Keynote Speech

Competitiveness of Companies and Sectors on the Road to the European Union

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It is now nearly two decades since the collapse of the Soviet Union and the failure of other economic systems that relied on central planning, state ownership of the major factors of production, and protection from competitive and market forces. It is generally accepted that a competitive economic system, based on market determined prices, transparent information, and the unfettered movement of resources is currently our best hope to achieve rapid overall economic growth and high standards of living. However, we have also learned during this period that finding this preferred road to prosperity, keeping up with the "traffic", and even staying on the path is not simple. It requires patience, a tolerance for uncertainty, and a willingness to take risk. Consumers, businesses, governments, and educational institutions need to move out of their traditional "comfort zones", embrace change, and take advantage of opportunities. Otherwise, they risk being left by the roadside as other businesses, countries, and citizens improve their positions.

In this paper I will review what are considered to be key aspects of economic success in the first part of the twenty-first century. I will then describe some of the central aspects – and challenges – facing the most successful economic union in the world today, namely the union of the 50 "states" in the United States. I will then turn to the importance of new and effective management and the role of advanced management education. "Lessons learned" from the new International Graduate Business School's (IGBS) MBA in Zagreb will be shared.

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A simple prescription for economic success for a business, especially one competing in the dynamic environment of the information age of the twenty-first century involves five factors:

1) Create a product or service of value to customers.
2) Keep costs low. Strive for efficient operations.
3) Develop a pricing scheme that captures much of that value for the firm.
4) Grow the market through effective marketing and promotion coupled with a dynamic innovation strategy.
5) Retain the customers so that they are "locked in" and view the firm as the default supplier.

Many business people try to succeed in an increasingly competitive market environment by focusing on step #2: lowering costs, retrenching, and competing by being the low cost supplier. In the short-run this can be an effective strategy, but in the limit it can deteriorate into what might be described as the "anorexic theory of management". A lean operation does have low costs, but it will not be an engine for economic growth, employment opportunities, or sustainable profits.

A more successful strategy is one that combines a focus on efficiency with a growth strategy. The *Wall Street Journal* last month[1] suggested that growth is critical if a firm wants to attract and retain talented employees. However, growth – either internally generated or through mergers and acquisitions – will be successful only if the firm's core business dimensions are recognized for their high quality. Growth for its own sake has little value. It needs to go hand-in-hand with increases in profits.

The papers in this session are important contributions to the understanding of what are the keys to business organizational success and investment and economic growth in transition economies. The paper by Svetlana Avdasheva provides a valuable insight into the way in which enterprises, more precisely, "business groups", are organized, managed, and controlled in Russia. The study by Tatiana Dolgopyatova looks at the important relationship between organizational structure and performance. As with the situation in many other countries, this analysis finds little relationship between the structure of corporate ownership and control on performance. There is no one structure

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[1] *"The Best Ways to Grow" the Journal Report: Leadership, Wall Street Journal, October 25, 2004, Section R.*

that clearly dominates others in terms of performance. The study by Malgorzata Runevic shows the importance and effectiveness of foreign direct investment in stimulating economic growth in the Baltic States. FDI, especially when it comprises a large proportion of total investment as it does in these countries, can be critical in enhancing the export competitiveness of various sectors.

It is generally accepted that a market based competitive economic system must have a clearly defined and consistently applied system of rules and expectations, especially as they relate to contracts and property rights and the transparency of accounting and financial information. We have also learned that high rates of productivity require unconstrained investment opportunities in the basic factors of production: labor, capital, land, and technology. Free movement of these factors of production, so that they can achieve their highest and best use, is a prerequisite to an effective economic system and a country's long run competitiveness in a system of open economies. That is not to say that there is no role for government in facilitating such an economic system and speeding up the transformation process. Yet it is important for government policy to be forward looking. Its emphasis should not be on protecting the status quo, subsidizing inefficient operations, or protecting businesses or workers from competitive forces. Instead it needs to let the system work, where "winners" truly succeed and reap the benefits whether they are generated by inventive technology, forward thinking and creative management, good timing, or even luck. In contrast, governments need to have a system where failures are truly the end, where bankruptcy means equity positions are lost and workers must find new positions, albeit with the possibility for government help with retraining and other adjustments but without a "safety net" that might become too comfortable.

The economic system in the United States is far from flawless. The recent corporate scandals (e.g., Enron, WorldCom, Adelphia, and Qwest), corruption and incompetence by accounting firms which led to the collapse of the accounting firm Arthur Andersen and the passage of the Sarbanes-Oxley Act, and recent investigations of the mutual fund industry and the insurance brokerage business indicate that there certainly is room for improvement. Yet a fundamental strength of the U.S. economic system is the free trade zone among the fifty states. Each of the states might be viewed as countries with its own government, parochial interests, and economic units that promote their narrow economic interests, especially protection from competition. Yet the U.S. has prospered as a whole by being willing to sacrifice the interest of the few for principles as diverse as a common currency, the free movement of labor and capital, and standard and reasonably transparent accounting and financial systems.

The role of education, especially management education, is another area where government – and business – investment is needed and is likely to produce high rates of return. This is especially true in economies that are still in the transformation process and face increased competition – and potential business opportunities – from the European Union whose educational institutions are emphasizing management education and are moving up in the raking of top MBA programs.[2] Later in this paper I will describe the case study of the development of a full-time MBA program at the International Graduate Business School - Zagreb and "lessons learned" from that experience.

The importance of managerial and technical education is likely to increase in the future. A recent study by Fernald and Ramnath (2004) found that there was an acceleration in total factor productivity in the United States starting in the mid-1990s. They give a substantial amount of credit to the information and communications technology (ICT) sectors of the economy. Yet they find that the majority of the acceleration in the rate of growth of total factor productivity did not occur *within* the ICT industries. Instead, they found most of the acceleration to be occurring in the way in which ICT technology is *used* in a wide range of sectors in the economy. They find that sectors as diverse as wholesale and retail trade and banking have combined ICT innovations with numerous organizational changes to lower their costs, expand the range of their goods and services, and improve their service quality. All these changes require a different level of management training and leadership skills than are found in traditional educational programs or via on the job training.

The importance of management education in a competitive economic system is emphasized in a recent book by Robert Anderson (2004), a former World Bank consultant. He concludes his review of challenges and constraints facing countries that are trying to improve their economic growth rates by stating:

> When business people are asked why their company's performance is so bad, they are likely to blame the banks for not giving them loans to modernize, high interest rates, high taxes, government corruption, or bad infrastructure such as roads or power supply. They rarely blame their own inadequate management. McKinsey [A series of country studies conducted by the McKinsey Global Institute] concludes that poor management is often the most serious problem

[2] *See for example the special section, "FT Business Education", in the Financial Times of Monday, November 1, 2004.*

> and is frequently caused by lack of competition. In other words, these companies can still be profitable without improving their performance because they face little competition. Owners and managers have little incentive to change.[3]

Clearly in Europe in the twenty-first century the "incentive to change" has occurred and will continue to increase. Advanced management education is certainly not a sufficient condition to ensure sustained economic growth and business success. However, it is increasingly clear that it is a necessary condition to achieve these objectives.

Let me turn next to a description of the efforts that my university has made in establishing a high quality management training program in Croatia. I will explain the background, indicate the adjustments that had to be made, and describe the MBA program that started in January 2004. I will summarize with "lessons learned" from this experience.

In August 2001, the Kelley School of Business at Indiana University was awarded a grant from the U.S. Department of State to work with a Croatian partner in developing a high quality, full-time, English language MBA program. The Request for Proposal (RFP) designated the Consortium of Faculties of Economics in Croatia (CFEC) as that partner. In the process of program development, IU was also charged with assisting in Croatian faculty development to upgrade teaching methodologies and curriculum content. Over time, these faculty would take on curriculum delivery in the MBA program, helping to ensure the program's sustainability.

CFEC representatives were appointed by the deans of each of the four faculties – the Universities of Osijek, Rijeka, Split, and Zagreb. Given the population of Croatia – approximately 4.5 million – the establishment of one high quality MBA program would be sufficient to satisfy the country's need for highly skilled managers, certainly for the next decade. By pooling their human and capital resources, and with the assistance of State Department funding and an experienced U.S. partner, all constituencies would benefit. These constituencies included:

- all four Faculties of Economics,
- the Croatian business and policymaking communities, in great need of trained managers,

[3] *Anderson (2004, p. 231).*

- the pool of prospective students and, ideally,
- the Southeastern European region through the development of a cadre of skilled managers with an established network.

The U.S. partner, Indiana University, would also benefit by extending and deepening its experience in transition economies and developing a new international partner for future collaborative activities.

Lessons Learned

The Consortium Model

The concept of a consortium, particularly in a small area (a country, region, province) or in a highly specialized field, is appealing for many reasons. A cohesive consortium can pool limited resources, avoid unnecessary redundancy, share risks, and build on the comparative advantage of its members to create a higher quality product or service. In Croatia, with a total population of approximately 4.5 million, limited resources, and a pressing need for a skilled management force in the short – as well as longer – term, the idea of a collaborative effort among the Economics Faculties of the country's four universities to create one high quality management training program makes eminent sense. The introduction of an experienced outside partner to serve as advisor should provide valuable assistance and support to the consortial effort, lowering the learning curve, minimizing the risks, and supplementing resource constraints of the consortium. In doing so, the external partner should quicken the development process and enhance the likelihood of a project's success.

IU's experience with the Consortium of Faculties of Economics in Croatia (CFEC) revealed a simple but fundamental requirement for a successful consortium-based project. *There must be a clear project objective on which all members agree.* In the Croatian project, the lack of agreement on a clear objective by all partners predestined failure – not necessarily failure of the project's goal, but rather of the consortium model to achieve that primary goal.

IU was aware that politics would play a significant role in the MBA program development project. The University of Zagreb is, after all, the oldest, largest and, from its perspective, the best academic institution in Croatia. It came as no surprise to learn that Zagreb intended to be the ’first among equals’ and to make key decisions throughout the development process, even beyond. While surely chafing under this attitude, Osijek, Rijeka, and Split decided that the potential benefits of being ’in’ rather than ’out’ exceeded the costs of inevitable jockeying for position within the Consortium. IU, on the other hand, was committed to an open, collegial process.

After reflection and extensive discussion, it was decided that a successful MBA program needed to be in the population, business, and governmental center, namely Zagreb. Further, it was decided that to avoid internal discord among the faculties it was important to operate with a single entity who would be a true academic partner. We were able to develop this relationship with the Institute of Economics, Zagreb (EIZ) and used its facilities to start the full-time MBA program in January 2004.

Challenges Faced

Full-Time vs. Part-Time

Graduate programs in Croatia are part-time programs – this is the accepted norm. The RFP called for a full-time MBA program, and IU agreed with the logic of an intensive course of study. A full-time program could generate highly trained managers in a short period of time. In discussions with business members in Zagreb, for example, it was common to hear that an individual had been enrolled in a part-time MBA program for up to 7 or more years.

IU was cautioned against trying to introduce a full-time program by almost every Croatian, whether from academia, the business community, or the government. The Consortium assured IU that a full-time program would never attract students, and even the Institute of Economics was uneasy with the notion. While the IU planning team took seriously the concern and discussed among themselves the challenge this would be, IU decided this was a risk that had to be taken. Croatians, IU pointed out, were well aware that the most highly rated MBA programs in the U.S. and Europe are full-time. The new Croatian MBA would rival those high quality programs only if it adopted similar standards – excellent faculty, talented students, and an intensive course of study, the value of which would be evident in the product. While willing to discuss the issue at length, IU had decided that this was a key element of the program, and a barrier worth breaking. The full-time program would have to be marketed with skill to recruit the first class of students; in years following, IU believed, the quality of the graduates themselves would be an outstanding marketing tool, even if the program structure needed to be modified to meet demand.

IU – and the MBA program itself – was incredibly fortunate to have an energetic, intelligent, and committed Croatian team for what was an inconveniently short recruiting season, particularly in light of the challenges we faced. Today's 2004-05 MBA class is composed of fourteen extremely bright and hardworking young men and women. In the end, IU concurred in the decision to allow two of these students to complete the MBA in a staggered manner. The two students are company-sponsored, and their employer requested this exception in light of the small window between admission into the program and the employer's need to absorb or reallocate ongoing work projects for the periods the students would be away.

Challenges Ahead

Short-Term

1) The key challenge facing the IGBS MBA program in the near term is the recruitment of a second class of MBA students. In light of the outstanding quality of the first class, IGBS and its partners will have to be very careful in reviewing applications and recommendations. Maintaining the high quality of the opening class, and its faculty, will make an important contribution to longer-term sustainability.

   Partners have agreed that the class of 2005-06 should be larger than the inaugural class. A student base of 20 to 25 will help the School's financial prospects, as grant funds become depleted, and continue to draw attention to the program. A "stretched" two year version is being considered.

2) A second challenge concerns MBA program personnel. The talents of entrepreneurial administration are not highly developed in many transitional states, as these professional positions are relatively new. This is the case in Croatia. However, IU and the Institute of Economics seem to have found the ideal Administrative Director in winter 2003. A former employee of the Ministry of Economy, Mr. Neven Trbovic is surprisingly insightful about the elements that are

needed to produce a high quality MBA program. He is also talented and energetic enough to make sure they are in place. Trbovic helped draft the IGBS promotional material – indeed, he designed what has become the IGBS logo – laid out an administrative plan that included all the key aspects that the Consortium had been exposed to during their week-long visit in February 2002 (marketing approaches and audiences, student recruitment, application criteria and procedures, tuition policies, alumni development – still comparatively uncommon in Europe – etc.). Trbovic's relations with students and faculty are excellent, and he is an important representative of IGBS Zagreb and the MBA program. Retaining Trbovic's commitment to the program and his services is very important to the success of the project in the next two years. His assistance in any inevitable transition will also be extremely valuable.

IGBS was fortunate to have an outstanding academic with extensive experience in U.S. business schools, Prof. Sonja Radas, as its first dean. Prof. Radas, with a background in Marketing, was extremely helpful in the recruitment of the first IGBS MBA class, and she understood the importance of faculty and course materials to the academic quality of the MBA program. Nevertheless, Prof. Radas is a scholar at heart and, after devoting great energy to the start-up process, she chose to return to research. Her successor, Dr. Zlatan Fröhlich, engineered a seamless transition and, it appears, is an excellent match for the current needs of the program. As an academic active in the policymaking and business worlds of Croatia and Europe, Dr. Fröhlich has excellent ties to business executives and economic policymakers. Thanks to his efforts, Kelley School of Business faculty have been able to include key guest lecturers in the classroom, and to arrange field trips to companies that typically result in an interaction with the CEO. The project is very lucky to have Fröhlich as dean, and anticipates his continued commitment to the program.

Long-Term

The long-term challenge for the IGBS Zagreb MBA program is sustainability. In the first, and likely in the second, years of the program, reliance on the support of the U.S. State Department has been essential. Also key has been the participation of Kelley faculty, which will continue in 2005-06. Yet, the program must begin to include non-Kelley and non-U.S. faculty to help guarantee its sustainability. Of course, if the program can generate sufficient revenue, 'outside' faculty can continue to participate. A number of Kelley faculty who were involved in the development of an MBA program at the

University of Ljubljana, Slovenia, in the early to mid 1990's continue to teach there, despite the fact that there is no U.S. government support and stipends for teaching are tiny. It is hoped that such relationships will grow out of the Croatian project as well, but the number will not be sufficient to deliver the entire curriculum.

Experience to date has been that Croatian faculty do not yet feel comfortable teaching side-by-side with Kelley faculty. There is also the political issue of Croatia's Economics Faculties boycotting the program, though we believe that is (a) a short-term phenomenon, and (b) there are not yet, unfortunately, sufficient Croatian faculty to deliver a top quality MBA curriculum.

IU is currently scheduling faculty for the 2005-06 year, and it is our intention to seek non-Kelley faculty – from the U.S., Europe, and Croatia – to deliver as much of the curriculum as possible, while not jeopardizing the quality of the program. Helping IGBS over this hurdle is the next important task of the U.S. partner.

References

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