

Estonia, the New EU Economy: Building a Baltic Miracle?

Edited by Helena Hannula, Slavo Radošević and Nick von Tunzelmann
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This book is intended for students of economics and management, general readers in Estonia and its Baltic neighbors, and those who seek to understand and evaluate Estonian economic development and social policy as well as internal and external changes in business. For Estonia, EU membership means international recognition and convergence of income level with the EU-15. Economic development is an important methodological cognitive instrument for understanding reality. At the same time economic development is a starting point for discussing alternatives for positive and normative economics; this instrument permits comparative analysis at a mega level. The edition brings an overall sense of coherence to the teeming world of macroeconomics and politics in Estonia. It is authored by an international team of twenty accomplished Estonian and British researchers: K. Bishop, R. Eamets, H. Hannula, J. Masso, T. Mickiewicz, K. Männik, K. Olenko, K. Philips, S. Radošević, E. Reiljan, T. Roolah, H. Roots, E. Tolmats, K. Ukrainski, M. Vadi, P. Vahter, U. Varblane, R. Vedina, T. Vissak and N. von Tunzelmann. The book is timely and original; the authors are experienced and able to interpret new developments. The readers of the book will benefit from its clear logic and language. It consists of five parts. The first part is an introduction, followed by three main parts, which discuss a variety of aspects and levels of economic development. The final part sums up Estonia's economic development and reviews future prospects. The aims of the book are to show: how the transformation and restructuring of 1990s brought rapid economic growth in Estonia; what factors encourage further economic growth; how Estonian economic experience is identified and made use of in the enlarged EU.

Chapter 1 of Part 1 is written by Nick von Tunzelmann, Helena Hannula and Slavo Radošević. This chapter characterizes the common context of central and east-

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ern European countries and the EU accession. The authors emphasize that the book covers a broad and rich context of potential growth and structural change in the eastern part of the enlarged EU. This chapter shows some cornerstones of the Estonian economy: rise of market economy, fixed exchange rate, the Currency Board Arrangement, liberal trade, favorable investment climate and broad-based taxation system.

Part 2 is titled Country Assessment – Growth and Financial Development. It embraces a wide macroeconomic view of the economic development of Estonia and other EU-27 countries. The theoretical framework of the link between convergence, different growth models and economic integration is discussed in Chapter 2 by Urmas Varblane and Priit Vahter. Theoretical characteristics are based on the empirical analysis of absolute and conditional convergence of the accessing countries in 1995-2005 and the EU as well as on econometric modeling of conditional and unconditional convergence among transition countries. The 5th enlargement of the EU is analyzed retrospectively and is compared with previous EU enlargements. Comparative statistical analysis shows ways for Estonia and other 5th enlargement countries to catch up with the EU-15 income levels.

Chapter 3, contributed by Katrin Olenko, illustrates the macroeconomic options in the rise of market economy in Estonia. The chapter analyzes the EU policy related to Estonian macroeconomic development in relation to the 5th enlargement countries gradually joining the EU monetary union. The differences in monetary policy of Estonia are insignificant in comparison with the differences in the rest of the euro zone, because monetary shocks in Estonia are similar to the EMU countries and the Balassa-Samuelson effect will not raise the inflation level higher than that set by the EMU.

Chapter 4, by Tomasz Mickiewicz, Kate Bishop and Urmas Varblane, explores the financial constraints of investment in Estonia in 1995-1999. Attention is paid to the dualistic structure of national industry – foreign capital companies, domestic capital companies and the size of the company. The microeconomic conclusion is drawn that industry in Estonia is dualistic and the dualistic nature of the economy can create conflicts and disparity between small domestic businesses and large foreign firms, related with foreign investors.

Part 3 is devoted to Structural and Organizational Changes at the macroeconomic level of the economy. Chapter 5, by Jaan Masso, Raul Eamets and Kaia Philips, concentrates on the labor market, its structure and changes in the three sectors of the economy from the early 1990s up to 2001. Creation and destruction of jobs are important simultaneous processes, related with reallocation of labor resources, firm size and business/company life period. International theoretical econometric modeling is employed in the analysis. The findings show that in the early transition period job destruction overwhelms job creation; however at later stages of Estonian economic development, destruction and creation of jobs are nearly in equilibrium. Jobs created

by SME are less permanent than the smaller number of jobs created by larger firms. This is due to high flexibility of job flows. The institutional environment and employment protection index in Estonia is comparable with the EU average.

Innovation in the Estonian forest and timber sector is compared with the Finnish forest and timber sector in Chapter 6, which is written by Kadri Ukrainski and Urmas Varblane. The authors emphasize the forms of collaboration in a business sector as well as the impact of knowledge upon technological capabilities and innovative performance of companies. Theoretical and empirical analysis shows that innovation sources are of uneven importance. Suppliers and customers in the timber sector are more important than universities or personnel. The timber sector is basically the only sector among the manufacturing industries that counterbalances the negative foreign trade balance created by other industries. In the period of 1994-2002, the forest and timber sector contribution to the total turnover of Estonian manufacturing industries was growing: on average, timber, paper, furniture industries were much more oriented towards foreign markets than other manufacturing industries. However, only joint collaborative efforts of Estonian government and Estonian companies can ensure further successful development of the sector.

Chapter 7, authored by Rebekka Vedina, Maja Vadi and Elina Tolmats, analyzes interactions of cultural elements in Estonian organizations. Under ever intensifying globalization, people such as Scandinavians, Germans, English or Arabs constitute the key element of economic development of any country. The authors theoretically characterize the main elements of culture and compare these elements with the values and attitudes of Russian-speaking employees in Estonian, Latvian and Lithuanian companies. The empirical study of Russian speakers in each Baltic country reveals similarities between these countries, stressing terminal values and paying less attention to instrumental values (responsibility, logics and honesty). The shift from industrial to service economics changes value priorities from material objects and physical security towards increasing self-expression and environmental protection, which, in turn, speeds up the process of transition.

Transformations of Estonian organizations, described by Maja Vadi and Harry Roots, are presented in Chapter 8. Changes that took place in the last decade of the 20th century are analyzed, applying Leavitt's model, which emphasizes four organizational elements (mentality, organizational goals, structure, and technology). The destruction of the relations of command economy and transitional conditions influenced the behavior of organizations and their members. The study revealed the fact that the role of entrepreneurs was extremely important in the beginning of independent economic development in Estonia, but later managerial competence became of crucial significance.

Part 4 presents an analysis of Internationalization and International Networks, described in Chapters 9 to 12. Chapter 9, written by Tiia Vissak, defines the role of

foreign ownership in the internationalization of Estonian enterprises. The theoretical part of the chapter is based on Uppsala's innovation-related Finnish models. The empirical part presents seven studies of internationalization. The chapter demonstrates that foreign owners can both quicken and slow down economic development as well as internationalization of their subsidiaries. Such firms can benefit from foreign direct income (FDI), ideas, know-how, technology, raw materials and foreign market expansion. Under the conditions of internationalization, firms can lose out through negligence of owners, criminal actions and the restriction of the autonomy of subsidiaries. The analysis proves that FDI impact on the host country depends on its size, development level, firm's size, the sphere of activity, experience level and other factors.

The main reasons for de-internationalization of Estonian manufacturing companies are discussed by Ele Reiljan in Chapter 10. This analysis enriches studies in the sphere, which raises practical issues. The complex approach to internationalization and de-internationalization processes is important for the future development of Estonia and other countries. Estonia's practical experience in the sphere of enterprise internationalization is abundant because FDI and foreign trade started to develop in the 1960s and at present de-internationalization in some spheres of particular markets has become a natural process. On the background of practical experience of the country the reasons, motives and forms (full/partial) of de-internationalization of manufacturing companies of Estonia are classified. For further research into this problem, the transaction cost approach and cluster network are suggested.

Chapter 11 demonstrates the autonomy and performance of foreign subsidiaries in five Central and Eastern European countries, described by Katrin Männik, Helena Hannula and Urmas Varblane. The authors examine the spheres of autonomy on the macroeconomic level, applying the data of five new EU-10 states members: Estonia, Poland, Hungary, Slovakia and Slovenia. The analysis shows that the higher the financing, marketing and autonomy of foreign subsidiaries, the bigger the positive changes in all the areas of activity (productivity, technology, personnel qualification and product quality, export trends etc.). The opposite conclusion characterizes technological autonomy because strong corporate links are very important for subsidiaries, located in technologically underdeveloped countries. The analysis confirms that the productivity of non-high-tech industries is higher than that of high-tech industries. Further research would be useful into the influence of the development of the host country economy on changes of foreign subsidiary autonomy.

The impact of emerging international networks on the strategic autonomy of foreign owned Estonian companies is investigated in Chapter 12 by Tõnu Roolah. The analysis focuses on the microeconomic data of Estonian manufacturing and services companies, describing their forms, changes in time perspective and other questions. The research concludes that case studies of the strategic autonomy of foreign owners

in Estonian companies, are not sufficient. Still, the findings indicate that the autonomy leads to increased activity.

Part 5 surveys the experience of economic development in Estonia, starting from the transition to a market economy and attempts to develop international competitiveness of the country. Chapter 13 by Slavo Radošević and Nick von Tunzelmann discusses the main core competences, necessary for further development of Estonia, indicating the importance of the information technology (IT) revolution, which could enlarge economic development in all activities and sectors of the economy; the need to catch up with the economic development of EU-15 programmes; and the necessity for deeper access of Estonian institutions into the EU, seeking the sustained development of the EU-27.

The book presents a wide and balanced view of current successes and failures in the economic development of Estonia: chapters in the book are almost equal in their number of pages, the methods of economic analysis are exhaustive, and the language of the narrative is clear and informative. 'Estonia, the New EU Economy: Building a Baltic Miracle?' is recommended to students of economics and management as well as to those interested in the economic development of the new EU members.