The Effect of Enterprise Strategies Employed During the Crisis on the Growth Options of Companies

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SUMMARY
The recent worldwide economic crisis had drastic consequences for the economies of nations around the globe. As we are at the end of the crisis period, the really interesting strategic question is: what will happen after the crisis. We have some, but only limited, research evidence to answer this question properly. Scholars try to obtain answers by studying the consequences of the previous crisis periods. However, the recent crisis was unique in its expansion and rather accelerated spread all over the world. The present paper attempts to analyze this issue from a company-level point of view. We are interested in learning what has happened during the crisis, and what the reactions of companies were to the emerging new economic, technological and social conditions. The author has conducted empirical studies in Hungary and in the Slovak Republic. The empirical background of the paper includes studies of publications of research groups engaged in doing surveys in the field, as well as primary data collections through questionnaire surveys and interviews conducted in Hungary and in Slovakia.

Keywords: economic crisis, enterprise strategy, adaptation, innovation

Journal of Economic Literature (JEL) codes: M200, L1, L210
DOI: 10.18096/TMP.2015.01.01

INTRODUCTION

The recent worldwide economic crisis had drastic consequences for economies around the world. Cross-border business and international trade declined in 2009 by about 9%, while foreign direct investment dropped by more than 40% in the same year (Ghemawat, 2010). While the leading nations of the world economy were plagued with recession, countries like China and India continued their growth path. In 2009 China realized 66% of the global growth in GDP, and India 11% (Ghemawat, 2010). The projected high growth rate of the BRIC countries will lead to radical restructuring in the world economy with North America and Europe losing their previous political and economic influence.

The crisis has had an enormous influence on the transforming Central and Eastern European economies as well. Some of these countries, like Hungary, Romania and Bulgaria had serious difficulties due to macroeconomic imbalance and increasing inflation (L. Muraközy, 2010). These countries were not prepared for the consequences of the rapidly spreading crisis, and – contributing further to the difficulties – seriously underestimated the possible extent of the crisis. At the end of the crisis, the really interesting strategic question is what will happen next. Will the development path repeat the tendencies followed before the crisis, or will totally new directions of development emerge? We have rather limited research evidence to answer this question properly.

Scholars try to get answers by studying the consequences of the previous crisis periods (Gulati, et al. 2010). But the recent crisis was unique in its nature, expansion and rather accelerated spread across the world, and therefore it is not certain that the processes will be the same as in recovery from earlier crises.

This paper tries to analyze the above issue from a company angle. We are interested in learning what has happened in companies during the crisis, what their reactions were to the emerging new economic, technological and social conditions, and what tendencies of development may be identified recently. The empirical
background of the paper includes an analysis of publications of researchers engaged in doing surveys in the field (e.g. Ringland et al. 2000; Waldman, 2010), as well as primary data collections through questionnaire surveys and interviews conducted in Hungary and the Slovak Republic.

MACROECONOMIC BACKGROUND

Hungary and Slovakia have many similarities concerning their social, economic and political heritage dating back to the period before the political changes around 1990 (Kiezun, 1991). But behind these similarities there are interesting alterations in the patterns of development, especially after 1990 (Balaton, 2007).

Hungary was rather successful in hosting a relatively large volume of foreign direct investments (FDI) during the first half of the 1990s. The Hungarian Government decided to adopt the sales type of privatization. This meant that state owned firms were offered for sale to those who could offer acceptable prices for the companies. As capital inside the country was rather limited, that type of privatization resulted in the overwhelming role of foreign investors in the ownership structure of enterprises located in Hungary by the end of the century.

Slovakia (and, until January 1993 Czechoslovakia) followed a different economic policy concerning privatization. Vouchers were distributed among the population and these vouchers could be exchanged for shares of state owned enterprises. The shares were then purchased by the investment funds owned by state owned banks. So the “privatization” had resulted in restored state ownership of enterprises by the mid-1990s. No relevant structural changes were implemented during the first half of the 1990s (Clark and Soulsby, 1999).

This policy had temporary macroeconomic advantages compared to Hungary. While in Hungary the restructuring was relatively accelerated it resulted in a high level of inflation (about 39% in 1993), a depression (38% GDP decline between 1989 and 1993 measured by comparable prices), and an unemployment rate of about 17% (Kornai, 1993), while in the Czech Republic and Slovakia there were no such radical consequences. Economic restructuring took a major step after the involvement of foreign direct investors during the second half of the 1990s. The necessary restructuring resulted in economic slow-down, inflation and increasing unemployment as well, but these consequences were moderate in their extent compared to those of Hungary.

Slovakia was rather successful since the second half of the 1990s in inviting foreign direct investors, especially in the automobile industry. This fact contributed to the relatively fast growth rate of the Slovak Republic around the turn of the century and helped the integration of Slovakia into the European Union. The growth rate of the country even accelerated after the integration and this resulted in the capability to change to the euro as the national currency in 2009.

In the same period Hungary became less attractive for foreign investors, partially due to high tax rates and increasing level of macroeconomic instability, parallel with rapidly spreading corruption. During the period between 2002 and 2010 the economic stability of Hungary eroded and the county became incapable of introducing the euro. State expenditures exceeded the level of income and the county was near to bankruptcy during the summer of 2010. The newly elected Government has introduced radical measures to restore the balance and their results could be observed after 2011.

PREVIOUS RESEARCH EVIDENCE ON STRATEGIC CONSEQUENCES OF THE CRISIS AT ENTERPRISE LEVEL

The start of the late economic crisis was marked by Lehman Brothers filing for Chapter 11 bankruptcy protection on September 15, 2008. Within six months the crisis has spread throughout the world and endangered many previously successful economies like Ireland. Even economically stable economies like the US, Germany and France were seriously hit and the consequences would influence the coming years in nearly all countries of the world.

As the crisis had approached its end, more and more scholars were interested in discovering what would happen after the crisis. Harvard Business Review has published a series of three papers in the March 2010 issue, spotlighting the topic of strategy in a weak recovery. The articles by influential authors such as Pankaj Ghemawat, Ranjay Gulati, and Nitin Nohria agreed that rather limited research evidence was available in the field and they tried to get ideas by studying the experiences of the previous crises since 1980. Although the authors admit that the previous crises were much more limited in their expansion and were also different in their origin and nature, they arrived at some conclusions worth having in mind when thinking on possible future enterprise strategies after the present economic crisis. One of the important conclusions drawn by Gulati et al. (2010) is that concentration only on cost-cutting during the crisis is unlikely to lead to successful expansion after the crisis (Gulati et al., 2010). The authors found that emphasis on operational efficiency parallel with concentration on market development and asset investment have resulted in the best results measured by increase in sales income and earnings before interests, taxes, depreciation and amortization (EBITDA) (Gulati et al., 2010). Mere concentration on reduction of employment level and cost cutting did not result in successful recovery after the crisis. It is also noteworthy from their study that concentration only on innovation and asset investment during the crisis was not connected to
successful enterprise performance after the crisis. So neither restriction nor mere innovation in itself seemed to be the proper cure during the economic crisis. Another lesson to bear in mind is that rapid, short term solutions often have disadvantages when evaluated by taking into account consequences in the long run (March, 2003).

Ghemawat (2010) forecast the possibly more important role in adapting to local norms and the growing organizational power of the local country. Parallel with increased pressures on pricing, multinational companies have to be sensitive to regional varieties of offering, as local differences will become more important. These organizational changes will increase diversity within multinational firm, but at the same time they will increase the need for cohesive corporate cultures and tightening talent management practices (Ghemawat, 2010).

As a consequence of the accelerated changes and turbulence during the last few years some authors speak about the next wave of creative disruption. Waldman in his recent book postulates: “In fact, the growth of the mobile internet, the return of economic growth after 2012, and the constant potential for entrepreneurs to come up with products and service that satisfy fundamental consumer need are, I believe, going to drive another great wave of creative disruption in the near future.” (Waldman 2010:46). He than states, “I predict that the era of creative disruption has only really just begun.” (Waldman, 2010:48).

The radical strategic changes that may emerge during the coming years will probably have an influence of the organizational structures and processes companies will be adopting. Ringland et al. (2010) speak about double-cone organizations where traditional hierarchy dealing with specified and routinized activities will be existing parallel with activities characterized by lack of clarity, ad hoc solutions, private inspiration, and luck.

Summarizing the above discussed predictions for the after-crisis situation it may be perceived that there seem to be limited possibilities for using the previously prescribed solutions. Learning, adaptation to emerging new situations and flexibility may be regarded as crucial capabilities that organizations of the future will need in order to be competitive. Bahrami and Evans have formulated that requirement as follows: “The object of becoming super-flexible is to be able to either intentionally precipitate a transformation, or to make modifications in response to changing situations. Adaptation occurs either during the course of, or after, an unfolding change episode, and may simply be random in that one may be just at the right place at the right time.” (Bahrami and Evans, 2005:22).

Research methods utilized in both countries included questionnaire surveys, interviews with top managers, analysis of company documents and case study development.

The Hungarian surveys were part of a larger research endeavor aiming at studying the competitiveness of Hungarian enterprises. The first survey was conducted in Hungary between April and November 2009. The author’s personal involvement in the research was connected to developing the questionnaire and analysing the survey data and writing working papers. The survey collected answers from 1,246 top managers working in 313 enterprises, belonging mainly to the SME sector. Distribution of firms according to the number of employees was as follows: 21% of the firms had below 50 employees, 47% between 50 and 99 employees, 20% between 100 and 249, and only 2% had more than one thousand employees.

Manufacturing industry companies represented 42.4% of the sample, service firms had a ratio of 23.0%, and trading companies 19.1%. In data analysis descriptive statistics, correlation analysis, factor and cluster analysis were use. The empirical findings used in the present paper were published in the Preliminary Report of the survey (Chikán et al., 2010).

The second survey was conducted between May and November 2013. The survey collected answers from 1,200 managers of 300 enterprises. Size distribution of the sample according to number of employees was as follows: 11% of the firm employed less that 50 persons, 48% between 50 and 99 employees, 26% between 100 and 249 employees, and 16% had more than 250 persons.

Distribution of companies according to branches of the economy was the following: 8% of firms belonged to agriculture, 45% to the processing industry, 4% to the supply of electric energy and gas, 8% to the construction industry, 20% to trade, 6% to the hotel and catering trade, and 9% to logistics. Data analysis methods were the same as in 2009. The findings were published in the Preliminary Report of the survey (Chikán et al., 2014). The present author’s personal involvement was participation in revising the questionnaire.

Overlap of the companies in the two surveys is limited, although in the survey of 2013 each of the companies were asked who participated in the previous survey in 2009. The structure of the two samples is similar according to size and profile of companies.

In Slovakia the questionnaire survey, the case studies and the interviews were conducted by graduating students at master’s level under the supervision of the author. The Slovakian questionnaire survey was conducted between September 2008 and February 2009, and included 200 companies. Distribution according to the number of employees was as follows: below 10 employees: 34%, between 10 and 49: 39%, between 50 and 99: 14%, between 100 and 249: 13%. Of the firms, 49% of the firms belonged to the service sector, 34% to industry, 4% to agriculture, and 12% to public administration (K.
REATIONS OF ENTERPRISES TO THE CRISIS IN HUNGARY AND SLOVAKIA

In this section we summarized the findings of the empirical research conducted in the two countries.

Hungarian experiences

As it was mentioned above, in Hungary there were two surveys during the period of the economic crisis. Below we provide a short account of the major findings.

Survey results from 2009

The empirical evidence from the questionnaire survey of 2009 in Hungary shows that the first – and most frequently observable – reaction of enterprises was to reduce cost levels, to downsize operations and to reshape organizational structures towards more simple and less expensive management systems. This is the traditionally observable reaction of companies and this strategy is most frequently advised to company managers by standard textbooks of economics and management. This strategy has resulted in many cases in the capability to survive the crisis situation and preserve conditions for continuing business activities when the crisis reaches its end.

Our sample shows that 34.6% of the companies suffered a decrease of more than 10% in domestic sales turnover in 2009 compared to the previous year, while 20.3% experienced a less than 10% decrease. Of the firms, 24.5% of the firms reported stagnation in their domestic sales. 35.9% realized less than 10% growth, and 15.0% managed to increase domestic sales turnover by more than 10%.

In export sales 40.4% of the companies reported an annual decrease of more than 10%, and 20.2% less than a 10% decrease. Of the firms in our sample, 18% experienced stagnation in exports, and 13.5% managed to realize modest growth (below 10%), while only 7% were capable of increasing export sales by more than 10%.

The crisis resulted in relevant changes in company strategies. While during the previous surveys (in 2004, 1999, and 1996) realization of profit was the most important target, in the 2009 survey 170 companies (60.3%) gave the answer that surviving the crisis was the most important aim, and 123 mentioned profit realization as the No. 1 strategic goal. There was no relevant difference among the companies according to their size. The most frequently followed strategy was defensive (26% of firms), and the shrinking strategy proved to be second most frequent (20% of companies). In 2008 growth oriented strategies were the most frequently observable ones (43%), and defensive strategies were followed by less than 10% of the firms. In 2009 companies mainly used their resources to defend their existing market positions. The defensive strategy in many cases was not the consequence of a purposeful strategy, but more as a result of a lack of strategy and a situation which might be described as muddling-through. Lack of clearly defined strategies was observed more frequently in case of smaller firms. We did not find any relevant effects of industry on the strategic orientation of firms.

It was a clear sign of defensive enterprise strategies that R&D was evaluated as the least important functional area within the company. 43% of the firms did not have branded products. The companies in our sample more frequently used the company name as the brand name, and only one fifth of the sample firms had an independent product brand name. The ratio of companies introducing new products and technologies had decreased compared to the previous survey in 2004. Companies generally complained that they got limited state support for innovation and lack of adequate financial resources was mentioned as a major reason behind the limited innovation. The importance of organization development was also under-evaluated by the responding managers. Modernization of organizational and management structures were given rather limited importance among the priorities of top managers.

The overall picture observable in the survey in 2009 shows a rather defensive management approaches where companies concentrated only on survival. They generally did not have strategies concerning how to start development, had rather restricted information on their future possibilities, and in many cases had no clear strategic direction. We could hardly observe any conscious steps to improve existing products or even more develop new products or upgrade technologies. The marketing efforts only concentrated on maintaining existing market shares and there were hardly any signs of trying to enter into new markets and develop products to be sold on new markets.

The overall picture of the Hungarian enterprises in 2009 showed that the necessary preparatory actions for the period after the crisis were missing in the practices of enterprise managers in our sample.

Survey results from 2013

In 2013, 46% of the companies reported declining sales possibilities in the domestic market, and only 18% of the respondents gave the answere that their sales options had improved in Hungary. Concerning export sales, the opinions were rather dispersed: 27% of the firms perceived improvement, while 25% saw declining sales possibilities abroad. The export sales was mainly oriented towards the developed Western-European EU member states. In 40% of the firms the export sales had increased in comparison to the value in 2009.
41% of the company top managers had the opinion that the crisis was more severe than they had expected it to be in the autumn of 2008. One third of the managers shared the opinion that the crisis was behind them, while 40% had the opinion that more than one year would be necessary to start growth. Another 17% gave the answer that growth might start within one year.

The influence of the crisis was mainly observable in the worsening liquidity of customers, in decreasing demands and in increasing environmental uncertainty. Between 2009 and 2012 the level of production had declined or stagnated in about 80% of the companies in our sample.

69% of the respondents shared the opinion that they fast adapters to the changing conditions. 57% of the firms did not have a written strategy, but had a shared picture for the future. The average time horizon of strategic planning had increased a bit compared to the previous survey. The percentage of companies developing strategies for the next 2 to 5 years had increased, while the ratio of firms having strategies for only the next 1 to 2 years had decreased. About half of the companies update their strategies annually. The most frequently observable strategy was concentration on stabilization, while during the previous survey a defensive strategy was the most widespread.

In strategy implementation the companies concentrated on product differentiation and quality improvement. Introduction of new products was not characteristic for the firms in the sample. In marketing, reduction of costs was a generally observable feature. The value of investments has decreased or remained at the same level in about two thirds of the firms. R&D expenditures have decreased in more than one third of the companies. Profitability did not reach the planned level. Strategic alliances had increased in marketing and sales, but not in R&D. At the same time the managers accepted the need for increasing R&D and innovation.

Comparing the survey results of 2009 and 2013, we can not identify drastic changes in the strategic orientation of Hungarian enterprises. There were, however, some weak signs of getting to the end of the crisis period and starting preparation for the future. This could be observed in the practices of product improvement and quality enhancement, and in emerging strategic alliances in marketing and sales. R&D and innovation, however, had not improved to any significant extent. It is a positive sign that enterprise managers had become aware of the need to increase their activity in R&D. It may be stated that enterprise managers were still in a waiting position – that is waiting for the start of economic growth – and their strategy was still waiting for this point before beginning innovative and growth oriented activities.

Slovakian experiences

The overall picture of the survey (conducted between September 2008 and February 2009) reveals that companies stagnated or decreased the volume of their output. A majority of the responding managers (59%) shared the view that the crises would last for about 2 to 3 years (the end of the crisis was connected to the start of an increase in the GDP of the country).

Labor costs were unchanged in 51% of the companies, while 26% reported a decrease, and another 15% forecasted changes during the coming months. A possible increase in wage level was mentioned by 5% of the respondents. Expenditure related to education and training was unchanged in 33% of the firms, decreased in 31%, and 21% of the managers expected a decrease during 2009.

Costs related to advertisement and communication remained unchanged in 34% of the firms, decreased in 29%, and an expected decrease was reported by 17% of the respondents. Expected growth of costs was mentioned by 13% of the companies in the sample. Overall marketing expenditure was unchanged (compared to the previous years) in the practice of 60% of the firms, a decrease was reported by 14%, and an expected decrease by another 14%. A possible increase in marketing costs was mentioned by 9% of the respondents.

Investments were reduced in 32% of the companies, 27% reported no changes, and 28% mentioned a possible decrease during the coming months, while an increase in investments was forecast by 12% of the firms.

The introduction of new technologies was reported as being unchanged in its intensity during the crisis by 56%, and decrease was mentioned by 13%. Possible decrease in the next years was predicted by 12%, and possible increase was mentioned by 15% of respondents. Increase in the intensity of introducing new technologies was characteristic for 4% of the firms.

Discussion

The most characteristic management strategy during the crisis in both countries was cost reduction and concentration on survival. However, other strategies were also observed which were connected to innovation and growth. This strategic approach was characteristic of enterprise managers having longer term strategic time horizons (Csiba, 2010). Another important influencing factor behind was the available financial resources to provide a possibility for executives to think ahead and start preparations for a possible growth period after the crisis. Our empirical studies show that this way of thinking was observable at the minority of enterprises especially in case of SMEs.

The entrepreneurially minded managers of the latter group of firms shared the view that the crisis period is not only an area with difficult problems to be solved in a short period of time, but at the same time it is a period of unprecedented opportunities to move forward and develop competitive advantages when increases in demand begin arriving (Waldman, 2010). These companies started to develop new R&D projects, invested in broader areas of innovation and now they are more or less prepared to
launch their new products and services which represent a higher level of technological development and meet customer needs at a higher level compared to the period before the crisis. Based on his previous experience and insights concerning the future possible directions of strategic development, the present author is convinced that the success stories after the crisis will be connected to enterprises following the innovation trajectory during the years of crisis.

Another field of development observable in our empirical studies is related to the increasing role of inter-organizational relationships through different forms of strategic alliances and emergence of clusters. The permanent need for cost efficiency and improvement of innovation capabilities drives companies towards new forms of strategic alliances, enhancing the capabilities of business firms to accelerate innovation, develop new capabilities through co-operation, share risks and make costly innovation projects financially realizable. These development tendencies have been observed especially in industries characterized by severe competition, high technological development rates, and needs for meeting new customer expectations (see Hokansson and Lind, 2004).

CONCLUSIONS AND FURTHER RESEARCH

We have to admit that the available empirical evidence is rather limited from the point of view of making a general forecast for future development tendencies. However, the observable intentions of enterprises provide possibilities for drawing attention to the emerging new tendencies and new strategic logic developed by enterprise managers. Further and more extended studies will be necessary to check whether the directions of development indicated by the studies presented here are broadly expanding new tendencies of enterprise level strategic management or they are only locally observable examples.

It was observable in both the Hungarian and the Slovakian sample that perceptions and intentions of managers with an influence on strategic directions of their firms have an important role in understanding the emerging strategies during and probably after the crisis. Therefore, there is a need for further and mainly qualitative studies concentrating on behavioral patterns of strategy formulation. The approach to strategy advocated by Henry Mintzberg and others (Mintzberg, 1994, Mintzberg et al., 1998, March, 1991, March, 1994). Both the literature and our empirical experience show that managers frequently show a preference for actions having an influence on the performance of their company in the short term, and thus short-term survival motivations outperform longer-term innovation and renewal. This is the issue described by March (1991) as the dilemma between exploitation and exploration. Short term – even quarterly – interests of managers in producing the financial results expected by shareholders work against renewal and longer term prosperity.

We have rich ideas supported by theoretical arguments and empirical evidences under the heading of “ambidextrous organization” (Skat-Rordam, 1999; Tushman and Anderson, 2004; Hokansson and Lind, 2004; Hokansson, 2010). The research work and the paper by Hokansson and Lind (2004) open up a new dimension of hopefully fruitful studies by drawing attention to the inter-organizational dimension of ambidexterity. Approaching the problem of how to meet the contrasting requirements of short-term efficiency and longer-term innovation, we are often faced with the dilemma of “right or left hand” (see e.g. Leavitt, 1987). Some managers are encoded for managing by their inspiration and vision, named as path-finding managers by Leavitt (1987), while other prefer well-structured approaches supported by rich empirical data and quantitative analysis. The present author is convinced that new insights into successful and unsuccessful business strategies either locally or internationally may be obtained through the deep-level knowledge and understanding provided by this area of investigation.

In order to be able to understand the deeper levels of influencing factors in strategic management decisions we have to analyze the psychological, religious, philosophical and practical life element as well. This is a huge endeavor which requires scholars from many different fields, and experiences from different countries have to be collected. At the present moment we have good chances in Hungary to organize the necessary number and composition of researchers and financial support may be acquired through the National Long Term Research Grant under the auspices of the Hungarian Academy of Sciences.
REFERENCES


