, or Greece, many such tourists would postpone indefinitely any sightseeing and would search for work through their networks of friends or relatives from these countries. (For the role of social networks for Romanians' transnational migration, see Sandu's excellent studies 2000a, 2000b, 2003).

reported income in the preceding month; for comparability reasons, income figures are expressed in U.S. dollars. Table 3 (see next page) presents the average monthly income of employers, self-employed individuals, and employees, by country and business field in 2000.

Some analysts tend to be skeptical of market transition studies that rely on self-reported income. This is so for several reasons: First, against the background of an uncertain, ever-changing socio-political environment, it is assumed that respondents of surveys conducted in transitional economies tend to under-report their incomes. This is particularly the case of ex-communist countries facing serious economic hardships, whose tax systems are perceived as a burden and are not highly rationalized (i.e., they lack proper mechanisms to collect taxes and to sanction tax evasion, and/or the bureaucrats in charge of tax collection are corrupt and/or subject to political pressures). Furthermore, like in many other countries, some individuals are more prone than others to cheat on their taxes. In Romania, for instance, some entrepreneurs and other well-to-do individuals (e.g., state bureaucrats, members of the Parliament etc.) transfer portions of their income to their kin. That is, to avoid paying (high) taxes, such individuals officially record some of the money they make under the names of their wives, daughters, sons, sisters, brothers, and parents.

Second, income figures are but one indicator of an individual's socio-economic situation. Media often portrays many of the newly rich in Eastern Europe as being driven by conspicuous consumption because some of the newly rich publicly talk of and display their lavish houses, Rolexes, designer clothes, and luxury cars.<sup>55</sup> Granted, the urge to impress other people is but one factor in this story of immodesty<sup>56</sup>; investing in many such tangible assets is also a response to the economic uncertainty that still prevails in the region. Thus, to properly describe the range of inequalities in transitional countries (among others), one should also take into account indicators of more or less tangible assets (e.g., properties, financial portfolios). Lacking such indicators, however, in the following analyses I had to rely exclusively on a respondent's self-reported income.<sup>57</sup>

<sup>55</sup> S Sampson, "Money without Culture, Culture without Money: Eastern Europe's Nouveaux Riches", *Anthropological Journal of European Cultures*, no. 1, 1994, pp. 7-30.

<sup>56</sup> Here is but one example of conspicuousness: In 2001, the next day after the business weekly "Capital" published the list of the 300 wealthiest Romanians, the businessman Gigi Becali criticized in a TV talk show the journalists from "Capital." Becali was outraged because "Capital" listed him as the fifteenth wealthiest Romanian, with 150 million US dollars, when in fact, he claimed, he was worth 300 million US dollars. He threatened to sue the financial weekly "Capital" for slander.

<sup>57</sup> Róna-Tas reports similar difficulties in capturing entrepreneurs' economic situation by relying exclusively on income figures: "For instance, successful [Hungarian] entrepreneurs drive Western cars that should be counted as their personal incomes. Instead, these cars are acquired through leasing agreements and are counted as operating expenses." (Róna-Tas, 1994, p. 53, note 5). Some of the entrepreneurs I interviewed in Romania in the early 2000 employed similar strategies to underreport their income and avoid paying taxes.

Table 3. Average Monthly Income in US Dollars of Entrepreneurs and Employees, by Country and Business Field

	Hungary			Poland			Romania		
	Employer	Self-employed	Employee	Employer	Self-employed	Employee	Employer	Self-employed	Employee
<b>Total</b>	317 (355)	294 (204)	191 (157)	405 (383)	362 (231)	274 (162)	239 (216)	142 (116)	86 (70)
<i>Business Sector</i>									
Agriculture	- <sup>a</sup>	178 (184)	179 (141)	170 (170)	269 (139)	293 (228)	- <sup>a</sup>	138 (142)	81 (70)
Industry	357 (357)	482 (422)	224 (157)	- <sup>a</sup>	- <sup>b</sup>	284 (245)	237 (212)	82 (82)	95 (72)
Trade	344 (267)	251 (178)	136 (125)	504 (577)	577 (533)	256 (228)	138 (116)	283 (128)	75 (47)
Services	222 (222)	331 (249)	185 (161)	461 (461)	332 (347)	276 (231)	325 (224)	72 (59)	83 (70)
No. of cases	12	48	323	8	55	315	16	18	300

\**Source:* "Poverty and Social Structure in Transitional Economies" (I. Szelényi, coord., 2000)

Notes: Median values in parentheses; <sup>a</sup> Not applicable due to lack of cases in the category; <sup>b</sup> Not applicable: only one case in the category

Keeping in mind these limitations, let us examine Table 3, which reveals some notable differences and similarities between and within countries. To begin with, monthly income figures attest that entrepreneurship is a rather lucrative activity: entrepreneurs in all of these countries (be they employers or self-employed individuals) are better off than employees. Furthermore, monthly income figures for each category reveal significant differences among Hungary, Poland, and Romania; such differences are consistent with the theoretical and empirical arguments presented previously. Firstly, given Romania's disastrous economic policy under Ceausescu and its less reformist post-1990 history, it is not surprising that Romanian entrepreneurs and employees make less money than their Polish and Hungarian counterparts (see Table 3). And secondly, the income differences between Romanian entrepreneurs and employees are similar to the income differences between these categories recorded in Hungary and Poland at earlier stages in transition.<sup>58</sup> At that time, new entrepreneurs were presented with more numerous economic niches and therefore they were able to garner higher benefits from exploiting such niches than in the late 1990s.

In these nationally representative surveys from 2000, Romanian employers' average income is approximately 3 times higher than employees' income (see Table 3). This difference is smaller in Hungary and Poland, where employers make 1.7 and 1.5 times, respectively more money than employees. Further, in Romania, self-employed individuals make on average 1.6 more money than employees, while Hungarian and Polish self-employed earn 1.5 and 1.3, respectively, more money than their compatriots who are employees (see Table 3).

Overall, Polish entrepreneurs make more money than their Hungarian and Romanian counterparts. In Poland, employers' monthly income is 1.3 times higher than in Hungary and 1.7 times higher than in Romania. On average, the Polish self-employed make 1.2 times more money than the Hungarian self-employed, and – notably – 2.5 times more money than Romanian self-employed.

For Hungarian employers, the most rewarding business sectors are industry and trade, which bring in at least 1.5 times the money than the service sector does. In Poland, employers' most profitable economic niches are trade and services. Romanian employers who operate in industry and services tend to earn from 1.7 up to 2.4 times more money more than those who operate in trade.

Agriculture seems to be least rewarding business field for Hungarian and Polish self-employed alike. Notably, in Hungary, agriculture is the only sector where employees can compete with the self-employed in terms of their average and median monthly income. In Romania, the self-employed in the service sector are the most disadvantaged group; they seem to earn even less than individuals employed in the same or any other field.

What socio-demographic factors make a statistical difference for income returns to being a post-socialist entrepreneur ten years into transition? How large

<sup>58</sup> EBRD, 1999; World Bank, 2002.

are net the income advantages of entrepreneurs as compared to employees? Table 4 presents the results of causal-type analyses of the determinants of income returns (i.e., natural log of monthly earnings) to entrepreneurship in Hungary, Poland, and Romania. “Respondents who are not in the labor force” are, for obvious reasons, excluded from these analyses.

Table 4. Coefficients from the OLS Regressions of (Natural Log of) Income on Selected Independent Variables

Variables	Hungary	Poland	Romania
Gender (male=1)	.155* (.066)	.224** (.064)	.328*** (.064)
Respondent's age (in years)	.032 (.022)	.068** (.022)	.012 (.022)
Respondent's age squared <sup>a</sup>	-.032 (.000)	-.004** (.000)	-.007 (.000)
Place of residence (urban=1)	.054 (.067)	.032 (.081)	.187* (.077)
<i>Human capital</i>			
Education (in years)	.102*** (.013)	.070*** (.015)	.057*** (.013)
<i>Position of authority Before 1988</i>			
R had a least 3 subordinates in 1988 (1=yes)	.015 (.097)	.067 (.135)	.072 (.121)
<i>Business sector<sup>b</sup></i>			
Agriculture (1=yes)	-.010 (.120)	-.300* (.142)	.167 (.133)
Industry (1=yes)	.120* (.038)	.029 (.040)	.073* (.036)
Trade (1=yes)	-.090 (.094)	.097 (.087)	-.069 (.106)
<i>Entrepreneurship<sup>c</sup></i>			
R is an employer (1=yes)	.447* (.198)	.512** (.195)	.582*** (.156)
R is self-employed (1=yes)	.339** (.100)	.148 (.125)	.375* (.148)
Constant	3.080 (.424)	3.149 (.463)	2.856 (.418)\
R <sup>2</sup>	.242	.170	.268
No. of cases	352	323	326

\*Source: “Poverty and Social Structure in Transitional Economies” (I. Szelényi, coord., 2000)

Notes: Figures represent unstandardized coefficients (standard errors); <sup>a</sup> Coefficient multiplied by 100 to show significant digits; <sup>b</sup> Reference category is “services”; <sup>c</sup> Reference category is “employee”;

\* p < .05; \*\* p < .01; \*\*\* p < .001

**Hungary.** Age and place of residence make no statistically significant difference on individuals' earnings. According to Gal and Kligman<sup>59</sup>, the pre-1990 gender inequalities have persisted and sharpened during transition. While my data does not allow me to address the range of gender inequalities before and after 1990, the results of my analyses confirm, at least, the existence of such inequalities: all other factors being equal, Hungarian men earn 17% more money than women.<sup>60</sup>

Consistent with findings of previous studies<sup>61</sup>, education plays an important role during transition. As shown in Table 4, each year of schooling increases an individual's income by 11%. Controlling for other factors, being an employer and a self-employed individual increases a respondent's income by 56% and 40%, respectively.

Ten years after the formal demise of "Goulash communism," respondents who enjoyed some sort of authority during socialism do not earn more than other individuals. This finding supports Eyal et al.'s earlier claim that, in and of itself, an individual's position of authority before the collapse of communism would become less and less relevant during transition in Hungary.<sup>62</sup>

**Poland.** The gender inequalities mentioned in the Hungarian case are also present in Poland, where men earn 25% more than women. Age has significant, positive effects on income, meaning that each year increases an individual's income by 7%. Like in Hungary, in Poland too, education has a significant contribution to one's earnings: controlling for other factors, each year of formal schooling translates into 7% surplus money. Unlike in Hungary, where employers and self-employed individuals are better off than employees, in Poland only employers command significantly higher income returns than other individuals. As shown in Table 4, being an employer in Poland increases one's income by 67%. Further, Poles who had at least three subordinates in 1988 have no significant income advantages as compared to other people.

**Romania.** Urbanites and men enjoy significant advantages as compared to other Romanians in the labor force. The former earn 21% more than rural residents and men make 39% more money per month than women. Notably, the effects of education on individual's earnings are positive, even though these effects are smaller than in both Hungary and Poland. Each year of education increases a Romanian's monthly income by 6%. However, income differences between entrepreneurs and employers are significantly higher in Romania than in Hungary and Poland. Being a self-employed with employees during post-Ceausescu's era increases one's monthly income by 79%; similarly, self-employed individuals make 45% more money than employees.

<sup>59</sup> S Gal & G Kligman, *The Politics of Gender after Socialism*, Princeton University Press, Princeton, 2000.

<sup>60</sup> In what follows, the net effects of various independent variables on individuals' incomes are obtained from the coefficients presented in Table 4 by applying the formula  $100(e^b - 1)$ .

<sup>61</sup> Eyal et al., 1998; Hanley, 2000a; Róna-Tas, 1994.

<sup>62</sup> Eyal et al., 1998,



## 6. Summary: Similarities and Differences among Hungarian, Polish, and Romanian Post-Socialist Small Entrepreneurs

Market transition studies – which, by the mid-1990s, have become regular features in mainstream American sociological journals – have generated a heated debate over the winners and losers of post-socialism. Many such studies, however, relied on data collected in the early years after the collapse of Eastern European communism. Employing 2000 data, in this study I explored the contours of small entrepreneurs in Hungary, Poland, and Romania – a case infrequently included in sociological analyses of post-socialist transition. Keeping in mind the already discussed limitations of these 2000 surveys, I outline below the major findings of my analyses.

*Entry into Entrepreneurship.* Human capital, as captured by an individual's education, plays an important role in this story of entrepreneurship: each year of formal schooling increases the chances of being an employer in Hungary and Romania. This is consistent with arguments advanced by Nee's "market transition theory"<sup>63</sup> and by the "post-socialist managerialism"<sup>64</sup> thesis that emphasize the increasing importance of human capital as a rewarding principle in post-socialism, especially in the case of rather complex, elite forms of entrepreneurship. Notably, education also has positive effects on entry into self-employment in both Hungary and Poland. Only in Romania, self-employment has low entry barriers in terms of human capital; in this case, the negative effect of education on being self-employed is similar to the effects found a decade earlier by Róna-Tas in Hungary.<sup>65</sup>

Based on Szelényi's work on socialist entrepreneurs<sup>66</sup>, the "capitalism from below" thesis suggests that such individuals are more likely than others to be entrepreneurs during post-socialism. This is so because they have the "proper" understanding or the cultural capital necessary to operate in a market environment. My analyses support this contention: in all of these three countries, as compared to other individuals, former socialist petty bourgeois are more likely to operate as small entrepreneurs. In Hungary, individuals who were self-employed in 1988 are also well represented among employers, which could be interpreted as a sign of upward mobility.

Consistent with Eyal et al's arguments, individuals who enjoyed some sort of authority before 1988 do not have a statistically remarkable presence among post-socialist entrepreneurs in Hungary and Poland (for the Polish case, see Hanley<sup>67</sup>). Notably, this also seems to be true in the case of Romanian employers. However, Romanians who had at least 3 subordinates in 1988 are more likely than other individuals to be self-employed in 2000. Finally, unemployment seems to function

<sup>63</sup> Nee, 1989.

<sup>64</sup> Eyal et al., 1998.

<sup>65</sup> Róna-Tas, 1994.

<sup>66</sup> Szelényi, 1988.

<sup>67</sup> Hanley, 2000a; 2000b

as a push-factor for entry into self-employment only in Hungary and Poland but not in Romania.

*Income Returns to Entrepreneurship.* Irrespective of the factors that push some individuals into the private sector as entrepreneurs, being a businessperson is an extremely lucrative activity in all of these countries. The median monthly incomes of employers and self-employed show that, in most cases, entrepreneurship is a road to riches: most entrepreneurs in these countries have higher median incomes than employees (for the use of this indicator, see Hanley<sup>68</sup>). Only for the agriculturally self-employed in Poland and for the Romanian self-employed in services, entrepreneurship does not seem to be a road to riches (i.e., the median income for both categories is smaller than the median income of employees in the same sectors).

From a causal perspective, I have emphasized the net positive effects of education on individuals' income in all of these countries. Similarly, being an employer is associated with significantly higher incomes than being an employee in all of these three countries. Age, another human capital indicator, makes a statistical positive difference only in Poland, where each year increases one's earnings by 7%. Self-employed individuals command more money than employees in Hungary and Romania but not in Poland. In terms of business sectors, as previously discussed, agriculture in Poland is associated with low income returns; in Romania and Hungary, operating in industry increases an entrepreneur's income by 8% and 13%, respectively.

Let me conclude this study by addressing the differences in the net effects of some independent factors on income returns of those in the labor force. As we move from Hungary to Poland to Romania, we note the increasing disparities between men and women's earnings. The largest net effect of gender on income is recorded in Romania, where men make near two fifths or roughly 40% more money than women.

Furthermore, it seems that the longer a country's history of economic reforms, the larger the effects of education on earnings. Each year of education increases a Hungarian's income by 11%, while for Romanians – whose country has had the shortest and most convoluted history of economic reforms – each year of formal schooling translates into 6% surplus income.

While in Romania self-employed individuals make on average less money than Polish and Hungarian entrepreneurs, Romanian self-employed with employees earn significantly more money than their compatriots who are employed. Specifically, Romanian employers and self-employed individuals make 79% and 45%, respectively more money than employees. In Hungary, the net effect of being an employer on income is 56%, while in Poland is 67%. In the latter country – which, by most accounts, has undergone the most radical economic restructuring in the

<sup>68</sup> Hanley, 2000a.

early 1990s – self-employment has no significant effects on an individual’s earnings. The picture sketched above suggests that these three countries’ socialist and post-socialist histories have had different effects on the rise of small entrepreneurship, and – following Fligstein<sup>69</sup> and Verdery<sup>70</sup> – it shows that market construction is a historical process and a political business.

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<sup>69</sup> N. Fligstein, “Markets as Politics: A Political-Cultural Approach to Market Institutions”, *American Sociological Review*, vol. 61, 1996b, pp. 656-673.

<sup>70</sup> Verdery, 2003;

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