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EBS REVIEW

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SPECIAL ISSUE ON RESEARCH IN THE ESTONIAN BUSINESS CONTEXT

Organizational Values and Organizational Practice

Corporate Moral Development and Stakeholder Issues

Conflict Management Modes and Leadership Styles

Innovation Obstacles and Management Focus

Estonian Business School

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ESTONIAN BUSINESS
SCHOOL

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Contents

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Editorial for a Special Issue Dedicated to Research in the Estonian Business Context

Dear Readers,

In 2008, we celebrated two important anniversaries. The Republic of Estonia had its 90th anniversary, and at the end of the year, the Estonian Business School celebrated its 20th birthday. This made us think of compiling an issue focused on recent research on management and business that deals with Estonian organizations and the Estonian business context. Therefore, we dedicated our current issue of EBS Review to contributions directly related to Estonia. The design and lay-out of the issue you are now holding is a bit different from the ones you have seen previously, this issue marks the 20th anniversary of our university and is designed accordingly.

All the papers in this issue were carefully selected to offer you valuable information about research conducted in business administration and management in the Estonian context in recent years. We are happy to note that besides faculty members from the University of Tartu and Estonian Business School, among the authors in this special issue we can find researchers from other countries. This gives us reason to believe that developments in the Estonian business community and research in this field have also created interest among our colleagues from other countries.

Below you will find a brief introduction to the papers in this issue.

In the introductory text you will find a short address from the founder and first rector of our university, Prof. **Madis Habakuk**, who discusses the impact Estonian Business School has had on the Estonian community and provides a brief overview of developments in the last 20 years.

In the first of our research papers, researchers from University of Tartu, **Krista Jaakson, Anne Reino** and **Maaja Vadi**, discuss the factors that cause organizational practice to differ from its values. The authors use a model where specific organizational, situational and causative factors represent potential stumbling blocks to the manifestation of values in organizational practice. In an empirical study, they have used critical incidents technique with incidents reported by members of many different Estonian organizations. The results of the study show that managers may not have delegated sufficient authority to their employees so that these employees could actually put the values of the organisation into practice. In addition, they identified that employees face situations where organizational systems ignore company values, or the value-set itself is inconsistent. Finally, the authors suggest that organizations make a clear distinction between values and their existing strategy; when changing the latter, the values should remain the same, while some efforts are perhaps needed to reinterpret them. The value of their paper lies in the empirical investigation of real-life situations at work and applying a theoretical framework to locate patterns, and their results have clear implications for organizations engaged in values-based management initiatives.

The second paper discusses the link between corporate moral development (CMD) and stakeholder relations during the rapid and radical changes occurring in the past two decades in the Estonian business community. **Mari Kooskora** from Estonian Business School and **Johanna Kujala** from University of Tampere introduce the concept of CMD and divide the development that occurred in the Estonian business context into five stages based on this model to analyze stakeholder relations during each of the described stages. As a result of the analysis, a framework is presented illustrating stakeholder relations and the changes in them in the five stages of corporate moral development in the Estonian business community over the past two decades. The empirical data for this research was collected using observations and interviews, and to some extent written and web-administered questionnaires. The total number of respondents exceeds 5 000. The analysis shows that changes in stakeholder relations can be directly related to changes in the business environment. At different developmental stages, different kinds of stakeholders were considered important for businesses. Stakeholder relations developed from give-and-take type relations in the earlier stages towards more reactive or even proactive modes of interaction in the later stages of corporate moral development. However, in the end, the authors conclude that understanding relations with stakeholders as truly collaborative or mutually beneficial is still rare in the Estonian business community.

The purpose of the paper by **Ülle Übius** and **Ruth Alas** from Estonian Business School is to investigate connections between organizational culture and individual and organizational level factors. The survey was conducted in Chinese, Estonian, Japanese, Slovakian, Russian and Czech electrical-electronic machine, retail, information-software production and machine-building enterprises. A linear regression analysis was conducted in order to analyze connections between types of organizational culture – clan, market, hierarchy, adhocracy; individual level factors – job satisfaction, attitude towards the firm, meaning of work; and organizational level factors – powerfulness of the firm in competition with rivals, the behaviour of the management and company policy. The total number of respondents was 5 742. The results of empirical study show that the types of organizational culture – clan, market, hierarchy and adhocracy – predict job satisfaction, attitude towards the firm, meaning of work, powerfulness of the firm in competition with rivals, the behaviour of the management and company policy, but this varies from country to country. The 11 models developed explain how four types of organizational culture predict individual and organizational level factors in Chinese, Estonian, Japanese, Slovakian, Russian and Czech enterprises.

Next, **Sigrit Altmäe** and **Kulno Türk** from the University of Tartu study the modes of conflict management and the leadership styles among managers and specialists in Estonian organizations, depending on their socio-demographic characteristics. The authors conducted a survey of 345 Estonian leaders and specialists from different organizations using Thomas-Kilmann's Conflict Mode Instrument and Fiedler's Leadership Style measure. It was discovered that in most cases individual characteristics have an impact on the instruments analyzed, for example, younger managers are more task-oriented, while older managers are typically relationship-oriented and avoid conflicts, women are more collaborative and avoid conflicts less and men tend to use the accommodating mode more than women. Rather surprisingly, according to the survey, women appear to be more competitive than men. The relationships between the mode of conflict management and leadership style were also assessed and this revealed that task-oriented managers and specialists tend to use the competing mode more than relationship-oriented employees.

The paper by **Tiit Elenurm** and **Jaanika Oper** from Estonian Business School studies the focus of innovative activities. Obstacles in the innovation process and innovation performance management principles in Estonian enterprises are revealed by applying the Henley SME innovation study 2007 questionnaire. The Estonian survey involved 102 enterprises from 11 business sectors, where retailing, financial services and manufacturing industries dominated the sample. The main research question explores which high priority principles of innovation performance management and obstacles to innovation in Estonian enterprises differentiate the focus of the innovation when compared to more advanced European market economies? The conceptual basis of the paper links innovation to capabilities and development priorities in enterprises in an economic environment where the cost advantages of

Estonian enterprises are decreasing and future competitive advantages in Europe depend on following innovation-driven strategic priorities. Financial service enterprises had the strongest product and service innovation outlook, while retailers focused more on reducing costs. Production enterprises were more interested in innovations for foreign markets. Finding resources for innovation relies too much on internal expertise and makes limited use of networking opportunities. Estonian enterprises share many perceptions of innovation outcomes and innovation management with "old Europe", but the survey results indicate that a risk-adverse culture is not seen as a serious innovation obstacle, while a lack of coordination and a shortage of great ideas appear to be more serious challenges.

Brent McKenzie from University of Guelph, Canada, has examined the concept of retail brand extension through the use of an empirical study that looks at one of Estonia's more successful retail brand extensions, Tallinna Kaubamaja and Selver. The study develops a model to measure the drivers of retail success for both the main brand and the step-down extension within Estonia, and empirically tests the model based on Estonian consumer survey data. Consumer retail expectations are explained by testing the significance of shopping behaviour constructs on consumer attitudes to the retail brand and customer loyalty measures. The results suggest that retailers must both duplicate and alter existing retail practices to succeed when extending their retail brand. This study is the first known study to empirically test the link between brand attitudes, merchandise factors and customer loyalty in Estonia. Therefore, implications for both retail study and practice within and outside Estonia are also discussed.

In the final paper **Kate-Riin Kont** from Estonian Business School discusses the role of the National Library of Estonia (NLE) for the state and the nation of Estonia, and argues that the successful work of the library under economic pressure requires better planning in the use of all resources. Her study focuses on mapping the principles of financial planning and the needs of contemporary libraries and information institutions, and analysing the financial activities, financing principles and likewise analysing statistical economic indicators from the most important articles about income-expenses from 1996 to 2006 for the National Library of Estonia. It is argued that although libraries are not enterprises that earn a profit there is still a need to find additional resources for activities and development by raising funds and participating in international projects. The author concludes that the library needs to work out and apply a system of organizational indicators for its further activities to provide a more concrete strategic direction for the activities of the institution and enable a better evaluation of what has been achieved. The importance of the finance manager at the library cannot be underestimated. The task of the finance manager is to foresee future trends, but also to analyze retrospectively and to concentrate on strategic questions and value creation and on the wider picture of organizational development.

Dear readers, we hope that this brief introduction to the topics of the current volume of EBS Review has sparked your interest in the topics and articles gathered in this issue. As usual, all the articles go through a time consuming process of review and evaluation, and the authors often have to rewrite and submit their papers several times before our distinguished editors are satisfied with the results. We consider the topics covered to be important and hope, dear readers, that you can find something interesting to discover. We would also like to show our gratitude to the authors, editors and partners, indeed to everybody who has helped us prepare this issue for our readers.

On behalf of the editorial board

Mari Kooskora

Address by the founder and inaugural rector of EBS

Madis Habakuk

What impact has Estonian Business School had on the Estonian community – this seems to be the main question that I as the founder have to answer on the 20th anniversary of EBS. Furthermore, it is also likely to remain the main question in the future.

EBS was founded in 1988 – the socialist era – and imported the necessary business education for a free market economy, since knowledge in several fields of great significance for this new system was practically non-existent in economics education at that time. Marketing, investment, entrepreneurship, sales, finance and international management make up only part of the list. Managers also had almost no knowledge of the English language. EBS followed the example of academic programmes and textbooks from major US and Canadian universities, and lecturers from those countries were invited to teach here. In addition, the Estonian community in Canada and our US partners contributed remarkably to the organisation of three-month internships. Although EBS only had about 50 graduates in its first years, their contribution to the development of the Estonian economy was noticeable. Graduates from the early years founded successful banks and businesses, or attained ministerial or even Prime Ministerial posts or other key positions. In this way EBS made its own small contribution to economic development in Estonia as one of the fastest economic start-ups and in the Baltic context.

The foundation of EBS and its development has contributed to the innovation of economic and business education in Estonia. We are pleased to note that educational establishments with much older traditions than EBS have found the study programmes, faculty, marketing and administration methods, public relations and internationalisation (founders, students, faculty, Organizational culture) at EBS innovative and worthwhile following. EBS has 20 years of experience educating in English and 10 years in exporting education, the importance of which cannot be valued too highly considering the decreasing student numbers.

EBS has been the flagship of Estonian private education for years, and has proved that it is possible to deliver a quality business education and develop research in the field without financial support from the state. The 15-year-old journal, EBS Review, is now also quoted on the international catalogue of databases. Considering the scarcity of resources, EBS' experience in the field should also be of interest to the Estonian government.

In 2008, EBS was selected among the 300 Best Business Schools in the world. This has not been achieved by any other educational institution functioning in a similar field in Estonia. I would like to express my gratitude to those working for EBS at present as well as to those who have contributed to the development of our institution in its earlier years.

EBS REVIEW
No 25 2008/09

Organizational Values and Organizational Practice: What Makes Them Diverge?

Krista Jaakson*, Anne Reino, Maaja Vadi
University of Tartu

Abstract

The objective of this paper is to discuss the factors that cause organizational practice to differ from its values. We use a model, where specific organizational, situational and causative factors represent potential stumbling blocks to the manifestation of values in organizational practice. We have used critical incidents technique and the incidents have been reported by members of many different Estonian organizations.

The results of the study show that managers may not have delegated sufficient authority to their employees so that these employees could actually put the values of the organisation into practice. In addition, we identified that employees face situations where organizational systems ignore the values, or the value-set itself is inconsistent. Finally, we suggest that organizations make a clear distinction between values and their existing strategy; when changing the latter, the values should remain the same, while some efforts are perhaps needed to reinterpret them.

The value of the paper lies in the empirical investigation of real-life situations at work and applying a theoretical framework to locate patterns. The results have clear implications for organizations engaged in values-based management initiatives.

Keywords: critical incidents, management by values, organizational practice, organizational values, values-based management, values-based organization

Introduction

Shared organizational values have long been recognized as the basis for a strong organizational culture (Schein, 1992; Deal and Kennedy, 1982) and key to successful management (Peters and Watermann, 1982; Collins and Porras, 1994). In practice, this notion has only recently become acute for Estonian organizations, although cultural issues have been in the academic background for quite some time. There are many organizations in Estonia that started from zero at the beginning of 1990s, and they have now reached a phase in their life cycle when efficiency-pursuits and capitalizing on intra-organizational resources is the main focus (Vadi and Vedina, 2007). Values commitments represent a resource of this kind that comple-

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ments and enforces formal rules and norms in the organization. Beljajeva (2007), for example, has found that as much as 94% of the 45 large Estonian organizations (with more than 500 employees) she studied have formulated organizational values and use them as a management tool. Thus, management by values seems to be familiar and attractive to many managers; some of them already have years of experience with it. In this situation it is appropriate to study the idiosyncrasy of local practice and draw some initial lessons.

Conceptually, values always influence organizational practices (Schein, 1992), and thus, there is an inherent concordance between them if the underlying values behind any given practice are analyzed. However, mismatch between the values and practice may arise when organizational values are transferred from the unconscious (underlying assumptions) to the conscious level (espoused values). From a practical point of view this process is known as formulating the organizational values. Having done that, the reverse direction of analysis is applicable – finding the practice that corresponds to a given value, and to paraphrase a famous saying, "the match is in the eye of a beholder" in this case. With the organizational values clearly defined, multiple preferences for proper practices are obtained. Diverging from organizational values at some point in time is then almost inevitable.

Popular managerial concepts such as values-based management (Andersen, 1997; Buchko, 2007) and managing by values (Blanchard and O'Connor, 1996; Dolan and Richley, 2006), hereafter referred to as MBV, invite organizations to define their values, then communicate and implement them. In addition to formulation, the communication phase guarantees that organizational values are mindfully acknowledged by stakeholders, and divergence from them in practice is generally found highly problematic for the organization. This is also admitted by MBV proponents because the implementation-phase consists of aligning the values with organizational practices via constant analysis of the match and eliminating value-gaps. Deviations from the values in those concepts are treated as removable occasional mistakes. MBV authors do not seem to accept the fact that the probability of divergence increases dramatically as soon as people become aware of the values.

This has raised doubts about the immediate success of organizational values as a key managerial instrument. Buchko (2007: 37) claims: 'There's been very little empirical effort devoted to examining many of the tenets of the proponents of 'values-based' management. To date, there has been little attempt to empirically test the suggestions and principles set forth by those who argue for a values-based management perspective.'

Indeed, except for descriptions of individual success-stories, surprisingly little analytical attention has been paid to the downside of MBV, the stumbling blocks which turn good intentions into a deficient reality. There is almost no empirical research devoted to answer the question why organizational values may still fail to shape practice, although much has been written from the theoretical perspective. This paper attempts to contribute to this gap by empirically analyzing the possible causes for the divergence between values and practice. Using a critical incidents technique, the aim of the study is to determine and discuss the factors behind work-related incidents, where the outcomes are not inline with the values of the organization. We look at objective factors (e.g. size of the organization, the nature of the incident), known as organizational and situational factors, as well as causative factors (i.e. why a particular outcome materialized). Two research questions are posed:

RQ1: What organizational and situational factors (if any) are related to the value-breaching outcomes arising from values-related critical incidents?

RQ2: What are the causative factors behind the value-breaching outcomes arising from values-related critical incidents?

This paper looks at the general limits of putting organizational values into practice and the direct implications that can be drawn from

MBV. To achieve the objective set and answer the research questions, the present study will first provide an overview of the critical factors behind successful MBV based on previous studies. We will then present empirical data on values-related critical incidents and analyze organizational, situational and causative factors associated with the value-breaching practice. A discussion of the results and implications for MBV follows before the concluding remarks.

Literature Overview

The Role of Organizational and Situational Factors

There has been discussion in the literature about whether all types of organizations benefit equally from explicit organizational values (Brunsson, 2002; Blanchard and O'Connor, 1996). Brunsson (2002) speculates that having clear values and acting according to them regardless of circumstances is appropriate for 'action organizations'; that is, organizations providing physical products, rather than 'political organizations' – the public sector. Other authors (Dolan and Richley, 2006) maintain that shaping practice according to espoused values is the dominant strategy in the 21st century, no matter what type of organization is in question, and, indeed, many public organizations in Estonia have found it useful to formulate values – the Ministry of Economic Affairs and Communications, the National Audit Office of Estonia, the Bank of Estonia, the Tax and Customs Board – to name just a few.

In reference to the size of the organization, the literature seems to suggest that it is rather large corporations that adopt a formal values initiative (Anderson, 1997; Collins and Porras, 1994; Wenstøp and Myrmel, 2006). Therefore, it is inevitable that the failures are also associated with large organizations. To some extent, this is to be expected because the risk of not knowing, understanding or accepting the values increases with the number of employees. The current study will test values-related practice in public vs. private sector organizations as well as on the basis of their field of activity and the size of the organization.

Moving on to situational factors, the position of key participants in a critical situation has been found to be an important determinant of the interpretation of behaviour. There is a broad consensus about the critical role of top executives when it comes to organizational values (Schein, 1992; Badaracco, 2003; Lencioni, 2002; Griseri, 1998; Solomon, 1999; Edmondson and Cha, 2006; Buchko, 2007). It has been found that employees perceive the values-related decisions of a person differently based on the person's position in the organization (Cha, 2004), while managers' actions are more likely to be seen to follow the established values. On the other hand, managers may prove to be the very sources of cynicism among employees: *The Management Agenda 2007*, surveying 500 managers in the UK, reports that as much as 60% of respondents reckon that the espoused values and actual values in their organization do not match – the main reason being that managers 'do not walk the talk' (Garrow and Stirling, 2007, p. 3). Thus, we may expect that situational factor to play a significant role, but the direction is less clear.

It is natural to ask whether some values could be better candidates to put into practice than others. Here, Collins and Porras (1994) conclude that the content of particular values does not matter. Solomon (1999) and Palmer et al. (2004) support this view by concluding that the values of organizations are to a large extent similar, and it is rather the process of formulating the values that matters because it reveals the issues that all parties consider important. Therefore, based on previous studies, there is no reason to assume that there are some universal and more 'practical' values compared to others, at least when several industries are involved. In the current study, instead of focusing on particular organizational values, we analyzed work-related incidents that were perceived as critical in terms of values. The idea from Smith and Wang (1997) was used – their study suggested that even if the underlying values are the same in all events, some types of incidents are perceived as more difficult to manage and different approaches were preferred when handling them. Incidents were divided into: human resource related, procedural or strategy related, (production or service) quality related, and finally, cooperation related events.

The sector, size and field of activity of the organization as well as the position of the key participant and type of critical incident make up those factors associated with the characteristics of an organization and situations where values are managed.

The Role of Causative Factors

The framework of potential causative factors is synthesized from the claims of MBV proponents. Authors advocating MBV as a practice that paves the way to the financial and emotional success of the organization do admit the need for some preconditions or simultaneous actions for the promises of MBV to materialize. It therefore follows that the lack of those preconditions may prove fatal. We acknowledge that such an approach may not reveal the entire pool of factors affecting the success of MBV. However, as long as there is no theoretical model or practical case study to rely on, we are left with speculations and the best we can do is test whether some of these are relevant in Estonian organizations.

Based on the review of available literature, we identified six main causative factors that may inhibit the manifestation of organizational values in practice. The first three are the features that have to be present for MBV to be successful, and we therefore call them enablers: commitment to values, communication and resources. The remaining three are the features that the literature warns about, we name them disablers: inappropriate organizational systems, inconsistent values and idealistic values. An enabler is a potential disabler if it is missing (e.g. lack of resources) or is not sufficient (values not communicated enough).

The first disabler of MBV emerges unless values are taken seriously. The question of commitment has been discussed by many authors: a lack of commitment from the top-management has been analyzed on the one hand, and detachment among employees on the other. Managers often hand the values initiative over to the personnel department with little personal attachment to the values themselves (Driscoll and Hoffman, 2000; Lencioni, 2002). Scepticism and even cynicism among employees has also attracted attention. Employees may not care enough about organizational values: they want to be told what to do, receive their salary in return, and not give any more thought to their organization or work. This view of the nature of employees, however, is rare in contemporary organizational behaviour. More convincing arguments come from the literature discussing the personal–organizational value fit (Barrett, 1999; Bocchino *et al.,* 2003; Finegan, 2000) and the demoralizing impact of the management's behaviour (Padaki, 2002; Griseri, 1999; Palmer *et al.,* 2004; Edmondson and Cha, 2006). At any rate, the arguments propose that a lack of commitment is not a cause, but a result of prior values-ignoring actions.

The second disabler may arise when internal organizational systems send mixed messages about what is valued. Procedures for hiring, performance management, customer dealings, and so on, must ensure that the intended values are enforced systematically. Values, once they are stated, are constantly tested by the practicalities and aversive circumstances that every organization is open to. Rhetoric alone falls short in handling such incidents. In a study of how the CEO's personal values are delivered to the followers, Liu (2004) surprisingly found that if the CEO uses a policy-oriented approach – routine-based system-driven norms and regulations to express his/her values – significant commitment from followers is achieved, compared with inspirational speeches. Solomon (1999: 49) supports this by stating: 'What everyone says is not nearly as important as what everyone does'. This is to say that administrative actions and the use of tradition may be more effective elements than a leader's rhetoric and the use of cultural forms according to the classification of cultural leadership put forward by Trice and Beyer (1993: 263). Behaviour relies on existing systems and institutional incentive mechanisms. The important implication here is that employees trust those mechanisms at least as much as explicit organizational values and what managers say; divergence between them can cause serious frustration (Padaki, 2002). *The Management Agenda 2002* reported that as much as 37% of 400 employees surveyed in the UK suggested that the reward systems within their organization actually contradict internal value statements (Ball, 2002: 32), referring to performance-related pay. Thus, organizational systems that ignore values constitute a potential stumbling block for practicing values.

We call the third disabler 'inconsistent values'. Trice and Beyer (1993: 8) have noted that 'cultures are not monolithic sets of ideas, but rather incorporate contradictions, ambiguities, paradoxes and just plain confusion'. This is because organizations are persistently torn between conflicting interests and objectives (e.g. lowering production costs versus providing high-quality products). Ideally, the purpose of the values is to balance those conflicting forces and help decision-makers (Buchko, 2007). But far too often the values are not more than manifestations of opposing interests, and it is not rare that the values guiding an employee appear to be in conflict with each other – when trying to behave according to one value, another is inevitably violated. This paradox is defined by Stohl and Cheney (2001: 354) – it arises from a situation 'in which, in the pursuit of one goal, the pursuit of another competing goal enters the situation (often unintentionally) so as to undermine the first pursuit'. In the MBV literature it is assumed that organizational values are internally consistent, otherwise managing according to them becomes a rather arbitrary process. To overcome this problem, it is suggested that values should be prioritized (Blanchard and O'Connor, 1996), but then the idea of second-order values becomes obscure. Surprisingly, little attention has been paid to that problem in the MBV literature.

The fourth disabler deals with communication. Communication of values is at the core of MBV (Blanchard and O'Connor, 1996; Driscoll and Hoffman, 2000), being an inexorable stage between formulating the values and putting them into action. Although people receive signals about values from various channels (mission statements, management decisions, strategy, budget, etc), there is rarely too much direct communication about values. People have unique interpretations of how the same values should be translated to actions and priorities on the job (Anderson, 1997: 29) and for that very reason employee participation in the early process of values formulation is highly recommended by some authors (Brønn *et al.,* 2006). Participation minimizes the risk of having values that employees feel no attachment to. But even if employees have been involved from early on, all decisions and actions should be put in to the perspective of values for them as well as for the general public. The connection between an espoused organizational value and a decision may be clear and self-evident for a manager, but this may not be the case for other stakeholders when such a connection is not specifically pointed out.

The arguments about idealistic values as a disabler of MBV are twofold. First, there is a notion that values are and, in fact, should be stable over time (Kabanoff and Daly, 2002; Anderson, 1997), and the organization might find itself being too constrained by them, especially in a rapidly-changing environment. It has been shown that organizational culture and certain values are a major source of resistance to change (Chelte *et al.,* 1989; Kabanoff *et al.,* 1995). Values that help the organization in the present may prove inefficient or even fatal in a year's time, and this is why practice diverges from the agreed values. Collins and Porras (1994) briefly address this problem by concluding that 'the right values' do not outdate. But in this case the line between the 'right values' and the minimum standards of behaviour, which have little to do with the culture of the organization, becomes very thin. Secondly, there is no agreement about whether values should be enforced (and sanctioned) performance criteria or simply idealistic targets (Lencioni, 2002; Buchko, 2007). The former may take the form of a business code with formal prescriptions for behaviour, which may or may not reflect the intended values (Kaptein, Schwartz, 2008). The problem with the latter is that business realities simply do not live up to idealistic values (Palmer *et al.,* 2004; Badaracco, 2003) and deviations from them are inevitable. At this point some authors argue that the mere articulation of ideals increases the probability of acting in a manner that the pursuit of perfection leads to higher performance even though perfection cannot be attained (Collins and Porras, 1994; Anderson, 1997). Although there surely is some truth here, this also means that values are different from organizational practice. In our study, we call this phenomenon of deliberate neglect of organizational values as 'idealistic values'; that is, actual values that help manage a certain incident are different from previously agreed values.

Figure Captions

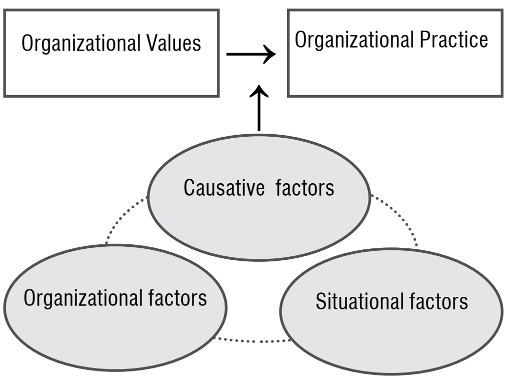

Figure 1: Potential Factors Affecting the Manifestation of Organizational Values in Organizational Practice

The final disabler is related to the resources required to secure the viability of organizational values in the long term. For example, certain resources are needed for communicating values, such as in-house courses or the appointment of internal and external officers to help employees put the values into action (Driscoll and Hoffman, 2000; Blazejewski *et al.,* 2006). In the current study, we consider resources broadly in terms of flexible procedures, the willingness on the part of the organization (and employees) to give up short-term profit as well as the explicit time, energy and money allocated in order to better implement the desired values.

Figure 1 summarizes both the organizational and situational as well as causative factors as potential stumbling blocks on the way to practicing values.

Method

Schein (1992) shows that even the espoused values of an organization are not always directly observable, let alone the basic underlying assumptions – the ultimate source of values. Therefore, values often remain hidden until they are challenged through critical incidents or events. Trice and Beyer (1993: 43) suggest that a good opportunity to detect cultural ideologies is in situations of contrast. In the present paper, the critical incidents technique is applied in order to develop ideas about why organizational values are not manifested in organizational practices. Therefore, a critical incident in this paper is defined as 'an observable human activity that contributes to or detracts from the general aim of the activity in a significant way' (Bitner *et al.,* 1990: 73) and not as an extreme behaviour originally put forward by Flanagan (1954: 338).

Organizational behaviour has previously been studied through critical incidents by Martin and Powers (1991), Meyer (1995) and Arnold (2006), for example. In all these studies, the respondents describing incidents in organizations are either observers or active participants. An important feature is that the respondents are not necessarily asked to report on their own behaviour, but rather on the practices and procedures that they perceive to exist in their organization and to analyze them in the light of organizational values. Critical incidents have a potential to reveal the possible gap between what is said about organizational values and what real actions convey to

Table 1: Organizations in the study sample

Field of activity	%	Field of activity	%	Size	%	Sector	No
Public administration	13	Production	13	Small companies (1-49 employees)	38	Private companies	71
Financial sector (banking, insurance, investment service)	12	Telecommunication and logistics	8	Medium-sized companies (50-249 employees)	21	Public companies	28
Education, medicine and infrastructure	13	Free time, culture and sports	11	Large companies (250-… employees)	39		
Trade	20	Construction and business service	9				
Not specified			1		2		1

members of the organization; that is, the (dis) integration of values and practices.

The incidents were reported by working students, who took a course in organizational behaviour between 2003 and 2005 at the University of Tartu, Estonia. After a lecture on organizational values and their management, the students were instructed to deliver a written assignment as follows:

a) *'Describe a specific incident that you have experienced in your organization that you believe was a good example of the manifestation of organizational values in practice'* *or*
b) *'Describe a specific incident that you have experienced in your organization that you believe was a practice that breached organizational values'.*

A total of 231 critical incidents at the workplace were gathered, out of which 198 could be used for the purpose of this study[1]. The loss of data was mainly due to three reasons. Firstly, some respondents described a series of events rather than a specific incident. Secondly, sometimes the general state of affairs instead of human behaviour was described, and thirdly, in many instances the incident had no connection with the reported organizational values. Therefore, it was impossible to determine whether a values-aligned or values-breaching incident was delivered and such incidents were neglected. Other than that, any incident the respondent chose to report as somehow related to his/her organizational values was considered critical and included in the final data set.

In addition to the critical incident, the students[2] were asked to briefly describe their organization (size, field of activity, sector; see Table 1) and its values, either formally espoused or perceived. This aspect is relevant to note, because many organizations did not have formal values, yet the member of the organization felt the practice did not correspond to what, in his/her opinion, should have been done in this situation.

The data were analyzed using thematic content analysis. Two researchers independently read the reports and coded the responses in order to identify pre-defined categories. These categories were:

a) type of incident – quality, cooperation, HR, procedural/strategy related;
b) outcome of the incident – aligned with values, values-breaching or partial. The latter refers to incidents where the practice of some values violated others;

[1] The number of actual organizations is smaller, because some students reported more than one incident. Additionally, students were allowed to pick the same organizations, if they had worked there. The exact identity of the organization need not be disclosed.

[2] Demographic statistics on respondents is not presented because organizations rather than individuals make a difference in the context of the study.

c) position of the key participant handling the incident – manager, employee or both;
d) causative factors behind the outcomes of the incidents – commitment, communication, resources, inconsistent values, value-ignoring systems and idealistic values. The first three factors (i.e. enablers) could be associated with any outcome, while the last three only characterized partial or value-breaching outcomes.

The researchers then compared their classifications. The interjudge liability was over 90% in the case of categories b) and c). Classifications of the type of incident and causative factors varied more due to permitting multiple coding of one unit of analysis. Researchers discussed those items where there was disagreement until agreement was reached and the data was coded for analysis (Table 2).

Having achieved a coded database, a correlation analysis and test for significance was conducted in order to find factors that distinguish the value-breaching outcomes of critical incidents from the aligned ones. As the aim of the study is to find out about the reasons why values and practice diverge, the value-breaching (hereafter, negative) outcomes of critical incidents are focused on in particular, and positive cases are only treated as comparative evidence. In addition to the positive and negative outcomes of critical incidents, we discovered several dozens of incidents where the solution was partial rather than clearly positive or negative. This means that, given the set of organizational values, the solution was in line with some values, but violated others. In our further analysis, these cases are examined separately.

Results

First, organizational factors were tested against the negative and partial outcomes of critical incidents. Correlation coefficients between the binary variables (Φ) for company size and negative/partial incidents ranged from -0.1 to 0.09. Negative incidents were associated with larger companies and partial solutions with medium-sized companies, but the differences were insignificant in each case. With regard to the organization's field of activity, the correlation coefficients for negative incidents were highest for organizations operating in free time, sports and culture (Φ=0.16) and construction and business services (Φ=-0.13), but again the differences were not statistically significant. The sector-analysis revealed that negative incidents are positively correlated with public organizations (Φ=0.16) and this is the only organizational level variable that is also statistically significant (p=0.02) according to the *F*-test.

Table 2: Description of critical incidents

Type of incident*	No	Position of key participant*	No	Outcome	No	Causative factors behind the outcome*	No
Quality	50	Management	128	Small companies (1-49 employees)	113	Commitment	92
Cooperation	52	Employee	92	Medium-sized companies (50-249 employees)	45	Resources	91
Human resources	66			Large companies (250-… employees)	40	Communication	73
Procedures or strategy	78					Inconsistent values	23
* Multiple coding permitted						Value-ignoring systems	35
						Idealistic values	10

As for situational factors, the position of the key participant who solved the critical incident was the next area of analysis. It can be seen from Table 2 that respondents described relatively more incidents where the manager dealt with finding the solution. There seems to be a systematic relationship between the managerial level of involvement and the positive outcome of an incident, as the correlation coefficient was 0.20 (p=0.01).

There were four types of incidents that were not mutually exclusive. For instance, internal systems were often mixed with service quality, and co-operation problems sometimes intermingled with a person's inadequate behaviour (HR-type) or some other combination was evident. Table 2 reveals that the core of critical incidents was most frequently related to procedures or strategy in the organization. The correlation coefficients with negative results are presented in Table 3.

Table 3: Correlation coefficients between types of incidents and negative/partial outcome to critical incidents

Type of incident	Negative outcome	Partial outcome
Quality	-0.22**	0.13*
Human resources	0.18**	-0.04
Cooperation	0.05	-0.06
Procedures or strategy	-0.08	0.04

*p < .05. **p < .01

The results indicate that quality-related incidents are not likely to reach a negative conclusion (on the contrary: quality seems to be the best candidate for values-aligned outcomes), but incidents involving HR-issues are. Partial solutions tend to occur slightly more often in incidents where the main problem is production or service quality.

The next focus of analysis was to determine the factors that could explain the particular solution to a critical incident. Table 4 presents the correlation coefficients between different factors and negative and partial solutions to incidents.

Table 4: Correlation coefficients for causative factors behind negative/partial outcome to critical incidents

Causative factors behind the outcome of incidents		Negative outcome	Partial outcome
Enablers	Resources	-0.40**	-0.19**
	Communication	0.04	-0.07
	Commitment	-0.09	-0.22**
Disablers	Values-ignoring systems	0.48**	0.16**
	Inconsistent values	-0.01	0.52**
	Idealistic values	0.15**	0.11

**p < .01.

According to Table 4, all anticipated factors except communication have explanatory power for why values-related critical incidents are not solved according to organizational values. We treat those incidents where some values were followed and others simultaneously violated as partial solutions. We maintain that this outcome also points at the stumbling block because practice degraded the values that were sacrificed.

Discussion

The discussion of the results will be structured on the basis of the two research questions posed in the introduction.

RQ1: What organizational and situational factors (if any) are related to the value-breaching outcomes arising from values-related critical incidents?

Organizational factors were related to the organization's size, sector and field of activity; situational factors dealt directly with the critical incident – its type and the participants involved. Our results show that the size and field of activity of an organization does not determine the results of values-related incidents. We had sufficient numbers of large, medium-sized and small organizations, but negative incidents were reported equally from all three. Thus, larger organizations do not show a tendency to deviate from their values according to this study.

However, public sector organizations tend to present incidents with negative solutions, and this indeed supports the view that political organizations differ from business organizations. But since we also looked at the interrelationship between organizational and situational factors, this result should be analyzed in a more compound manner. An interesting observation can be made from Table 3. Negative solutions are less likely to occur if production or service quality problems are at the heart of the incident. Not surprisingly, quality-related incidents occur in the private sector rather than the public sector. The public sector, by contrast, is best characterized by HR incidents (2/3 of all HR-incidents come from public organizations), which in turn positively correlate with the negative solutions according to Table 3. This is one reason why unsuccessful MBV initiatives can be found in the public sector – these organizations may espouse values such as efficiency, patron-service and so on, but when an employee happens to violate them, the incident is not adequately addressed in order to firmly re-establish the values, as in the following incident[3]:

> *Strict observance of rules and discipline are explicit organizational values at the public military college. Once, two students at the college missed classes because of drinking. The rules are very strict in this respect: alcohol abuse and not showing up in class is not acceptable behaviour for a future officer and such students are made redundant immediately. Since it was not the first occasion these two had exhibited poor behaviour, their co-students assumed they would be forced to leave the college. To everyone's surprise the director of the college let the students continue, saying that he did not wish to ruin their career.*

Of course, there might be other factors outside the scope of this study that are characteristic of public sector failures in the use of MBV. A specific organizational culture, such as a rigid internal process-oriented culture might be one example here. Also, unattainable organizational values could be an explanation, because people formulating the values often do not feel personally committed to them. Yet, we maintain that it is not so much the public sector that is unsuitable for MBV, but rather HR-related issues that tend to challenge values. Why is this so? Joseph L. Badaracco Jr. has discussed the success of 'quiet leaders', referring to their specific way of solving dilemmas in business. Choosing between values and people is seeing the world in black and white, he claims. Compromises between the two, advocated by Badaracco, is not what MBV would suggest according to which values always come first. Sacrificing real people to abstract values is emotionally charged and it is exactly this type of incident that is more often faced in the public sector. Thus, the type of incident seems to play a role in the outcome, namely HR having negative and quality-related incident positive outcomes.

Another situational factor we analyzed involved the position of the person performing the decisive role in solving a critical incident. We found that in many of the reported incidents that reflected the maintenance of organizational values, the manager was the key person in charge of the outcome. This result supports the stream of evidence that organizational values more or less equal the manager's values in the eyes of employees. The managerial level of involvement strongly reduced the likelihood of a negative solution with regard to organizational values. This distinctly emerged in the following example case:

> *Credibility is the main value in this dry-cleaning company. A jacket brought for dry-cleaning lost colour and shape in the process, although the cleaner had followed the manufacturer's precautions. The manager of the dry-cleaning store contacted the customer and informed her about the unfortunate course of events. The manager explained the situation and helped the customer to contact the manufacturer and ask for redress due to insufficient warnings.*

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[3] The incidents presented here and below are summaries of the cases provided by respondents and they are approximate translations from Estonian.

There are alternative, while not mutually exclusive, explanations for this phenomenon. The formation of organizational values, although affected by the members of the organization, is first and foremost related to its leader's values and so it is natural for him/her to act according to values even in the most controversial situations. Alternatively, the result may imply that managers are more concerned about the organizational values. In other words, managers are more committed to MBV, because it is their own initiative, they have invested a lot of resources in the project or for some other reason. Moving away from managers' possible emotional attachment to values, it is also plausible that following organizational values is viewed as any other managerial task by the subjects. Dealing with problems and finding a values-based solution might be rooted in the stereotype of being a manager, if not officially stipulated in his/her job description.

But it is also possible that managers do not in fact differ in their behaviour with respect to organizational values. Cha (2004) has demonstrated that employees tend to regard the activities of the management as being aligned with organizational values, whereas the same action by a co-worker could be perceived as values-breaching. The more ambiguous the organizational values, the more varied their interpretation. Given the design of the current research, this effect could also be present in this study. However, in order to make any firm conclusions about why managers are better at MBV, a separate study should be conducted.

The results have at least two important implications for managers trying to engage in MBV. Firstly, managers could enhance the process of formulating organizational values according to their personal convictions and not necessarily aim for the alignment of these with the values of all employees. Whether or not employees are able to distinguish managerial and organizational values, managers are better off when organizational values reflect their genuine preferences for professional conduct. The second implication emerging from the results is that for the successful implementation of MBV, managers have to be constantly hands-on, personally solving various smallish and serious incidents at work. Only then can employees recognize that the organizational values are being actively and consistently implemented. Such micro-management becomes necessary unless managers delegate the responsibility for the implementation of values to employees. On the other hand, adding responsibilities require rights to be given, too, and as the next section will demonstrate, this seems to be a serious bottleneck in the organizations studied.

RQ2: What are the causative factors behind the value-breaching outcomes arising from values-related critical incidents?

We analyzed several attributes that the literature has paid attention to with regard to MBV: commitment, organizational systems, inconsistent values, communication, idealistic values and resources. The illustrative summary of all factors and their combination behind value-breaching outcomes is presented in Figure 2.

Based on the current study, there are three clear disablers of the manifestation of organizational values in practice. Firstly, it is worth noting that 'resources' is a factor that is unlikely to be associated with a negative solution to a critical incident – as expected, it is a strong enabler of MBV. This is one factor that significantly distinguishes values-aligning and values-breaching practice – very often when a critical incident finds a values-based solution it was due to the company's willingness to bear extra costs or outright losses in order to signal that it takes its values seriously. The incident below demonstrates this relationship:

> *The most important value of this logistics company operating at sea is customer satisfaction. A critical incident took place in winter 2003 – a year that was extraordinarily cold in Estonia and the sea froze. Deliveries to the company's customers were at risk. Logistics companies pay insurance fees to the Estonian government who run the ice-breaker supposed to keep the sea ice-free. But in 2003, the government could not fulfil*

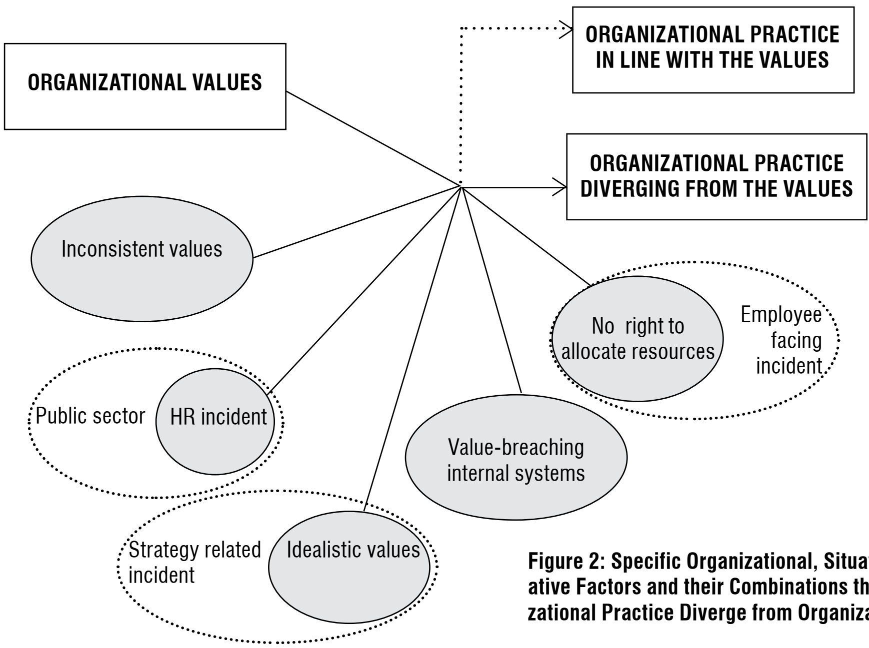

Figure 2: Specific Organizational, Situational and Causative Factors and their Combinations that Make Organizational Practice Diverge from Organizational Values

its obligations – the icebreaker was needed elsewhere. The company was on the verge of having to let its customers down. However, bearing remarkable financial risk, they rented an icebreaker from Norway to satisfy their customers.

Recalling the result above, that positive solutions and managerial involvement are related, it is evident that managers have monopolized the decisions over resources and this makes employees worse off in terms of delivering the values in practice. Consequently, if organizational values are to be followed at all levels of the organization instead of being the management's discretionary policy, then front-line employees should also have sufficient autonomy and power to deliver these values. The following incident clearly illustrates the typical position employees hold with regard to values and practice:

The cherished value of that restaurant is customer satisfaction, both in terms of food and service. One gentleman hosting a dinner for his guests had finished in the restaurant and wished to pay by credit card. The waiter tried to complete the transfer several times, but the system was down. Since the gentleman had no cash with him he offered the waiter to pay by transfer. Unfortunately, the waiter only had the right to issue an invoice with a letter of guarantee. So he refused. The gentleman had to go out in the rain to find the nearest ATM in order to pay; his guests were left waiting. The waiter understood by the manner in which he slammed the door that the customer was far from satisfied, but he was sure he did the 'right' thing.

Of course, changing this pattern requires organizational trust – managers should feel that the delegated power will not be abused, and employees should feel secure in being able to make (sometimes costly) decisions in the spirit of the organizational values because they know they will not be punished.

The second causative factor that explains why critical incidents are not handled according to the values is that organizations have adopted systems or procedures that do not support the values. A somewhat extreme case was reported from the financial sector:

A finance company has stated its official values: credibility and professionalism. A customer wishing to enter into a contract with the company found out to his and the *clerk's surprise that he already had signed a contract with that company. Of course, the contract was not real apart from the registration number. It then became clear that one clerk had systematically created dummy contracts. Why? Because the clerks received performance-related pay based on the number of new customers attracted.*

Why such divergence between values and internal systems exists may stem from a variety of sources. It could be that systems are relatively rigid or that it is difficult to design them according to values. Also, one might assume that values are mere publicity with no intention of them actually being implemented, and the organizations are deliberately avoiding enforcement of the values through internal systems. A problem of semantics might also come into the picture: espoused values are meant to convey one thing and they are perhaps even supported by the systems, but to many they also denote something else, which is out of the scope of the company[4].

This leads to a third disabler in handling critical incidents – the solutions are based on arguments other than values; that is, existing values turn out to be overly idealistic. This typically emerges when making strategic decisions in companies under economic strain; for instance, downsizing or closing some business units, where formerly established values are neglected in this process. This may be due to the fact that genuine values had not previously been formulated (i.e. values were no more than public relations instruments), because for some reason old values ceased to contribute to the organization's success and a dramatic change was indeed needed, or, as the case below demonstrates, the company has not made a clear distinction between the values and the pursued strategy.

Good working conditions and the wellbeing of the employees had always been part of this small wood-processing company's rhetoric. But due to bad weather conditions, the price of the raw material had increased considerably and one production line had to be closed until new technology was introduced. The company wanted to avoid paying layoff compensation and forced people to leave on their own initiative. Those that agreed to such an arrangement were promised re-employment as soon as the new technology was in place. This saving for the company meant that not only were employees left without compensation, but they lost their state unemployment benefits as well.

This result implies that the espoused organizational values are intermingled with the chosen strategy and are therefore practical for running the every-day business. In other words, organizational values have developed or have consciously been chosen in order to better implement certain strategies. However, these values are bound to be short-lived because of changes in the environment and the organizational need to adapt. Hence, organizations interested in MBV should critically assess their values: are these values important to us no matter what, or has our current strategy or tactics taken the shape of a values-statement? If the latter is the case, any change in the strategy may be viewed as a violation of values by the employees, and certainly no organization would want this to happen. It might be necessary, however, to discuss in the organization what exactly organizational values mean for the new strategy and how these help them to orientate in the new situation.

As a final comment about negative incidents, our data did not suggest that commitment is a significant enabler or disabler of MBV. Commitment problems, if present, are obviously generated by one of the factors above: insufficient authority to make decisions, value-ignoring systems or values that were too idealistic given the circumstances. This is not to say that commitment is not relevant when pursuing MBV; however, instead of talking about an abstract phenomenon such as commitment one should concentrate on the very factors that affect it. Nei-

[4] The example could be the value 'respect' meaning 'treat your colleague as you wish to be treated yourself' on the part of the company, but also interpreted as 'accept the reluctant customer and do not bother' on the part of the employees.

ther is communication a significant determinant of the outcomes of incidents. Again, we do not claim that the definition of MBV that stresses communication as an important feature should be revised; on the contrary, it seems that the relevance of communication is so established that even those who fail to align organizational practice with its values do this for reasons other than communication.

Turning to partial solutions, one can see from Table 4 that the factor with the highest load is inconsistency of values. This is, of course, a predictable result. There were 40 incidents where a partial solution was found, of which 18 were associated with conflicting values much like the following incident:

> *There are two distinctive values promoted in this vocational school: student-friendly environment and quality of education. Since many students come to the school from some distance away and stay in the school dormitory, the curriculum is arranged according to bus-schedules on Friday afternoons and Monday mornings. However, some students take the option of starting the weekend even sooner and come to school by noon on Monday. Teachers try to present less demanding material on those days, but they feel that the 'friendly' environment has started to seriously hamper the quality of teaching.*

Common examples of conflicting values include value sets consisting of 'customer-orientation' and 'good reputation' (these contradict one another when customers request unethical service), 'professionalism' (responding to customer's needs however long it takes) and 'being operational' (respond to requests as quickly as possible) and, most typically, 'performance-orientation' together with 'customer-orientation'. The potential for contradictions is embedded in any given pair of values. Meyer (1995: 220) found that 'autonomy' and 'authority' represented conflicting values in a Community Childcare Centre, and the workers structured their behaviour to achieve a compromise or a limited accomplishment of these competing values. Many respondents in our study have experienced the same situation, and we propose that any managerial concept, including MBV should not intentionally put employees into such a position.

Conclusions

The aim of this article was to learn about the stumbling blocks that cause the divergence of organizational practice and values. We collected data about nearly 200 critical incidents handled or mishandled according to organizational values. Our first finding was that values-related practice does not depend on company size or field of activity. The view put forward by some scholars that public sector organizations might not pursue organizational values as successfully as private companies was supported by our results. However, the reason for this need not be the sector per se, but the different types of incidents that organizations in different sectors typically face. Incidents related to production or service quality are more likely managed according to values (or at least partly so), but such incidents rarely occur in public sector organizations. Instead, public organizations present a high proportion of HR-incidents, which seem to challenge organizational values more than other types of incidents. In this light, it is understandable why accusations have emerged that proper MBV is harsh and inhumane, especially when intended to regulate human behaviour rather than motives (Griseri, 1998; Badaracco, 2003).

Secondly, we found that incidents handled by managers are perceived to be in accordance with organizational values, a result that also supports some earlier findings. We argue, however, that managers are probably better performers due to their power to allocate extra resources to support the values. Unless the same rights are given to employees, the saying that MBV makes a manager out of every member of an organization is empty in practice. Devoted adoption of MBV requires trust and a brave delegation of rights and responsibilities in order to deliver values at all levels of the organizational hierarchy.

The third disabler of practicing organizational values turned out to be value-ignoring internal systems in the organization. The concept of MBV states that all procedures, decisions and incentive mechanisms should reflect the values, but this study indicates that this is not always the case and values were often just used as an instrument for public relations.

However, the fourth disabler is that organizations are reluctant to espouse the values that they would truly follow regardless of the strategy pursued. When facing tough times, the organization's concerns about survival will prevail and decisions taken in such a context may have little to do with the values formulated previously (and possibly superficially) when the organization was doing well.

In the current study, partial solutions to critical incidents were also viewed as problematic in terms of the manifestation of values in practice. The causative factor behind partial outcomes was inconsistency of values. Here is a thought for the managers or consultants formulating the values. 'Stability' and 'innovation' obviously produces confusion, but our incidents also revealed more subtle cases. Profit and good performance, which typically are not explicitly espoused values, are assumed to be supported by 'soft' values such as teamwork, customer-orientation, etc. Yet, there are plenty of incidents in reality, where following soft values requires that (financial) performance should be sacrificed, at least in the short term.

Limitations

There are certain constraints that come from the research process itself as well as the phenomenon studied. Firstly, the classification of incidents as critical – subjectivity is largely involved in this process, even though an inter-judge method somewhat decreased this factor. In future studies, computer-aided classification and software-supported content analysis of incidents should be developed.

Secondly, not all organizations in the study had explicitly formulated values, and the values then analyzed represented the respondent's perception about what the organizational values were. In such cases, using one member of the organization as the only source to report on their organizational values might raise the question of whether these values are actually in place in the organization and how the other members would have responded. Thus, the second source of subjectivity – the observer's own values, interests and even his/her level of moral development – is an integral part of this type of study. In addition, all critical incidents and their solutions unavoidably bear the respondents' subjective interpretation. Although this question does point to one of the potential limitations of the study, the authors assume that people usually see in the present what they have seen before – an historical sense-making process is involved. In this study, out of 198 incidents less than half were value-breaching examples and one could question whether this is sufficient for reaching conclusions. Although increasing the number of negative incidents is another direction for developing the study, we were able to detect a clear pattern of relationships. Regarding the method in general, we acknowledge that the strengths and weaknesses of the critical incident technique apply to this study.

The results of the study open new perspectives about the relationships between organizational values and organizational practices, and the suggested patterns of behaviour call for further research. In-depth case studies of failed MBV initiatives from the management's point of view would supplement this type of study.

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Corporate Moral Development and Stakeholder Relations: An Empirical Analysis of the Estonian Business Community

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Abstract

The purpose of this paper is to discuss the linkage between corporate moral development (CMD) and stakeholder relations during the rapid and radical changes occurring in the past two decades in the Estonian business community. During the period from 1985 to 2005, Estonia moved out of the former Soviet Union's sphere of control and became one of the front running countries among the new member states of the European Union. In this paper, we first introduce the concept of CMD and divide the development that occurred in the Estonian business context into five stages based on this model. After that, we analyze stakeholder relations during each of the described stages. As a result of this analysis, we present a framework illustrating stakeholder relations and changes in them in the five stages of corporate moral development in the Estonian business community during the past two decades. The empirical data for this research was collected using observations and interviews, and to some extent written and web-administered questionnaires. The total number of respondents exceeds 5,000.

Our analysis shows that changes in stakeholder relations can be directly related to changes in the business environment. At different developmental stages, different kinds of stakeholders were considered important for businesses. Stakeholder relations developed from give-and-take type relations at the earlier stages towards more reactive or even proactive modes of interaction at the later stages of corporate moral development. However, understanding relations with stakeholders as truly collaborative or mutually beneficial is still rare in the Estonian business community.

Keywords: Corporate moral development, stakeholder relations, Estonian business community, change.

Introduction

Business, whether we like it or not, has become the most powerful collective entity on the planet. Today, few doubt the need for profits to keep companies viable, but when profit is seen as a product rather than a by-product of good business choices, long-term (unwanted) consequences result for companies and society.

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Therefore, it is becoming increasingly apparent that the full integration of ethical standards into business practice is not only preferable, but also necessary for long-term organizational survival (Freeman, 2000).

In 1971, Ahlstedt-Jahnukainen stated that the firm is not a closed system lacking any relationship to the outside world, but it is open and connected to several external systems in a number of ways as well as through its stakeholders (Näsi, 1995: 104). Moreover, a growing body of evidence indicates that corporate relations with various stakeholders, corporate citizenship, responsibility, and accountability are becoming as vital to the bottom line as an effective business model (Freeman, 1995: 35; Paine, 2002). Increasingly more attention and effort are being directed towards concerns for ethical and responsible business practices, and the view that all business organizations have multiple stakeholders whose needs and interests have to be considered to achieve sustainable success is finding growing support. A major reason for increasingly adopting the stakeholder concept when setting business objectives, is the recognition that businesses are affected by the environment and society in which they operate. The competitiveness and ultimate success of a corporation is seen as a result of teamwork that embodies contributions from a range of resource providers including investors, employees, creditors and suppliers. Some authors (Logsdon and Yuthas, 1997; Snell, 2000) have also drawn direct linkages to organizational moral development and stakeholder orientation.

The purpose of this paper is to discuss the linkage between corporate moral development (CMD) and stakeholder relations during the rapid and radical changes that occurred in the Estonian business community from 1985 to 2005. The paper starts by introducing the concept of CMD in more detail and discussing stakeholder relations at different stages of CMD. Based on the CMD model, the development of the Estonian business community is divided into five periods representing different stages of CMD. After that, we take a deeper look at the stakeholder relations during each of the described stages by analysing (1) who the important stakeholders in each stage are, (2) what the relations to these stakeholders are like in the different stages, and (3) what the outcomes or consequences of these relations in terms of corporate responsibility are like at each stage. As a result, we present a framework illustrating stakeholder relations and changes in them in the five stages of corporate moral development in the Estonian business community during the past two decades. The paper is concluded with a profound discussion on the presented framework.

Corporate Moral Development

Inspired by the work on individual moral development by Kohlberg (1969), Reidenbach and Robin (1991) presented the idea that corporate moral development changes from strictly self-interest and self-serving to a broader consideration for others and society. They developed a model of Corporate Moral Development (CMD) to illustrate the balancing of business and ethics in organizations suggesting that as individuals can be classified within a stage of moral development so too can organizations. The authors identified five stages of moral development describing the behaviour of the corporation as: amoral, legalistic, responsive, emerging ethical and developed ethical. These stages exhibit the morality/moral maturity of an organization through certain behaviours, attitudes, values, corporate culture and explicit or implicit artefacts.

The CMD model suggests that corporations that give profit higher preference than ethics can be found in the first stages, and corporations that give ethics priority over profitability are found in the higher stages of moral development. Similar ideas about organizational moral development were addressed by other authors, who maintained that organizations can be categorized into stages based upon their behaviours (e.g. Sridhar and Cambrun, 1993; Carlson and

Kacmar, 1997; Logsdon and Yuthas, 1997 and Snell, 2000).

In the corporate moral development model, stage one organizations are basically characterized as ‘amoral’. In such corporations, the owners and managers are seen as the only important stakeholders and the corporate culture encourages maximizing profits at all costs. Being caught disobeying ethical laws is viewed as a form of normal business and punishment is consequently endured as part of doing business. It is argued that this type of organization is not too commonly found (Lindfelt, 2002: 33). Stage two organizations are defined as ‘legalistic’, these are seen as having reached a higher level of maturity and corporations on this level obey the law, but no more than that. We can argue, that similarities can be found here with the two first levels of economic and legal responsibilities in Carroll’s model of corporate social responsibility (e.g. Carroll, 1991: 40).

Stage three organizations have begun to develop ethical concerns and are characterized as ‘responsive’. These organizations have developed some external relationships with the community, may behave ethically and take some social responsibility, but only for self-serving reasons. Stage four organizations have already started to implement the artefacts of an ethical organization, such as codes of conduct and ethics committees. Such corporations are labelled as ‘emerging ethical’ and they recognize that being ethical sometimes involves a trade-off with profits. Typically, such corporations also show a concern for values in their mission statement or its planning documents. The documenting of ethically responsive actions is a part of a stage four organization’s practice. Finally, stage five organizations have clearly articulated value statements and implement these in practice and are characterized as ‘developed ethical’ organizations. Such corporations have worked out moral principles that can be relied upon to help the organization deal with ethical issues. According to Reidenbach and Robin (1991) this kind of corporation is quite rare.

Corporate Moral Development and Stakeholder Relations

We can argue that a major reason for increasingly adopting the stakeholder concept when setting business objectives, is the recognition that businesses are affected by the ‘environment’ and society in which they operate. The idea is that ‘holders’ who have ‘stakes’ interact with the firm and thus make its operation possible (Näsi, 1995: 19).

Today, to a greater or lesser degree and in different ways, all businesses come into regular contact with customers, suppliers, government agencies, families of employees and special interest groups. According to Carroll (1991), the stakeholder approach puts ‘names and faces’ on the members of society who are the most critical for the business, and to whom the company must respond. The range of stakeholders differs from company to company; however, generally the stakeholder groups recognized by most firms include owners (shareholders), employees, customers, partners, local communities and the society at large.

Although the stakeholder approach is not explicitly discussed in the original CMD model, some authors have created more direct linkages with concepts of corporate social performance and stakeholder orientation (Logsdon and Yuthas, 1997: 1216), and Snell (2000) integrated a corporate outlook for stakeholders into the discussion of organizational moral development.

Thus, referring to the CMD model, we can say that at the pre-conventional level (amoral and legalistic stages), decisions are made and stakeholder relationships exist only in the interests of the top managers or owners. While these decisions may also serve the interests of other parties, there is no requirement that they do so. It is also argued that executives can be opportunistic and self-aggrandizing to the detriment of legitimate claims made by other stakeholders (e.g. Donaldson and Preston, 1995; Jones, 1995).

According to Logsdon and Yuthas (1997: 1217), the commitment to some form of moral reasoning begins with conventional moral development (responsive and emerging ethical stages). The sources of moral standards in conventional reasoning are external forces that are accepted as legitimate and desirable within the organization's environment. They argue that at Stage 3 (responsive stage of CMD), the top management is concerned with fitting in with their peers and this involves some level of responsibility toward others, and concern for stakeholders begins as they begin to realise the importance of employees and the community in which they operate. The management projects a pleasant self-image by maintaining good relations with key stakeholders and considers media and public opinion important. The market-based stakeholder orientation is supplemented by legal requirements that relate to specific stakeholders, as organizations try to understand the needs, expectations and moral claims of stakeholders, and executives accept society's legal standards as legitimate for preserving social order (Reidenbach and Robin, 1991).

Thus, conventional moral reasoning focuses on a narrow range of stakeholders that are specified in economics and law; that is, owners, lenders, customers, employees, and others who have a market-based or contract-based relationship with the firm (Logsdon and Yuthas, 1997). The nature of the rights and duties between the organization and these stakeholders is specified in contracts, either explicit or implied, and subject to legal adjudication. However, by equating legal with ethical behaviour, they run the risk of lagging behind changing stakeholder expectations, and also forego the benefits of meeting stakeholder expectations that are not required by law (Jones, 1995).

Post-conventional moral reasoning (ethical organizations) is what is usually associated with mature ethical analysis. Post-conventional analysis goes beyond peer and legal expectations to emphasize the active promotion of the welfare of stakeholders based on respect for others. This level of moral reasoning necessarily involves a broad range of stakeholders, both market-based and non-market-based (such as local communities, environmental groups and the poor and disadvantaged members of society). Organizations at this level do not view themselves as separate from this broad range of stakeholders, but recognize their interconnectedness in pursuing the welfare of society.

At the developed ethical stage, social contract orientation recognizes that peer and legal standards (as emphasized at responsive and emerging ethical stages) are not sufficient to be fully moral. Instead, the top management participates in dialogue about social values and responsibilities that go beyond peer and legal requirements (see Donaldson, 1992; 1994; Dunfee, 1991; Logsdon and Yuthas, 1997). Organizations that operate at the post-conventional level have accepted a broader set of stakeholder relationships and thus, are likely to be perceived as being more concerned about their legitimacy than organizations at the conventional stage of moral development, at this level the top management encourages analysis of issues according to universal ethical principles, such as individual rights and duties, justice and utilitarianism (Cavanagh *et al.,* 1981; Velasquez, 1982; 2002).

Corporate Moral Development in the Estonian Business Community

The analysis of corporate moral development in the context of the Estonian business community was based on the above presented CMD model. The empirical data was collected using observations and interviews and to some extent written and web-administrated questionnaires with more than 5,000 respondents. These included 183 in-depth and focused interviews, 88 web-administrated questionnaires, 900 structured questionnaires and 3,900 written descriptions of conflict situations in Estonian business organizations and society (see Kooskora, 2008: 53). The 20-year period was divided into five different periods, which related to the stages in the CMD model. The analysis of the study showed that corporate morality in the majority of Estonian business organizations developed from a double morality in the period of socialist erosion through an ethical vacuum, instrumental and legalistic stages to a responsive stage emerging during EU accession in 2004 and 2005. Table 1 depicts the synthesis of this analysis.

The first period 1985–1990 is referred to as the period of socialist erosion. At that time, businesses officially operated under a closed state controlled system and the Soviet ideology with its norms and values. However, unofficially, managers and politicians in higher positions utilized opportunities for their own benefit. There was a low level of trust among business actors, and a high level of corruption in society.

The next period, known by the name rough entrepreneurial capitalism, lasted from 1991 to 1995. It started when Estonia regained its independence from the Soviet Union and began to build up new political, economic and social systems. At that time, the entire society and particularly its economy were struggling for survival. Practically no regulations or rules existed in business, as the legal system was only starting to develop, and the young government imposed very few restrictions on business activities. There were no ethical or legal considerations in business organizations. For example, this time is characterized by many contracts being violated – if they existed at all – and the abuse of power on the basis of position was commonplace. Furthermore, people behaved in a way that seemed 'right for them', and wild, sometimes even criminal activities, took place. This period can be seen as a reaction to the changed environment where the former Soviet values and norms no longer existed, and nothing new emerged to replace the void, meaning that the level of risk as well as opportunity in business was high.

By 1995, the private sector had achieved a dominant role in the economy partly due to privatisation activities and partly thanks to the emergence of a number of new private firms. The period of 1995–1999 is referred to as the business boom. The ultimate goal was to earn maximum profit, and this included restruc-

Table 1: Synthesis of corporate moral development in the Estonian business community from 1985 to 2005

Stages of CMD in Estonian contex	**Double Morality**	**Ethical Vacuum**	**Instrumental**	**Legalistic**	**Responsive**
Period in the context of the Estonian business community	**Socialist erosion (1985–1990)**	**Rough entrepreneurial capitalism (1991–1994)**	**Business boom (1995–1999)**	**Catching-up (2000–2003)**	**EU convergence (2004–2005)**
General description	Officially a closed state-controlled system, soviet ideology with its norms and values; unofficially managers and politicians in higher positions utilizing opportunities for self-benefit, low level of trust, high level of corruption.	Nobody thought and cared about business ethics; short-term survival of the business at any price was the main aim. Reaction to the changed environment, practically no regulations, in places wild, even criminal activities.	Profit was the ultimate goal, there was no place for business ethics; maximum profits at all costs. Breaking the law was not considered serious, tendency to avoid and neglect laws and regulations.	Business ethics over the law has no place in business; however, following the letter of law is mainly respected, thus, legal equals ethical.	Ethical statements and concerns are emerging in businesses as a tool to create a positive image; business ethics pays when profitable.

turing former state owned organizations with the aim of increasing personal gain for business managers and higher officials, improving ones lifestyle and gaining prestige. Some rules and regulations governing business activities had been established, but these were usually avoided and neglected. For example, not paying taxes, the use of envelope salaries, the absence of written contracts with employees, no consideration for working conditions or employee safety, and the use of tax-free companies were widely practiced. The main priority was to earn profit without considering how it was done or what impact it had on others. Relationships were instrumental, using others as tools for organizational and personal gain.

The period of catching-up during 2000-2003 was characterised by a clear orientation towards joining the EU and NATO and a context where legal systems were already in place. During this period, compliance with laws and regulations became more important than during the previous period. As laws and regulations became more important in business activities and organizations, it was no longer appropriate to neglect and avoid the laws and regulations concerning for example, paying taxes, having written contracts and abiding by them, and having legal relations with employees regulating employment. Furthermore, legality in business became a priority, and 'legal' was equated with 'ethical'.

The last period from 2004 to 2005 is referred to as the EU convergence period. These years were characterised by a more stable political, economic and social environment, and business organizations recognized the need to go beyond purely short-term economic and legal objectives. Considerations of business ethics and corporate social responsibility became important topics of discussion, and much emphasis was put on public image and reputation. Corporate social responsibility was practiced in order to correct mistakes, at least when these were profitable and seen as being good for the company's reputation. Being considered as an equal partner among other EU and Western (but not Eastern) countries became an important aspect in business activities.

The higher stages in the Reidenbach and Robin (1991) CMD model (emerging ethical and developed ethical) were not detected in the Estonian business community during the period under analysis. According to Reidenbach and Robin (1991, 279), the responsive stage is a pivotal point in CMD since it is a stage where businesses test the efficacy of socially responsive behaviour and begin to understand the economic value of moral behaviour. We can conclude that from a historical viewpoint, there has been clear progress in corporate morality in the Estonian business community, and moral development stages have evolved along with the contextual forces. Over the 20-year period under scrutiny, the Estonian business community seems to have reached the stage where ethical statements and concerns are understood as a useful tool for creating a positive image and regarded as valuable when profitable.

Stages of Moral Development and Stakeholder Considerations in the Estonian Business Community

To further understand corporate moral development in the Estonian business community during the two decades under analysis, we incorporate the stakeholder approach into our analysis. We return to Freeman's (1984) classic definition of the stakeholder approach that states: "The stakeholder approach is about groups and individuals who can affect the organization, and is about managerial behaviour taken in response to those groups and individuals." Furthermore, Freeman (1984) defines a stakeholder as "any group or individual who can affect or is affected by the achievement of the organisation's objectives." Thus, we decided to analyze (1) who the important stakeholders were, and (2) what relations to these stakeholders were like in terms of the actions taken by business organizations or managers toward these stakeholders. In addition, we decided to include the outcomes or consequences of stakeholder relations in terms of corporate responsibility in our analysis (cf. Kujala *et al.,* 2007; see also Näsi, 1995). Table 2 describes the empirical research instrument used in this study for analyzing the stakeholder relations at different stages of corporate moral development in the Estonian business community.

In the empirical analysis, we first asked who the most important corporate stakeholders in the Estonian business community were. In this analysis, we were interested in which actors were seen as important partners and who were relations built with. After that, we moved our attention to stakeholder relations by asking what the actions toward different stakeholders were like. Finally, we looked at the outcomes by investigating the consequences of stakeholder issues to reveal concrete results of stakeholder actions as well as the drivers and motivation behind stakeholder actions.

Table 2: Framework for empirical analysis of stakeholder relations

Elements of stakeholder relations	Empirical research questions
Stakeholders	Who are the important stakeholders?
Relations	What are the actions towards these stakeholders like?
Outcomes	What are the consequences of stakeholder relations in terms of corporate responsibility?

The results of our analysis showed that during the period of socialist erosion, referring to the double morality stage of the CMD model, the main stakeholders were ministries, regional authorities and larger customers. Stakeholder considerations as we understand them today did not exist, but the Soviet system, especially in rural areas and large monopolies, made some managers take a paternalistic approach to the care of the workers and the local community. Employees were often exploited; they were just given orders, but at the same time kept from obtaining information, sometimes information that was relevant for accomplishing the tasks, and their opinions were not considered important. Ultimately, we can point out a situation where people at higher hierarchical levels had more opportunities for personal gain than others, and they often exploited these opportunities and their employees to operate various kinds of deals, barter deals and sales, and activities were often unethical and sometimes illegal. As a result of this work morale and trust were low while high levels of corruption made stealing from state organizations, bribery and blackmail as well as utilizing opportunities for personal gain possible.

The next period in the CMD model was characterized by rough entrepreneurial capitalism and the corresponding ethical vacuum and lasted from 1991 to 1995. At that time the main stakeholders involved politicians, foreign investors (who were often seeking fast and easy opportunities to financial success), owners (local owners were often in managerial positions or on corporate boards, thus directly involved in corporate activities) and banks. All other stakeholders, including the employees were treated as a means to getting things done. We can highlight privatizing former state owned organizations and starting new businesses as the main activities. These activities can be seen as a reaction to the changed environment and were often unethical and also illegal. As a result only economic responsibilities were considered important, others were neglected, even totally rejected; consideration of the impact on other stakeholders including partners, suppliers and clients was rare. A situation where the former Soviet values and norms no longer existed and nothing new emerged to replace the void increased the level of risk as well as opportunities in business.

The period 1995-1999 was characterized as the business boom period, referring to an instrumental stage in the CMD model. The main stakeholders included banks, owners, board members, shareholders and to some extent customers. Relationships were instrumental – using others as instruments for organizational and personal gain, existing to serve the needs and desires of companies and individuals – and were based on authority and power. The main activities were restructuring and re-designing old Soviet style enterprises and also starting new businesses from scratch. The main priority was to earn a profit without considering how it was done and what impact it had on others. This resulted in a situation where corporate activities and behaviour were in conflict with accepted and valued ethical principles; there was no ethical reasoning. The society and the environment were not considered important, and the employees were often exploited and treated as a means of earning a profit without any rights and no consideration for safety and healthy working conditions. Earning a profit and a tendency for finding loopholes in legislation were also characteristic of this stage.

The next period, catching-up (2000-2003), is characterized by a clear orientation towards joining the EU and NATO, and a context where legal systems were already in place. This period refers to the legalistic stage in the CMD model, as the main focus is on following the letter of the law, and where ethics and legality are often equated. The main stakeholders in this period included the owners and authorities, the State, public, media and customers. Relationships were regulated by laws and regulations and the stakeholders were treated according to the law. Legal contracts were used for the benefit of the company and the individual, responsibilities were equated with paying taxes and the legal obligations to provide goods and services had to meet the minimal legal requirements. As a result, business actors were concerned with the legality of their behaviour and activities, following a compliance strategy, being driven by the law, but indifferent to morality, focusing instead on minimum compliance.

The period 2004-2005 is referred to as the EU convergence period and corresponds with the responsive stage in the CMD model. The main stakeholders of that period were partners, customers, local community, media, and the importance of employees increased. The organizations became more sensitive to the demands of society, and being concerned about fitting in with local community expectations gained importance. There were contract based relations with the main stakeholders and maintaining good relations with those stakeholders who had the greatest impact in business activities was regarded as more important than in the previous stages. Although organizations were starting to recognise the need for moral management and understood the economic value of moral behaviour, their approach was still reactive, primarily focusing on correcting mistakes and often pursuing PR, sponsorship and charity, with the aim of gaining more profit or better reputations. As a result, the risks and opportunities were significantly decreased and there was an appeal to a sense of duty and loyalty. Organizations had a desire for approval – they were interested in fitting in with the industry and the local community and started to recognize social duties and obligations. The result of our empirical analysis is summarized in Table 3.

Discussion and Conclusions

Based on a suggestion by several researchers in the field of business ethics (e.g. Carroll, 1995; Freeman and Liedtka, 1991; Freeman *et al.,* 2004; O'Malley, 2003; Paine, 1997), this paper began with the assumption that the integration of ethical standards into business is not only preferable, but also necessary for long-term organizational survival. This paper has focused particularly on corporate moral development (CMD), which was understood here as the process of balancing concern for ethics and morality with profits. In this work the theoretical model of CMD by Reidenbach and Robin (1991) was used. In addition, stakeholder relations were discussed along with the CMD model from the viewpoint of the stakeholder concept (e.g. Freeman, 1984; Näsi, 1995) and following the ideas of Logsdon and Yuthas (1997) and Snell (2000).

CMD was empirically investigated in the Estonian context in the period from 1985 to 2005. In this period, the Estonian business community changed from a socialist to a free market system, and this change was regarded as rapid and radical, 'where almost everything in society was transformed in a short period: the political and economic system, ownership relations and citizenship, friends and enemies' (Heidmets,

Table 3: Stakeholder relations and changes in them in the five stages of corporate moral development in the Estonian business community

Stages of CMD	Stakeholders	Relations	Outcomes
Double morality Socialist erosion (1985–1990)	Ministries, higher and regional authorities, biggest customers, workers, the local community	Real stakeholder relationships did not exist, in rural areas some managers took paternalistic care of workers and the local community. Employees often exploited, were given orders and kept from getting information, their opinions not considered.	People on higher hierarchical levels had more opportunities for personal gain than others, and they often exploited these possibilities and their employees to operate various kinds of deals, barter deals and sales, activities were often unethical, sometimes illegal. Work morale low.
Ethical vacuum Rough entrepreneurial capitalism (1991–1994)	Politicians, foreign investors, owners, shareholders, boards	Privatising former state owned organizations, starting new businesses, activities unethical, often illegal. Economic responsibilities, others neglected, even totally rejected. Employees often exploited and treated as means to get things done.	A tendency to avoid responsibilities. Survival and economic responsibilities emphasised. Consideration of the impact on other stakeholders including partners, suppliers, and clients was rare.
Instrumental Business boom (1995–1999)	Banks, owners, shareholders, boards, customers	Restructuring, re-designing old Soviet style enterprises; starting from zero point, self-beneficial relationships based on authority and power, no consideration of ethics, legal standards needed to be overcome. Society and environment not considered important, employees often exploited.	Activities and behaviour discordant with accepted and valued ethical principles, no ethical reasoning. Earning profits, tendency to find loopholes in legislation.
Legalistic Catching-up (2000–2003)	State, public, media, customers	Stakeholder responsibilities equated with paying taxes, and obligations to provide goods and services meeting the minimal legal requirements. Legal contracts for company and personal gain.	Concern for the legality of behaviour and activities, following a compliance strategy, law driven, indifferent to morality, focused on minimum compliance.
Responsive EU convergence (2004–2005)	Partners, customers, local community, media, employees	More sensitive to the demands of the society, contract based relations with main stakeholders, Maintaining good relations with those of biggest impact: gaining partners' trust, meeting customers' expectations. Starting to recognise the need for moral management and understand economic value of moral behaviour, reactive style.	Decreased risks and opportunities, appeal to sense of duty, loyalty, desire for approval, interested in fitting in with industry and local community

2007). These changes also caused clear changes in terms of how stakeholders were considered, analyzed here in five different periods that correspond to the five stages of CMD in Estonia.

The fact that the CMD model (Reidenbach and Robin, 1991) as well as stakeholder theories (Freeman, 1984; 1995; Näsi, 1995) originate from developed and market-oriented business communities makes the comparisons with the two first stages in the context of the Estonian business community difficult. At the earlier stages, the key stakeholders were more typical of transition economies than developed business communities. While conducting the research we could not find anything comparable to the double morality stage, the first period of our study, within Reidenbach and Robin's model of CMD (1991) or in other studies in this field, which are mainly carried out in the context of more developed business communities. Stakeholder relations in the later periods of the Estonian business community started to resemble those of the original studies using this model. Therefore, it can be argued that the first stage depicted in our study is primarily typical of a transitional business community.

However, the second stage, the ethical vacuum stage, can be compared to Kohlberg's (1969; 1984) pre-conventional level, and is also described by several authors in the organizational context (e.g. Baxter and Rarick, 1989; Maclagan and Snell, 1992; Sridhar and Camburn, 1993; Logdson and Yuthas, 1997; Snell, 2000). As during this period practically no regulations or rules existed in business, people in business behaved any way that seemed right to them. Exploitation dominated stakeholder relations and there was a tendency to avoid responsibilities other than economic responsibilities.
We see this stage as a reaction to the changed environment, where personal gain and profitability were given preference and there was practically no room for the consideration of others or their interests. Our analysis showed that any form of moral thought or discourse was inhibited (also described in Maclagan and Snell, 1992), the emphasis was on self-aggrandizing without regard for others (e.g. Logdson and Yuthas, 1997) and avoiding harm to oneself and one's organization (e.g. Sridhar and Camburn, 1993) was typical during this period. All these characteristics are representative of the pre-conventional stage of moral development, and directed the behaviour of people in business during the ethical vacuum stage in the Estonian business context.

The third period relates to the amoral stage in Reidenbach and Robin's (1991) CMD model; however, in the literature on Organizational moral development, the amoral stage has often been characterised as an instrumental stage, where culture (Victor & Cullen, 1988) supports the maximisation of self-interests at the individual or organizational level (Weber, 1993, p. 422; Snell, 2000, p. 279). Additionally, it can be argued that the relationships and activities and behaviour of business actors in the Estonian business context at this stage can be viewed as instrumental, thus this stage is referred to as the instrumental stage in the context of the CMD model in our study. Within this period we saw that the relationships existed to serve the needs and desires of companies and individuals (see also Logdson and Juthas, 1997); these were based on authority and power.

It can be argued that powerful and influential stakeholders such as owners, board members and shareholders were considered important, while less powerful stakeholders like employees were often exploited and treated as a means for earning a profit without any rights and even no consideration for safety and healthy working conditions. Seeing organizations as a part of the society and environment was rare and issues concerning the society and the environment were practically neglected. We can argue that these features as well as equating responsibilities with making a profit, no consideration for ethics and seeing legal standards just as obstacles to be overcome are typical to the first stage in the original CMD model by Robin and Reidenbach (1991) and are also described by Carroll (1991) in his pyramid of corporate social responsibility.

The next, legalistic stage can be found in both, the original CMD model by Robin and Reidenbach (1991) and the CSR model by Carroll (1991). Our analysis showed that during that period in the Estonian business context, stakeholder responsibilities were equated with paying taxes and the obligation to provide goods and services that meet the minimal legal requirements. Legal contracts were made in the form of self-benefit, serving primarily company and personal interests. How businesses behaved was directed by the concern for the legality of the behaviour and activities following a compliance strategy and driven by the law; an indifference to morality and focusing on minimal compliance can be seen as clear signs of the legalistic stage. Furthermore, we argue that laws and regulations became more important in business activities as did creating a sense of legality and giving priority to compliance with laws and regulations in business activities around the same time as the legal systems in the Estonian business environment were being developed thereby suggesting that the former was driven by the latter.

The last period in our study refers to the responsive stage in the CMD model, where many business organizations gradually become involved in CSR activities, especially when these were profitable or created a good public image, and we can start talking about stakeholder relations with a wider range of stakeholders, including local communities and the society. During this stage, organizations started to become more sensitive to the demands of society, while having contract based relations with key stakeholders and being more interested in maintaining good relations with those stakeholders with the greatest impact. Gaining partners' trust, meeting customer expectations and starting to recognise the need for moral management and understanding the economic value of moral behaviour were characteristic of that period.

Although stakeholder relations and responsible behaviour were often used as marketing and or a PR tool during the responsive stage, and the reactive style dominated, we can argue that the level of CMD and consideration for stakeholders had improved in comparison with previous stages. Moreover, Reidenbach and Robin (1991, p. 279) have identified this stage as a pivotal point for most corporations, describing it as a learning stage wherein businesses test the efficacy of socially responsible behaviour and begin to understand the economic value of moral behaviour, and moving beyond this stage means changing their reactive into proactive behaviour and this requires the recognition of the social contract between business and society.

However, the situation in the Estonian business context has not yet improved, and thus it is not possible to speak about the next emerging ethical and developed ethical stages of CMD. In other words, when looking at the results of this study, it can be seen that Estonian business organizations have not developed further than the responsive stage of the CMD model developed by Reidenbach and Robin (1991), but when we look at the situation from the historical viewpoint this study shows clear progress in CMD.

The results of this study show that during the rapid and radical changes in Estonia it was the external context, especially factors in the political and economic environments that played a more important role in shaping CMD and stakeholder relationships than the internal forces within companies. Hence, we argue that changes in stakeholder relations can be directly related to changes in the environment. At different developmental stages, different kinds of stakeholders were considered important for the businesses. In the earlier stages of corporate moral development, we find stakeholders who are more characteristic to transition economies, such as ministries, politicians and regional authorities. The role of such officials became lower at the instrumental level, but higher again at the legalistic level. This study showed how stakeholder relations developed from give-and-take type relations during the earlier stages of corporate moral development towards more reactive or even proactive interaction during the later stages. Stakeholder relations started to develop in parallel with the development of the business community. However, understanding relations with stakeholders as truly collaborative or mutually beneficial is still rare in the Estonian business community. This can also be seen in the outcomes of stakeholder relations where responsibility, respect and trust among business actors are not yet part of everyday business practices.

In conclusion we can say that although political as well as economic environments will probably continue to play an important role in shaping CDM in the future in Estonia, the role of stronger social values is currently being discussed and publicly demanded. And although it was a more stable environment (politically, economically as well as socially) that enabled business organizations to recognize the need to go beyond purely short-term economic and legal objectives during the responsive stage, and not an internal need or understanding, the understanding of the value of long-term perspectives and sustainability can be seen as encouraging developments from this study. The fact that businesses are thinking for the long-term and sustainability in business activities are gaining increasingly more attention and importance gives us a reason to believe that it is possible to talk about emerging ethical and maybe even developed ethical stages of corporate moral development within the context of the Estonian business organizations in the future.

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Can Organizational Culture Predict Individual and Organizational Level Factors?

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Abstract

The purpose of this paper is to investigate connections between organizational culture and individual and organizational level factors. The survey was conducted in Chinese, Estonian, Japanese, Slovakian, Russian and Czech electrical-electronic machine, retail, information-software production and machine-building enterprises. A linear regression analysis was conducted in order to analyze connections between types of organizational culture – clan, market, hierarchy, adhocracy; individual level factors – job satisfaction, attitude towards the firm, meaning of work; and organizational level factors – powerfulness of the firm in competition with rivals, the behaviour of the management and company policy. The total number of respondents was 5742.

The results of an empirical study show that the types of organizational culture – clan, market, hierarchy and adhocracy – predict job satisfaction, attitude towards the firm, meaning of work, powerfulness of the firm in competition with rivals, the behaviour of the management and company policy, but it varies country by country. The 11 models developed explain how 4 types of organizational culture predict individual and organizational level factors in Chinese, Estonian, Japanese, Slovakian, Russian and Czech enterprises.

Keywords: organizational culture, job satisfaction, meaning of work, attitude towards the firm, powerfulness of the firm in competition with rivals, the behaviour of the management, company policy, Estonia, China, Slovakia, Czech, Russia, Japan.

Introduction

This paper analyses connections between types of Organizational culture – clan, market, hierarchy and adhocracy; individual level factors – job satisfaction, attitude towards the firm, meaning of work; and organizational level factors – powerfulness of the firm in competition with rivals, the behaviour of the management and company policy in Chinese, Estonian, Japanese, Slovakian, Russian and Czech enterprises.

The main research questions are: how does organizational culture predict individual and organizational level factors? Are there connections between organizational culture and job satisfaction, attitude towards the firm, meaning of work, powerfulness of the firm in competition with rivals, the behaviour of the management and company policy?

This paper will continue now with the discussion and defining of the main concepts and terms used. This will be following by a discussion of the relevant theory. Then we will describe the emprical study and the results of that study before presenting our concluding remarks.

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Organizational culture

According to Schein (1992), Organizational culture is the pattern of basic assumptions that a given group has invented, discovered or developed in learning to cope with its problems of external adaptation and integral integration. Trice and Beyer (1993) have also connected culture with environment, seeing Organizational culture as a collective response to uncertainty and chaos.

According to Cameron and Quinn (1999), there are many kinds or levels of culture that affect individual and organizational behaviour. At the broadest level, a global culture, such as the culture of a world religion or the culture of the Eastern hemisphere, would be the highest level

The researchers Hofstede (1980) and Trompenaars (1992) have reported marked differences between countries based on certain key dimensions. For example, national differences exist between countries on the basis of universalism versus particularism, individualism versus collectivism, neutrality versus emotionality, specificity versus diffuseness, focus on achievement versus ascription, focus on past versus present versus future and an internal focus versus an external focus (Trompenaars, 1992).

According to Cameron and Quinn (1999), culture defines the core values, assumptions, interpretations and approaches that characterise an organization. A Competing Values Framework is extremely useful in helping to organize and interpret a wide variety of organizational phenomena. The four dominant types of culture – hierarchy, market, clan and adhocracy emerge from the framework. Most organizations develop a dominant cultural style. More than 80 percent of the several thousand organizations they studied have been characterized by one or more of the culture types identified by the framework. Those that do not have a dominant cultural type either tend to be unclear about their culture, or they emphasize nearly equally the four different cultural types.

The Hierarchy Culture

Weber (1947) proposed seven characteristics that have become known as the classical attributes of bureaucracy (rules, specialization, meritocracy, hierarchy, separate ownership, impersonality and accountability). They were adopted widely in organizations whose major challenge was to generate an efficient, reliable, smooth-flowing and predictable output.

The organizational culture compatible with this form is characterized by a formalized and structured workplace. Effective leaders are good coordinators and organizers. Maintaining a smooth-running organization is important. The long-term concerns of the organization are stability, predictability and efficiency. Formal rules and policies hold the organization together. New employees begin by doing only one specific job (Cameron and Quinn, 1998).

The Market Culture

The market type of organizational culture was based largely on the work of Williamson (1975) and Ouchi (1981). The term market refers to a type of organization that functions as a market itself. It is oriented towards the external environment instead of internal affairs. It is focused on transactions with external constituencies including suppliers, customers, contractors, licensees, unions, regulators and so forth. The market operates primarily through economic market mechanisms, mainly monetary exchange. In other words, the major focus of a market culture is to conduct transactions (exchanges, sales, contracts) with other constituencies to create competitive advantage. Profitability, bottom line results, strength in market niches, stretch targets and secure customer bases are primary objectives of the organization. The core values that dominate market type organizations are competitiveness and productivity. The major task of the management is to drive the organization towards productivity, results and profits. It is assumed that a clear purpose and an aggressive strategy lead to productivity and profitability (Cameron and Quinn, 1999).

The Clan Culture

A number of researchers observed fundamental differences between the market and hierarchy forms in America and clan forms in Japan (Ouchi, 1981; Pascale and Athos, 1981). It is called a clan because of its similarity to a family-type organization. Typical characteristics of clan-type firms include teamwork, employee involvement programs and corporate commitment to the employee.

Some basic assumptions in a clan culture are that the environment can best be managed through teamwork and employee development, customers are best thought as partners, the organization is in the business of developing a humane work environment and the major task of management is to empower employees and facilitate their participation, commitment and loyalty (McGregor, 1960; Likert, 1970; Argyris, 1964).

The organization is held together by loyalty and tradition. The organization emphasizes the long-term benefit of individual development with high cohesion and morale being important. Success is defined in terms of the internal climate and concern for people (Cameron and Quinn, 1998).

The Adhocracy Culture

The root of the word adhocracy is ad hoc – referring to a temporary, specialized, dynamic unit. Most people have served on an ad hoc task force or committee, which disbands as soon as its task is completed. Adhocracies are similarly temporary. They have been characterized as "tents rather than palaces" in that they can reconfigure themselves rapidly when new circumstances arise. A major goal of an adhocracy is to foster adaptability, flexibility and creativity where uncertainty, ambiguity and/or information-overload are typical. An important challenge of these organizations is to produce innovative products and services and to adapt quickly to new opportunities. Unlike markets or hierarchies, adhocracies do not have centralized power or authority relationships. Instead, power flows from individual to individual or from task team to task team depending on what problem is being addressed at the time. A high emphasis on individuality, risk taking and anticipating the future exists as almost everyone in an adhocracy becomes involved with production, clients, research and development and so forth (Cameron and Quinn, 1999).

Connections between Organizational culture, individual and Organizational level factors

Organizational culture and job satisfaction

Sempane, Rieger and Roodt (2002) conducted a study in a service organisation to establish whether a relationship existed between job satisfaction and Organizational culture among employees within a service organisation. Their research has proven a significant positive correlation between these two variables (r = 0,743). In a study conducted by Tzeng, Ketefian and Redman (2002), they wanted to determine the relationship between nurses' assessment of Organizational culture, job satisfaction and patient satisfaction and nursing care. They found that the strength of Organizational culture predicted job satisfaction well and positively.

Silverthorne (2004) found that organizational culture plays an important role in the level of job satisfaction and commitment in an organization.

Lund (2003) examined the impact of types of Organizational culture on job satisfaction according to Cameron and Freeman's (1991) model of organizational cultures comprising clan, adhocracy, hierarchy and market cultures. The results indicate that job satisfaction levels varied across the corporate cultural typology. Job satisfaction was positively related to clan and adhocracy cultures and negatively related to market and hierarchy cultures.

Organizational culture and attitudes toward the firm

Organizational culture is important because shared beliefs and norms affect employee perceptions, behaviours, and emotional responses to the workplace. For example, culture has been found to influence organizational climate and provider attitudes including work attitudes (Aarons and Sawitzky, 2006; Carmazzi and Aarons, 2003; Glisson and Hemmelgarn, 1998; Glisson and James, 2002), as well as employee behaviours that contribute to the success or failure of an organization (Ashkanasy, Wilderom and Peterson, 2000).

Organizational culture and meaning of work

According to Seel (2000), organisation culture is the emergent result of continuing negotiations about values, meanings and proprieties between the members of that organisation and with its environment. In other words, culture is the *result* of all the daily conversations and negotiations between the members of an organisation. They are continually agreeing (sometimes explicitly, usually tacitly) about the 'proper' way to do things and how to form meaning about the events of the world around them.

According to Stevens (1991), effective strategy implementation depends on the extent to which resultant changes conform to existing knowledge structures used by members of the organization to make sense of and give meaning to their work. Such cognitive paradigms form the cultural construct of the organization.

Organizational culture and behavior of management

According to Kanne-Urrabazo (2006), many managers do not deny the importance of organizational culture in employee satisfaction, and few fail to realize the direct impact they have in shaping it. It is oftentimes believed that cultures are predetermined; however, this is a false assumption. It is crucial that managers at all levels are aware of their roles and responsibilities in upholding positive workplace environments that can increase employee satisfaction.

According to Schein (2004), organizational cultures are created by leaders, and one of the most decisive functions of leadership may well be the creation, management and – if and when that may become necessary – the destruction of a culture.

Organizational culture and firm policy

According to Cronqvist, Low and Nilsson (2007), and consistent with predictions from economic theories about corporate culture, they also found that the effects of corporate culture in the policies of the firm are long-term and stronger for internally grown business units and older firms. Their evidence is also consistent with firms preserving their cultures by selecting management teams that fit the culture. Their evidence showed that a firm's corporate culture matters in its policy choices and performance.

Organizational culture and competitive advantage

According to Cameron and Quinn (1999), the major distinguishing feature in successful companies, their most important competitive advantage and the most powerful factor they all highlight as a key ingredient in their success, is their organizational culture.

Three attributes that a firm's culture must have to generate sustained competitive advantages have been isolated. Previous findings suggest that the cultures of some firms have these attributes; thus, these cultures are a source of such advantages according to Barney (1986).

Based on the relevant literature we developed the following general propositions:

P1. Four types of Organizational culture – hierarchy, market, clan and adhocracy predict individual level factors – job satisfaction, attitude towards the firm and the meaning of work.

P2. Four types of Organizational culture – hierarchy, market, clan and adhocracy predict organizational level factors – powerfulness of the firm in competition with rivals, the behaviour of the management and company policy.

Empirical study

The authors of this article conducted the study in Chinese, Estonian, Japanese, Slovakian, Russian and Czech enterprises. In order to find connections between types of Organizational culture and job satisfaction, attitude towards the firm, the meaning of work, powerfulness of the firm in competition with rivals, the behaviour of the management and company policy in Chinese, Estonian, Japanese, Slovakian, Russian and Czech enterprises, the authors conducted an empirical study in 2007–2008. The research was conducted with 1150 respondents in Chinese enterprises, with 623 respondents in Estonian enterprises, with 1570 respondents in Japanese enterprises, with 605 respondents in Slovakian enterprises, with 684 respondents in Russian enterprises and with 1110 respondents in Czech enterprises. The companies were selected in a non-random manner, as the organisation registers do not have a solid basis for random sampling because only a fraction of the registered enterprises are active in China, Estonia, Japan, Slovakia, Russia and the Czech Republic. The total number of respondents was 5742.

Methodology A standardised questionnaire comprising 64 items was developed by the Denki Ringo research group (Ishikawa et al, 2006) and translated from English into Chinese, Estonian, Japanese, Slovak, Russian and Czech. The questionnaire was administered in Chinese, Estonian, Japanese, Slovakian, Russian and Czech electrical-electronic machine, retail, information-software production and machine-building enterprises. The questions in the survey addressed 4 different types of culture – hierarchy, clan, market, adhocracy; individual level factors – job satisfaction, attitude towards the firm, the meaning of work; and organizational level factors – powerfulness of the firm in competition with rivals, the behaviour of the management and company policy.

The linear regression analysis was used in order to find statistically relevant connections between individual and organizational level factors and 4 types of Organizational culture – hierarchy, clan, market and adhocracy.

The main research question is: Do the four types of Organizational culture – hierarchy, market, clan and adhocracy predict the individual level factors – job satisfaction, attitude towards the firm, meaning of work; and the organizational level factors – powerfulness of the firm in competition with rivals, the behaviour of the management and company policy?

Results

New Scales of four Organizational culture types – clan, market, hierarchy, adhocracy

Based on Cameron and Quinn (1999), we developed subscales for measuring the types of organizational culture. Items were selected. The internal consistency, or Cronbach Alpha coefficient was .92 for clan culture, .90 for market culture, .87 for hierarchy culture and .91 for adhocracy culture.

We developed a questionnaire for measuring the four types of Organizational culture. The final version consists of 19 items, which form four subscales – with 5 items for clan, 4 items for market , 5 items for hierarchy and 5 items for adhocracy.

Connections between Organizational culture types, individual and Organizational level factors

Our main purpose was to evaluate how organizational culture predicts individual and organizational level factors. The authors used a linear regression analysis. In the analysis individual and organizational level factors were taken as a dependent variable and types of culture as independent variables. We calculated a standardised regression coefficient Beta, which

Table 1: Four types of Organizational culture forecast individual and organizational level factors in Chinese enterprises (according to standardised regression coefficient Beta).

		B	Beta	t	Sig.
CHINA					
Individual level factors Job satisfaction					
N=1150, R^2=.019, F(4.1145)=5.6838, p<.000	CLAN	.013	.018	0.450	.652
	MARKET	.003	.004	0.099	.920
	HIERARCHY	.011	.030	0.982	.325
	ADHOCRACY	.086	.112	2.675	**.007***
Attitude towards the firm					
N=1150, R^2=.001, F(4.1134)=53552, p<.000	CLAN	.000	.000	0.019	.984
	MARKET	-.004	-.012	-0.315	.752
	HIERARCHY	-.007	-.041	-1.338	.181
	ADHOCRACY	.007	.020	0.519	.603
Meaning of work					
N=1150, R^2=.072, F(4.1145)=22.327, p<.000	CLAN	.065	.056	1.434	.151
	MARKET	.013	.011	0.273	.784
	HIERARCHY	.043	.072	2.411	.016
	ADHOCRACY	.231	.191	4.670	**.000***
Organizational level factors Powerfulness of the firm in competition with rivals					
F(4.1136)=75435 p<.000	CLAN	-.002	-.004	-0.117	.906
	MARKET	-.010	-.018	-0.456	.648
	HIERARCHY	-.003	-.013	-0.423	.671
	ADHOCRACY	.036	.063	1.564	.117
Behaviour of management					
N=1150, R^2=.002, F(4.1136)=66745 p<.000	CLAN	.005	.014	0.392	.694
	MARKET	-.000	-.002	-0.068	.945
	HIERARCHY	-.006	-.034	-1.119	.263
	ADHOCRACY	.012	.033	0.879	.379
Company policy					
N=1150, R^2=.003, F(4.1128)=94225, p<.000	CLAN	.011	.011	0.365	.714
	MARKET	.029	.029	0.886	.375
	HIERARCHY	.013	.034	1.145	.252
	ADHOCRACY	.010	.010	0.321	.747
Notes. * - coefficient statistically significant, p<0,01					

enabled us to predict how strongly organizational culture forecast the individual level factors and the organizational level factors. The analysis was applied separately for each of the 4 types of culture and for the 3 individual level factors and organizational level factors.

The four types of Organizational culture predict the individual level factors and the organizational level factors differently in different countries (Table 1, 2, 3, 4, 5, 6).

According to the linear regression analysis results in Table 1, the adhocracy culture predicts job satisfaction (R^2=.019, F(4.1145)=5.6838, p<.000) and meaning of work (R^2=.072, F(4.1145)=22.327, p<.000) in Chinese enterprises. The predictive power of the other individual and organizational level dependent variables is not so uniform and differs according to the variable. The determinant coefficients R^2 are calculated for the regression model including the four types of Organizational culture as independent variables.

Table 2: Four types of Organizational culture forecast individual and organizational level factors in Estonian enterprises (according to standardised regression coefficient Beta).

		B	Beta	t	Sig.
ESTONIA					
Individual level factors					
Job satisfaction					
N=623, R^2=.466, F(4.618)=135.12, p<.000	CLAN	.382	.094	2.032	.042
	MARKET	.347	.545	10.760	**.000***
	HIERARCHY	.351	.129	2.826	**.004***
	ADHOCRACY	-.154	-.047	-1.045	.296
Attitude towards the firm					
N=623, R^2=.669, F(4.618)=313.50, p<.000	CLAN	.378	.293	8.022	**.000***
	MARKET	.232	.169	4.250	**.000***
	HIERARCHY	.189	.219	6.088	**.000***
	ADHOCRACY	.256	.250	6.941	**.000***
Meaning of work					
N=623, R^2=.246, F(4.618)=50.424, p<.000	CLAN	.281	.155	2.816	**.005***
	MARKET	.521	.155	4.497	**.000***
	HIERARCHY	-.173	-.143	-2.632	**.008***
	ADHOCRACY	.340	.237	4.347	**.000***
Organizational level factors					
Powerfulness of the firm in competition with rivals					
N=623, R^2=.554, F(4.618)=192.17 p<.000	CLAN	.018	.009	0.220	.906
	MARKET	.871	.425	9.182	**.000***
	HIERARCHY	.308	.237	5.690	**.000***
	ADHOCRACY	.229	.149	3.575	**.000***
Behaviour of management					
N=623, R^2=.644, F(4.618)=280.28 p<.000	CLAN	.486	.293	7.743	**.000***
	MARKET	.675	.382	9.263	**.000***
	HIERARCHY	.217	.195	5.233	**.000***
	ADHOCRACY	.028	.021	0.572	**.000***
Company policy					
N=623, R^2=.638, F(4.618)=273.31, p<.000	CLAN	.526	.518	13.560	**.000***
	MARKET	.227	.072	1.739	.082
	HIERARCHY	-.087	-.044	-1.170	.242
	ADHOCRACY	.747	.319	8.454	**.000***
Notes. * - coefficient statistically significant, p<0,01					

According to the linear regression analysis results in Table 2, all four cultures – clan, market, hierarchy and adhocracy – predict attitude towards the firm (R^2=.669, F(4.618)=313.50, p<.000) and meaning of work (R^2=.019, F(4.1145)=5.6838, p<.000) in Estonian enterprises. The individual level factor, job satisfaction, is predicted by market and hierarchy culture types (R^2=.466, F(4.618)=135.12, p<.000). Among organizational level factors, powerfulness of the firm in competition with rivals, is predicted by market, hierarchy and adhocracy culture types (R^2=.554, F(4.618)=192.17, p<.000); the behaviour of the management is predicted by clan, market and hierarchy culture types (R^2=.644, F(4.618)=280.28, p<.000); and company policy is predicted by clan and adhocracy (R^2=.638, F(4.618)=273.31, p<.000). The determinant coefficients R^2 are calculated for the regression model including the four types of Organizational culture as independent variables.

Table 3: Four types of Organizational culture forecast individual and organizational level factors in Japanese enterprises (according to standardised regression coefficient Beta).

		B	Beta	t	Sig.
JAPAN					
Individual level factors **Job satisfaction**					
N=1570, R^2=.023, F(4.1565)=9.6115, p<.000	CLAN	-.109	-.149	-2.628	.008*
	MARKET	-.004	-.006	-0.121	.903
	HIERARCHY	.028	.036	0.654	.512
	ADHOCRACY	.186	.240	3.716	**.000***
Attitude towards the firm					
N=1570, R^2=.002, F(4.1529)=.81749, p<.000	CLAN	.000	.000	0.009	.992
	MARKET	-.002	-.007	-0.189	.849
	HIERARCHY	-.006	-.024	-0.570	.568
	ADHOCRACY	-.005	-.019	-0.399	.689
Meaning of work					
N=1570, R^2=.046, F(4.1565)=19.258, p<.000	CLAN	.023	.042	0.755	.450
	MARKET	-.099	-.162	-3.296	**.001***
	HIERARCHY	-.009	-.015	-0.279	.779
	ADHOCRACY	.182	.311	4.860	**.000***
Organizational level factors **Powerfulness of the firm in competition with rivals**					
N=1570, R^2=.010, F(4.1528)=4.1516 p<.000	CLAN	-.022	-.057	-1.229	.218
	MARKET	-.007	-.017	-0.430	.666
	HIERARCHY	-.060	-.144	-3.154	**.001***
	ADHOCRACY	.068	.164	3.074	**.002***
Behaviour of management					
N=1570, R^2=.017, F(4.1531)=7.0007 p<.000	CLAN	-.010	-.034	-0.808	.418
	MARKET	-.018	-.056	-1.478	.139
	HIERARCHY	-.045	-.153	-3.535	**.000***
	ADHOCRACY	.075	.251	5.094	**.000***
Company policy					
N=1570, R^2=.056, F(4.1531)=23.047, p<.000	CLAN	-.014	-.033	-0.791	.428
	MARKET	-.072	-.153	-4.132	**.000***
	HIERARCHY	-.004	-.011	-0.262	.792
	ADHOCRACY	-.029	-.064	-1.346	.178
Notes. * - coefficient statistically significant, p<0,01					

According to the linear regression analysis results in Table 3, among individual level factors, job satisfaction is predicted by clan and adhocracy culture types (R^2=.023, F(4.1565)=9.6115, p<.000) and meaning of work is predicted by market and adhocracy culture types (R^2=.046, F(4.1145)=19.258, p<.000) in Japanese enterprises. Among organizational level factors, powerfulness of the firm in competition with rivals (R^2=.010, F(4.1528)=4.1516, p<.000) and the behaviour of the management (R^2=.017, F(4.1531)=7.0007, p<.000) are predicted by hierarchy and adhocracy culture types; company policy is predicted by the market culture (R^2=.056, F(4.1531)=23.047, p<.000).

Among individual level factors, attitude towards the firm isn't predicted by any culture types in Japanese enterprises. The predictive power of the other individual and organizational level dependent variables is not so uniform and differs according to the variable. The determinant coefficients R^2 are calculated for the regression model including the four types of Organizational culture as independent variables. Thus, our hypothesis is supported by the results of the empirical analysis.

Table 4: Four types of Organizational culture forecast individual and organizational level factors in Slovakian enterprises (according to standardised regression coefficient Beta).

		B	Beta	t	Sig.
SLOVAKIA					
Individual level factors					
Job satisfaction					
N=605, R^2=.021, F(4.1573)=9.6118, p<.000	CLAN	-.210	-.058	-0.938	.348
	MARKET	.026	.219	3.523	**.000***
	HIERARCHY	.177	.051	0.870	.384
	ADHOCRACY	.048	.316	5.251	**.000***
Attitude towards the firm					
N=605, R^2=.003, F(4.143)=.81256, p<.000	CLAN	.102	.066	1.061	.289
	MARKET	-.001	-.000	-0.011	.990
	HIERARCHY	.148	.101	1.697	.090
	ADHOCRACY	.205	.141	2.349	**.019***
Meaning of work					
N=605, R^2=.042, F(4.1672)=18.269, p<.000	CLAN	-.020	-.013	-0.225	.821
	MARKET	.536	.275	4.596	**.001***
	HIERARCHY	.088	.059	1.066	.286
	ADHOCRACY	.295	.207	3.574	**.000***
Organizational level factors					
Powerfulness of the firm in competition with rivals					
N=605, R^2=.012, F(4.1535)=4.1476, p<.000	CLAN	.104	.036	0.620	.535
	MARKET	.035	.296	4.943	**.000***
	HIERARCHY	.103	.039	0.702	.482
	ADHOCRACY	.458	.178	3.110	**.002***
Behaviour of management					
N=605, R^2=.019, F(4.1642)=7.0009, p<.000	CLAN	.157	.101	1.880	.060
	MARKET	.396	.201	3.636	**.000***
	HIERARCHY	.220	.149	2.857	**.004***
	ADHOCRACY	.349	.243	4.586	**.000***
Company policy					
N=605, R^2=.057, F(4.1563)=23.065, p<.000	CLAN	.392	.133	2.383	**.017***
	MARKET	.786	.209	3.629	**.000***
	HIERARCHY	.657	.236	4.348	**.000***
	ADHOCRACY	.263	.098	1.782	.075
Notes. * - coefficient statistically significant, p<0,01					

According to the linear regression analysis results in Table 4, among individual level factors, job satisfaction (R^2=.021, F(4.1573)=9.6118, p<.000) and meaning of work (R^2=.042, F(4.1672)=18.269, p<.000) are predicted by market and adhocracy culture types and attitude towards the work is predicted by the adhocracy culture type (R^2=.003, F(4.143)=.81256, p<.000) in Slovakian enterprises. Among organizational level factors, powerfulness of the firm in competition with rivals is predicted by market and adhocracy culture types (R^2=.012, F(4.1535)=4.1476, p<.000), the behaviour of the management is predicted by market, hierarchy and adhocracy culture types (R^2=.019, F(4.1642)=7.009, p<.000) and company policy is predicted by clan, market and hierarchy culture types (R^2=.057, F(4.1563)=23.065, p<.000). The determinant coefficients R^2 are calculated for the regression model including the four types of Organizational culture as independent variables. Thus, our hypothesis is supported by the results of the empirical analysis.

Table 5: Four types of organizational culture forecast individual and organizational level factors in Russian enterprises (according to standardised regression coefficient Beta).

		B	Beta	t	Sig.
RUSSIA					
Individual level factors					
Job satisfaction					
N=684, R^2=.693 F(4.611)=346.25, p<.000	CLAN	.406	.103	1.327	.185
	MARKET	.450	.089	1.223	.222
	HIERARCHY	.070	.017	0.248	.804
	ADHOCRACY	-.065	-.018	-0.259	.795
Attitude towards the firm					
N=684, R^2=.112, F(4.219)=6.9650, p<.000	CLAN	.022	.014	0.203	.838
	MARKET	.464	.239	3.456	**.000***
	HIERARCHY	.234	.150	2.264	.024
	ADHOCRACY	.106	.077	1.168	.244
Meaning of work					
N=684, R^2=.004, F(4.217)=.24794, p<.000	CLAN	-.058	-.040	-0.520	.603
	MARKET	-.002	-.001	-0.017	.985
	HIERARCHY	.066	.044	0.620	.535
	ADHOCRACY	-.048	-.036	-0.513	.608
Organizational level factors					
Powerfulness of the firm in competition with rivals					
N=684, R^2=.230, F(4.218)=16.351, p<.000	CLAN	.425	.177	2.608	**.009***
	MARKET	.788	.260	4.021	**.000***
	HIERARCHY	.363	.149	2.397	**.017***
	ADHOCRACY	.269	.124	2.001	.046
Behaviour of management					
N=684, R^2=.226, F(4.216)=15.842, p<.000	CLAN	.287	.143	2.095	.037
	MARKET	.559	.218	3.365	**.000***
	HIERARCHY	.204	.098	1.568	.118
	ADHOCRACY	462	.255	4.078	**.000***
Company policy					
N=684, R^2=.326, F(4.200)=24.254, p<.000	CLAN	.655	.245	3.724	**.000***
	MARKET	.803	.234	3.754	**.000***
	HIERARCHY	.489	.178	2.917	**.003***
	ADHOCRACY	.469	.199	3.247	**.001***
Notes. * - coefficient statistically significant, p<0,01					

According to the linear regression analysis results in Table 5, among individual level factors, attitude towards the firm is predicted by the market culture type (R^2=.112, F(4.219)=6.9650, p<.000) in Russian enterprises. Among organizational level factors, powerfulness of the firm in competition with rivals is predicted by clan, market and hierarchy culture types (R^2=.230, F(4.218)=16.351, p<.000); the behaviour of the management is predicted by market and adhocracy culture types (R^2=.226, F(4.216)=15.842, p<.000); and company policy is predicted by all four types of Organizational culture (R^2=.326, F(4.200)=24.254, p<.000). Among individual level factors, job satisfaction and meaning of work are not predicted by any culture types. The predictive power of these two individual level dependent variables is not so uniform. The determinant coefficients R^2 are calculated for the regression model including the four types of Organizational culture as independent variables. Thus, our hypothesis is supported by the results of the empirical analysis.

Table 6: Four types of organizational culture forecast individual and organizational level factors in Czech enterprises (according to standardised regression coefficient Beta).

		B	Beta	t	Sig.
CZECH					
Individual level factors					
Job satisfaction					
N=1110, R^2=.186 , F(4.603)=34.590, p<.000	CLAN	.333	.343	0.864	.431
	MARKET	.013	.875	4.342	**.000***
	HIERARCHY	.701	.640	1.634	.118
	ADHOCRACY	.669	.641	5.704	**.000***
Attitude towards the firm					
N=1110, R^2=.1 3 4 , F(4.643)=25.003, p<.000	CLAN	.151	.763	1.572	.079
	MARKET	.567	.914	4.345	**.000***
	HIERARCHY	.344	.828	2.284	.042
	ADHOCRACY	.021	.430	3.577	**001***
Meaning of work					
N=1110, R^2=.063 , F(4.611)=10.306, p<.000	CLAN	.323	.182	0.967	.691
	MARKET	.950	.354	3.431	**.002***
	HIERARCHY	-.812	-.426	-0.792	.327
	ADHOCRACY	.691	.631	3.049	**000***
Organizational level factors					
Powerfulness of the firm in competition with rivals					
N=1110, R^2=.003, F(4.629)=56025, p<.000	CLAN	.805	.397	0.445	.398
	MARKET	-.190	-.076	-0.666	.867
	HIERARCHY	-.674	-.308	-0.979	.485
	ADHOCRACY	-.963	-.506	-1.653	.287
Behaviour of management					
N=1110, R^2=.597, F(4.989)=366.39 p<.000	CLAN	.297	.189	0.908	.623
	MARKET	.208	.709	9.006	**.000***
	HIERARCHY	.457	.864	2.776	**.017***
	ADHOCRACY	.382	.298	5.741	**.000***
Company policy					
N=1110, R^2=.413, F(4.631)=111.13, p<.000	CLAN	.996	.773	2.654	**.030**
	MARKET	.803	.699	10.543	**.000***
	HIERARCHY	.356	.484	1.416	.149
	ADHOCRACY	.749	.211	8.046	**.001***
Notes. * - coefficient statistically significant, p<0,01					

According to the linear regression analysis results in Table 6, among individual level factors, job satisfaction is predicted by market and adhocracy culture types (R^2=.186, F(4.603)=34.590, p<.000), attitude towards the firm is predicted by market and adhocracy culture types (R^2=.134, F(4.643)=25.003, p<.000) and meaning of work is predicted by market and adhocracy culture types (R^2=.063, F(4.611)=10.306, p<.000) in Czech enterprises. Among organizational level factors, the behaviour of the management is predicted by market, hierarchy and adhocracy culture types (R^2=.597, F(4.989)=366.39, p<.000) and company policy is predicted by market and adhocracy culture types (R^2=.413, F(4.631)=111.13, p<.000). The organizational level factor, powerfulness of the firm in competition with rivals, is not predicted by any culture types in Czech enterprises. The determinant coefficients R^2 are calculated for the regression model including the four types of Organizational culture as independent variables. Thus, our hypothesis is supported by the results of the empirical analysis.

Conclusions

The results of this study contribute to understanding the connections between organizational culture, and individual and organizational level factors. We compared data from Chinese, Estonian, Japanese, Slovakian, Russian and Czech electrical-electronic machine, retail, information-software production and machine-building enterprises.

The national culture where the organization operates influences how types of Organizational culture predict individual and organizational level factors. In different countries different types of Organizational culture dominate. Nowadays, it is even common for a subunit of one type of Organizational culture to exist in larger organizations that have a dominant culture of a different type.

There is a critical need for cultural change in modern organizations. The chaotic, rapid-fire vacillations in the external environment create the risk that yesterday's organizational culture will inhibit rather than contribute to corporate success (Cameron, Quinn, 1999). Nowadays, it is also common that the culture in an organization has changed over time, so that now it consists of traits of different types of culture. Usually, one culture dominates. Therefore, it is important to be aware of all the types of culture that exist in the organization and their impact on individual and organizational level factors.

There are many kinds or levels of culture that affect individual and organizational behaviour. At the broadest level, a global culture, such as the culture of a world religion or the culture of the Eastern hemisphere, would be the highest level. Researchers, such as Hofstede (1980) and Trompenaars (1992), have reported marked differences between continents and countries based on certain key dimensions. For example, national differences exist between countries on the basis of universalism versus particularism, individualism versus collectivism etc. (Trompenaars, 1992).

According to Cameron and Quinn (1998), typical characteristics of clan-type firms include teamwork, employee involvement programs and corporate commitment to employees. The market culture is focused on transactions with external constituencies, including suppliers, customers, contractors, licensees, unions, regulators and so forth. Clear lines of decision-making authority, standardized rules, procedures, control and accountability mechanisms are valued as key to success in the hierarchy culture-type. A major goal of adhocracy is to foster adaptability, flexibility and creativity, and uncertainty, ambiguity and/or information-overload are typical to organisations with an adhocracy culture. These different aspects of four types of Organizational culture influence individual and organizational level factors.

According to our study in different countries different culture types predict individual and organizational level factors differently (Figure 1, 2).

The propositions discussed at the beginning of the paper will now be re-evaluated. *P1* which postulated that the four types of organizational culture – hierarchy, market, clan and adhocracy – predict the individual level factors – job satisfaction, meaning of work and attitude towards the firm was supported, but the support varies in different countries. Job satisfaction is predicted by clan culture in Japan, market culture in Estonia, Slovakia and Czech, hierarchy in Estonia and adhocracy in China, Japan, Slovakia and the Czech Republic. Meaning of work is predicted by clan culture in Estonia, market culture in Estonia, Japan, Slovakia and Czech, hierarchy in Estonia and adhocracy in China, Estonia, Japan, Slovakia and the Czech Republic. Attitude towards the firm is predicted by clan culture in Estonia, by market culture in Estonia, Russia and the Czech Republic, hierarchy in Estonia, and adhocracy in Estonia, Slovakia and the Czech Republic.

P2 postulated that the four types of organizational culture – hierarchy, market, clan and adhocracy – predict the organizational level factors – powerfulness of the firm in competition with rivals, the behaviour of the management and company policy. The *P2* postulate was also supported and it also varies in different countries.

The clan culture predicts powerfulness of the firm in competition with rivals in Russia, while this was predicted by the market culture in Estonia, Slovakia and Russia, the hierarchy culture in Estonia, Japan and Russia, and the adhocracy culture in Estonia, Japan and Slovakia. The clan culture predicts the behaviour of the management in Estonia, while this is predicted by the market culture in Estonia, Slovakia, Russia and the Czech Republic, the hierarchy culture in Estonia, Japan, Slovakia and the Czech Republic and the adhocracy culture in Japan, Slovakia, Russia and the Czech Republic. The clan culture predicts company policy in Estonia, Slovakia and Russia, while this is predicted by the market culture in Japan, Slovakia, Russia and the Czech Republic, the hierarchy culture in Slovakia and Russia, and the adhocracy culture in Estonia, Russia and the Czech Republic.

Exactly how Organizational culture forms a part of all the possible important intangible attributes may vary from Organizational unit to Organizational unit, or even among national cultures. A large part of these "intangible attributes" are human and can therefore be captured (DiMaggio, 1997).

According to Muijen and Koopman (1994), organizational culture of industrial organizations was studied in 10 European countries using the FOCUS-instrument, based on the Quinn model (Quinn, 1988) to measure organizational culture. One possible explanation for their findings is that not only do national preferences influence the values within an organization, but also the values of its founders and important leaders in the sector are also influential.

Hofstede et al. (1990) found that, whereas organizations from different nations differ in fundamental values, organizations from the same nation differ only in organizational practices.

Weber et al. (1996) also found that in international and domestic mergers and acquisitions, national and organizational cultures are separate constructs with variable attitudinal and behavioural correlates.

Newman and Nollen (1996) reported that work units perform better when their management practices are compatible with the national culture. They advocate that management practices should be adapted to the national culture for high performance. Variables describing the national culture are highly significant in explaining the variance in adoption decisions in addition to the traditional micro and meso variables. These findings support the proposition that cultural differences between countries, even within the EU, are still so large that they impact the likelihood of adoption by companies operating in different countries (Waarts and Van Everdingen, 2006).

Organizations are, in many ways, embedded in the society in which they exist, and therefore, research on cultural differences should examine both national and organizational cultures.

The conclusion from this study is that the types of Organizational culture – clan, market, hierarchy and adhocracy – predict the individual level factors – job satisfaction, meaning of work and attitude towards the firm and the organizational level factors – powerfulness of the firm in competition with rivals, the behaviour of the management and company policy.

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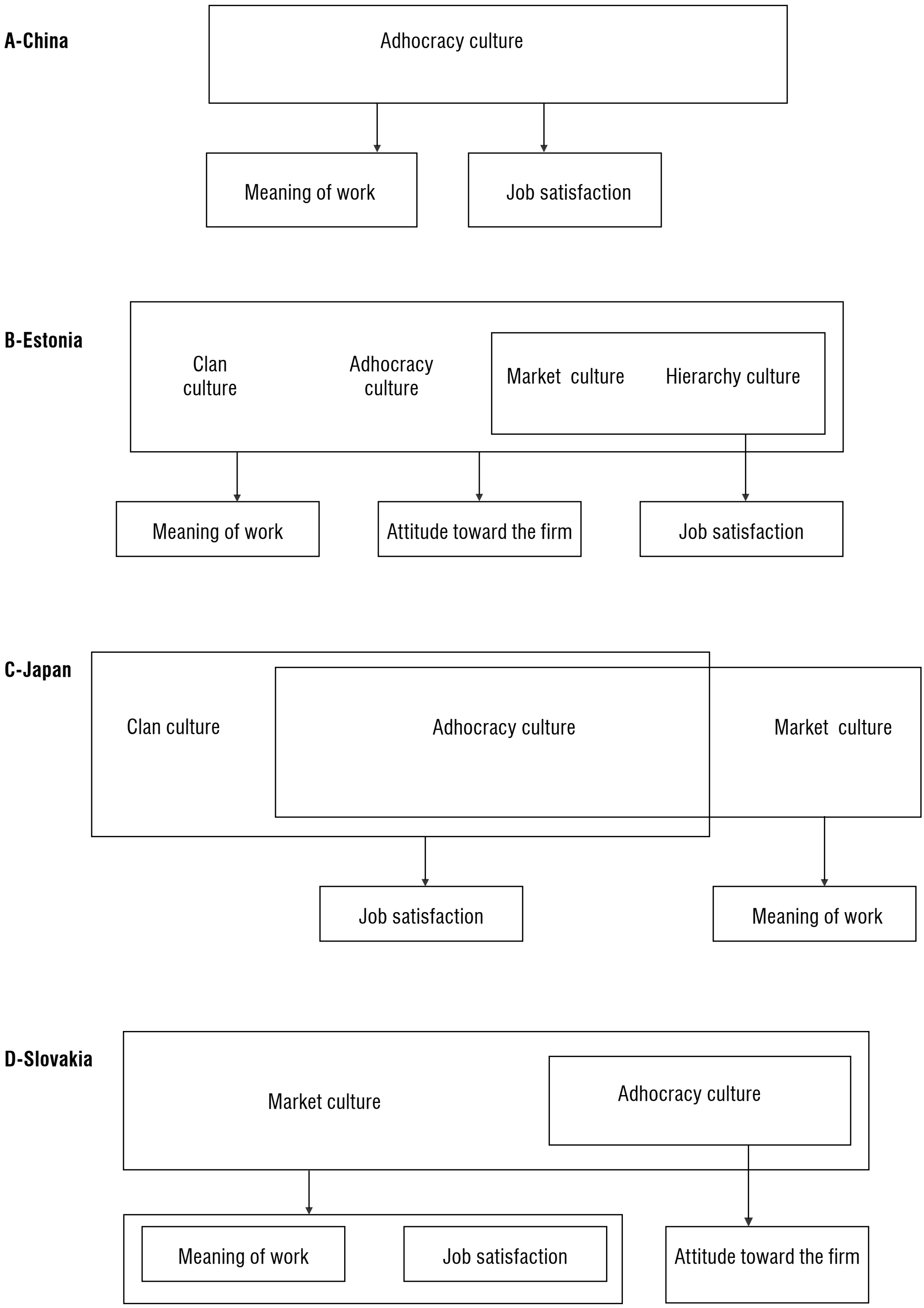
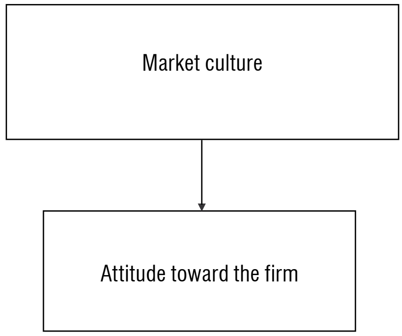
APPENDICES

Appendix 1.

Figure 1. How Organizational culture predicts individual level factors in Chinese, Estonian, Japanese, Slovakian, Russian and Czech enterprises



E-Russia



F-Czech

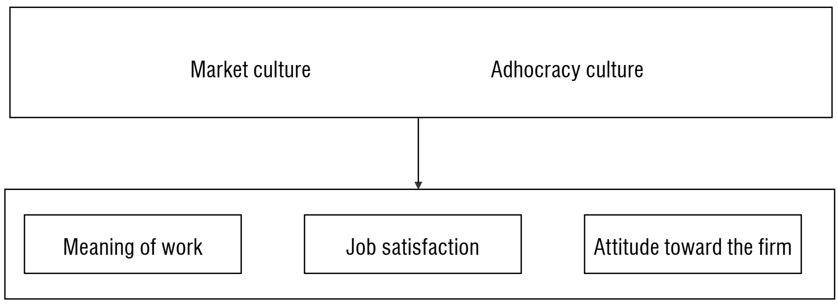
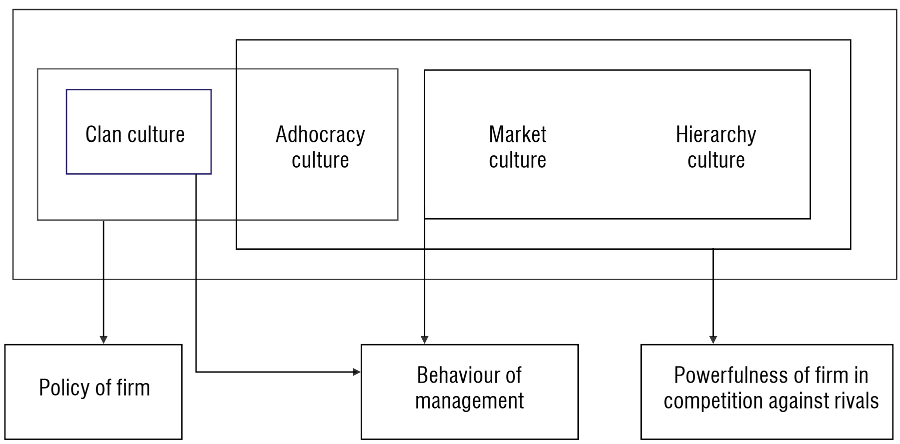
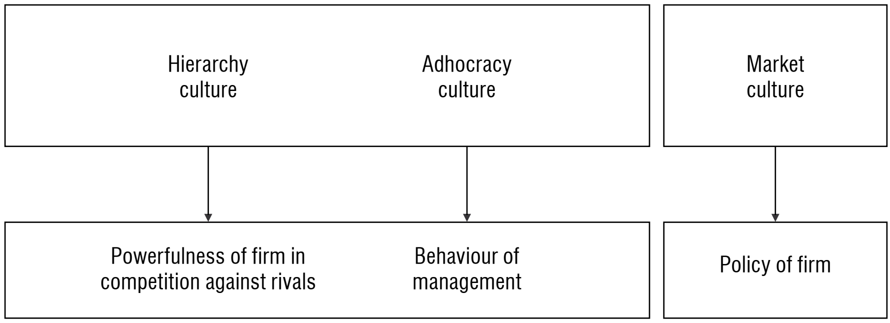


Figure 2. How Organizational culture predicts Organizational level factors in Estonian, Japanese, Slovakian, Russian and Czech enterprises

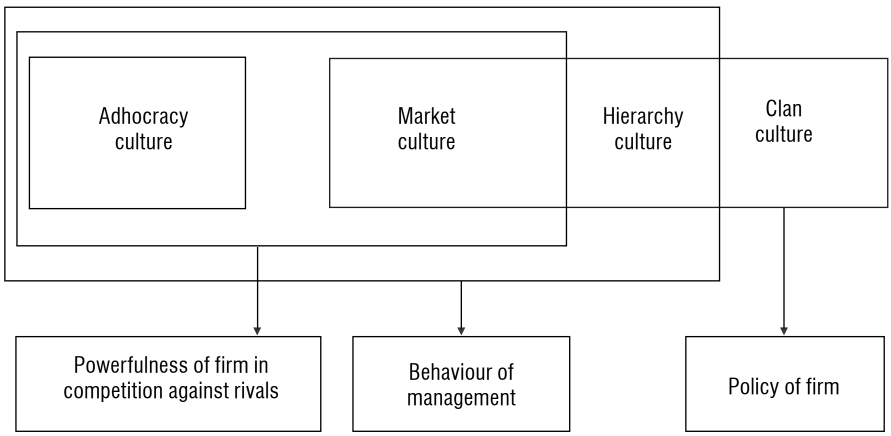
A-Estonia



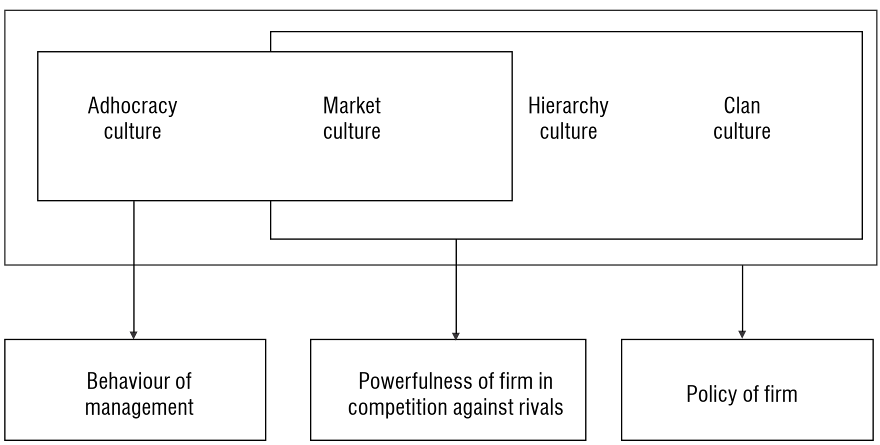
B-Japan



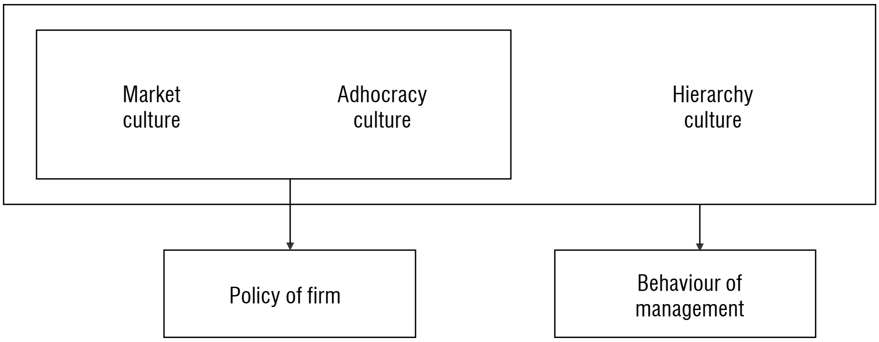
C-Slovak



D-Russia



E-Czech



Appendix 2. Questionnaire about individual and Organizational level factors

Job satisfaction					
Are you satisfied with following working conditions?	**Dissatisfied**		**More or less**		**Satisfied**
a. Self-actualization of your ability at work	1	2	3	4	5
b. Range of your competence at work	1	2	3	4	5
c. Labor conditions (e.g. light, heating, noise)	1	2	3	4	5
d. Trust between workers and management	1	2	3	4	5
e. Work load	1	2	3	4	5
f. Length of working time	1	2	3	4	5
g. Payments and bonuses	1	2	3	4	5
h. Competence of management	1	2	3	4	5
i. Promotion possibilities	1	2	3	4	5
j. Training and retraining	1	2	3	4	5
k. Security of employment	1	2	3	4	5
l. Equal opportunities for men and women	1	2	3	4	5
m. Welfare provisions in the firm	1	2	3	4	5
n. Interaction with your boss	1	2	3	4	5
o. Interaction with your colleagues	1	2	3	4	5
p. Access to information about organisation	1	2	3	4	5

Meaning of work					
What do you think about the meaning of work?	**Entirely disagree**		**More or less**		**Satisfied**
a. Work gives you status and prestige	1	2	3	4	5
b. Work provides you with income that is needed	1	2	3	4	5
c. Work keeps you absorbed in and excited	1	2	3	4	5
d. Work provides you with social contact with other people	1	2	3	4	5
e. Work is a way for you to serve for society	1	2	3	4	5
f. Work is in itself interesting	1	2	3	4	5

Attitude toward the firm					
How do you think of your attitudes toward the firm?	**Disagree**		**Unsure**		**Agree**
a. I always have ideas that can be approved by management	1	2	3	4	5
b. I would like to take part in company's decision making, because I think my opinion is important	1	2	3	4	5
c. I could take managerial position is situation demanded it	1	2	3	4	5
d. I am ready to take risk if it is approved	1	2	3	4	5
e. It is normal to sacrifice something for organisation's sake	1	2	3	4	5
f. Sometimes I feel myself a screw in a large machine	1	2	3	4	5

Powerfulness of firm in competition against rivals					
How much do you think your firm is powerful in competition against rivals concerning different aspects below raised?	**Powerless at all**		**Unsure**		**Powerful enough**
a. Image of the firm	1	2	3	4	5
b. Quality of products and service	1	2	3	4	5
c. Cost	1	2	3	4	5
d. Brand	1	2	3	4	5
e. Technology	1	2	3	4	5
f. Marketing	1	2	3	4	5
g. Scale merit	1	2	3	4	5
h. Aftercare service	1	2	3	4	5
i. Quality of human resources	1	2	3	4	5
j. Capability of Top management	1	2	3	4	5

Behaviour of management					
As for the behaviour of management, do you agree the following views?	**Disagree**		**Unsure**		**Agree**
a. If management promised something, than it will do what promised	1	2	3	4	5
b. Management is sure that it controls activity of all departments	1	2	3	4	5
c. Leaders of organisation have long term goals	1	2	3	4	5
d. Management puts clear goals for workers	1	2	3	4	5
e. Leaders and managers follow principles they set for the organisation	1	2	3	4	5
f. There is a clear set of principles that are followed by organisation in it's activity	1	2	3	4	5

Policy of firm					
How do you perceive policy of your firm ?	**Disagree**		**Unsure**		**Agree**
a. Management is apt to be behind the time for reacting to changing market	1	2	3	4	5
b. We always try to overcome our rivals	1	2	3	4	5
c. If market demands it, our organisation can quickly restructure	1	2	3	4	5
d. Goals of organisation are clearly set on all organisation's levels	1	2	3	4	5
e. In some situations instructions and regulations are obstacles to effective work	1	2	3	4	5
f. it is possible to be a good manager even not knowing answers to all questions of subordinates	1	2	3	4	5
g. In some cases one worker is under two managers	1	2	3	4	5
h. Every process of work is governed in detail by instructions and rules	1	2	3	4	5
i. The order of organisation is not hierarchically structured rigidly	1	2	3	4	5
j. Employees qualification is considered to be a very important source of competitive domination	1	2	3	4	5
k. Resources including human resources are not allocated properly nor integrated totally	1	2	3	4	5
l. Reward for success does not go to the department although everyone put an effort	1	2	3	4	5
m. We realize our input into society and feel our importance	1	2	3	4	5

Appendix 3. Questionnaire about four culture types – clan, market, hierarchy and adhocracy

Clan					
	Disagree		**Unsure**		**Agree**
a. Agreement is easily achieved even concerning hard problems in organisation	1	2	3	4	5
b. Competition between colleagues usually brings more harm than use	1	2	3	4	5
c. It is not accepted to talk about people behind their back	1	2	3	4	5
d. In group everyone must put maximum effort to achieve common goal	1	2	3	4	5
e. Reward for success must go to department, because everyone put an effort	1	2	3	4	5

Market					
	Disagree		Unsure		Agree
a. Customers' interests are often ignored in decision making of organisation	1	2	3	4	5
b. We constantly improve our methods of work to gain advantages over rivals	1	2	3	4	5
c. During conflict everybody tries to solve it quickly and mutually profitable	1	2	3	4	5
d. It is very important to feel market changes to react contemporarily	1	2	3	4	5

Hierarchy					
	Disagree		Unsure		Agree
a. We have informal norms and rules which are to be followed by everyone	1	2	3	4	5
b. Rules of the company must not be disobeyed even if employee thinks that he acts in favour of company	1	2	3	4	5
c. Instructions and regulations are needed to govern every process of work	1	2	3	4	5
d. Organisation must have strict hierarchy	1	2	3	4	5
e. One needs to control spending of resources strictly, or total disorder will happen	1	2	3	4	5

Adhocracy					
	Disagree		Unsure		Agree
a. Workers of any division have equal perspectives	1	2	3	4	5
b. Information is available for everyone. One can get any needed information	1	2	3	4	5
c. Projects are coordinated easily through all functional units	1	2	3	4	5
d. New ideas must be applied immediately otherwise they become old and obsolete	1	2	3	4	5
e. Most competent representative of group must make decisions even if formally he is not a leader of the group	1	2	3	4	5

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Conflict Management Modes and Leadership Styles Used by Estonian Managers and Specialists[1]

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Abstract

The purpose of this paper is to find out the modes of conflict management and the leadership styles among managers and specialists in Estonian organizations, depending on their socio-demographic characteristics using Thomas-Kilmann's Conflict Mode Instrument and Fiedler's Leadership Style measure. In order to achieve that, a survey of 345 Estonian leaders and specialists from different organizations was carried out.

Effective management, the balanced use of different leadership styles and the ability to act according to the situation are key elements for the success of an organization. We discovered that in most cases individual characteristics have an impact on the instruments analyzed, for example: younger managers are more task-oriented, while older managers are typically relationship-oriented and avoid conflicts, women are more collaborative and avoid conflicts less and men tend to use the accommodating mode more than women. Rather surprisingly, according to our survey, women appear to be more competitive than men. The relationships between conflict management mode and leadership style were also assessed and this revealed that task-oriented managers and specialists tend to use the competing mode more than relationship-oriented employees.

When making generalizations on the basis of the current analysis, it must be noted that the sample does not represent the average Estonian manager or specialist. In order to make generalizations we need to do more research – more accurate and in depth analysis of the relationships between conflict management modes and leadership styles needs to be carried out.

Keywords: Conflict Management Mode, Conflict Mode Instrument (CMI), Leadership styles (LS), Least Preferred Co-worker Test.

Introduction

Conflict is a fact of life, in organizations just as everywhere else, as people compete for jobs, resources, power, acknowledgement and security. This has become an inevitable part of life and it is crucial to know how to cope with conflict. The more people we communicate with, the more different and varied opinions we experience. This may lead to tension and a lower ability to work. That is why managers need to pay more attention to conflict management as it leads to better solutions in achieving company goals. Communication and collaboration are two key terms in today's working environment. Conflict is not a temporary situation, it will not disappear as stress at work decreases – conflicts are an inevitable part of an organiza-

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tion (Nugent, 2002; Withers and Winski, 2007; Littlejohn and Domenici, 2007: 179-180; Runde and Flanagan, 2007: 26-28).

Previous research indicates that managers spend roughly 20% of their time dealing with conflicts (Appelbaum *et al.,* 1999: 64; Lippitt, 1982: 67). This is one of the reasons why sociologists and economists devote so much time to research into conflict. Conflict management is closely related to leadership style (LS) and both depend on personality and the surrounding environment. LS is defined as the way managers choose to achieve a specific task or goal by influencing their employees. LS depends on socio-demographic indicators such as the type of work, position within an organization and the employee's individual personal traits (Omeltchenka and Armitage, 2006) and cultural background (Rodriguez, 2005).

When managing conflicts it is advisable to use all five conflict management modes and a balanced use of cooperation and competition. Adam Brandenburger and Barry Nalebuff (1996) define *co-opetition* in their book *Co-opetition*, as a new combined term for cooperation and competition. The idea behind the term is that areas where cooperation and competition are used will be defined by competitive organizations and/or persons (Gnyawali, He, Madhavan, 2006).

In our research we employ a dataset from managers and specialists in different Estonian organizations and institutions, and we analyze the results depending on their gender, age, position and the size and type of organization. We employ Thomas-Kilmann's and Fiedler's theories and their standard tests, which are still highly regarded in the field of management literature (Ma *et al.,* 2008; Thomas *et al.,* 2008).

This paper is structured as follows: in the next section we give a brief overview of the conflict management and leadership literature and describe Thomas-Kilmann's CMI (Thomas and Kilmann, 1974) and Fiedler's LS (Fiedler, 1967; Hayes, 1977; Cole, 1993); the third section discusses the data and measurement issues and presents the results; the last section is devoted to the discussion and conclusions.

Theoretical Background

Conflict Management and Thomas-Kilmann's Conflict Mode Instrument

Conflict management is one of the central components of management theories. Putnam and Poole (1987: 552) for instance define conflict as "the interaction of interdependent people who receive the opposition of goal, aims, and or values, and who see the other party as potentially interfering with the realization of these goals (aims, or values)." There is a choice of how to handle conflict and it may occasionally be very hard to find an adequate solution, and this can cause ambivalent attitudes and stress (Bagshaw, 1998).

When managing conflict, it is essential to keep to a constructive level and avoid unnecessary emotions. In order to resolve conflicts constructively it is necessary to leave personal feelings aside and concentrate on finding possible solutions to the problem. Then it is possible to reduce the tension in the working environment and utilize the energy and the creativity of the employees in order to realize the company's aims. Redundant competition should be avoided and cooperation should be encouraged. Cooperation should be regarded as one of the most important principles as it is the key to successful relationships between people. Therefore, managers should be aware of the importance of cooperation and the need for its constant development.

During the past decades, there has been a consensus that conflicts are an inevitable part of organizations. Hence research has focused on *conflict management* rather than on *conflict avoidance*. In doing so, managers are trying to recognize, acknowledge and manage conflicts in an appropriate manner; furthermore, conflict situations are used as opportunities to further develop the organization and its individuals (Darling and Walker, 2001: 230). Conflicts can help make necessary changes, and thus, help the organization to survive and improve (Cornelius and Faire, 1989). Some theorists even suggest provoking small conflicts as they are considered to be a prerequisite for an effective and strong organization (Robbins, 1994; Hellriegel *et al.,* 1995).

The dominant strategy that individuals use to handle conflicts is known as the *Conflict Management Mode* (CMM). Most conflict management theories try to identify the CMM in individuals and arrange them in a two-dimensional system, depending on their task- and relationship-orientation (de Vliert and Kabanoff, 1990).

One of the most popular models for studying behaviour in conflict situations still widely used in the world today is *Thomas-Kilmann's CMM Model* (Thomas *et al.,* 2008; Ding, 1996; de Vliert and Kabanoff, 1990; Thomas and Kilmann, 1974). This model was derived from Blake and Mouton's conceptual scheme employing problem solving, smoothing, forcing, withdrawal and sharing in the CMM (Blake and Mouton, 1964). The *Conflict Mode Instrument* (CMI) is used in order to identify the dominant CMM and to distinguish between the five modes. There are a number of analogous models with variations in the names of the modes, but these share the same principle (Lippitt, 1982; Rahim, 1983; Cornelius and Faire, 1989; Littlejohn and Domenici, 2007: 78-79).

According to the CMI (Lippitt, 1982: 70-71; Blake and Mouton, 1964; Thomas and Kilmann, 1974), the following five CMMs can be identified:

Competing – trying to achieve a goal at the other person's expense in a manner, which is both assertive and uncooperative. Competing is necessary in the case of crisis and where a quick decision is required and there is no time for long discussions.

Collaborating – confronting a conflict by considering all possible solutions. A satisfying outcome for both conflict parties will be found. The parties concentrate on similar interests rather than different opinions. Collaboration is one of the most effective and most used CMMs, but is not suitable in situations where a quick decision is needed.

Compromising – the objective is to find mutually acceptable solutions that partially satisfy both parties. Both parties are willing to give up something in order to get at least partially what they want (Rahim and Magner, 1995). Compromising people normally do not deny the problems, but at the same time they do not concentrate on them either. Using this mode, a win-win solution may be possible. Compromising is effective in situations where the goals are not so important or it is easy to give-up something that is not vital. Its use is also recommended when there is a lack of time and when collaborating is impossible.

Accommodating – the parties believe that their differences in views and values are resolvable. One party is ready to neglect its own needs and concentrates on the interests and views of the other party. It can take the form of selfless generosity or charity. By using the accommodating mode, chaos and a worsening of relations is avoided and harmony and social trust is created.

Avoiding – the parties try to put the conflict aside, ignore it and do not actively search for a solution. The conflict may cease to exist or a solution may be found later. Both parties are indifferent to their own and others' problems. Avoiding is suitable when the conflicts are too emotional and not important.

The choice of CMM depends on the situation; any of these modes could be useful under certain circumstances (McKenna and Richardson, 1995; McShane, 1998; Munduate *et al.,* 1999). There are numerous studies investigating the relationship between the preferred CMM on the one hand, and individual and organizational characteristics, such as gender, age, profession and ethnicity, on the other. A significant correlation can be found between gender, age, position and CMM. The results of the literature show that women prefer more accommodative CMMs (Thomas, 1977; Rosenthal and Hautaluoma, 1988; Smith *et al.,* 2000), and males on the other side prefer more confronting (Thomas, 1977; Rosenthal and Hautaluoma, 1988), aggressive (Kilmann and Thomas, 1977) and competitive CMMs (Thomas *et al.,* 2008; Rubin and Brown, 1975). Older employees tend to avoid conflicts (McKenna and Richardson, 1995; Brahnam *et al.,* 2005). At progressively higher organizational levels, assertiveness (competing and collaborating) increases monotonically. At the same time, unassertive styles (avoiding and accommodating) decrease. Compromising shows a curvilinear relationship to organizational level, decreasing at both the highest and lowest levels. Cultural background, traditional values and social norms can also play a significant role in the choice of the best approach to conflict resolution (McKenna and Richardson, 1995; Ding, 1996; Brahnam *et al.,* 2005).

Fiedler's Contingency Theory

Since the early 20th century, management literature has focused on the personality of leaders. A general consensus has evolved that although the personality has an important role in leadership, not all leaders have to share the same personal traits. A successful leader chooses from a set of individual abilities how to act according to the situation (Fiedler, 1967; Hayes, 1977; Hersey and Blanchard, 1993; Fiedler, 2005).

According to Fiedler's *Contingency Theory* (Fiedler, 1967, 2005), a leader's effectiveness is based on "situational contingency". This is seen as the result of the interaction of two factors, namely the *leadership style and situational favourableness*. Favourableness, or *situational control*, has three components: leader-member relations, task structure and leader position power. These determine the effectiveness of the leader. A *favourable situation* is said to exist when there is a good leader-to-member relation, a highly structured task and high leader position power. Fiedler found that task-oriented leaders perform best when the situation is extremely favourable or unfavourable, but that relationship-oriented leaders are more effective in situations with intermediate favourability.

For different levels of organizational hierarchy, leadership requirements are also likely to be different (Fiedler, 1967). Leaders may either prioritize the achievement of particular tasks over the relations within the team, or vice versa; but successful leaders are aware of their particular leadership styles and consciously choose the optimum style according to the situation's needs (Hayes, 1977; Ayman, 2002). The task- or relationship-orientation of a leader can be measured using Fiedler's *Least Preferred Co- worker Test* (LPC Test). The test has 18 bipolar choices (e.g. 1-unpleasant and 8-pleasant). On an eight-point Likert scale, the respondent has to describe the person he or she has worked the least well with. The responses to the scales are then added together. The higher a person's score, the higher his or her value on the scale and the larger the LPC score. According to Fiedlers theory, a high LPC score indicates that the employee is relationship-oriented and a low LPC score suggest that the person is task-oriented in a conflict situation (Likert, 1961; Fiedler, 1967; Greenberg and Baron, 1997; Becerra and Gupta, 2003; Kennedy and Gallo, 1986: 608). When interpreting the test results, it is important to consider the individual characteristics of the country and the culture.

Previous studies have indicated that the LPC score depends on age and position in an organization. Younger managers tend to be more task-orientated (Anderson and Blanchard, 1982; Omeltchenka and Armitage, 2006); older managers on the other hand are relationship-oriented and aim to provide a better and more supportive working environment. In addition, they are less competitive than younger managers. Gender alone seems to have no significant effect on the leadership style (Hofstede, 1991; Anderson and

McLenigan, 1987; Anderson and Blanchard, 1982; Nemeth *et al.,* 1976).

Data and Methods

The empirical analysis is based on a survey conducted between 2000 and 2005. A total of 345 (73%) valid responses were obtained, of which 57% were from female and 43% from male respondents. The sample consisted of 471 managers and specialists from different Estonian organizations who were participating in MBA level management courses. The results of our regression analysis indicate that several positions (e.g. top leader, middle level manager, director and head teacher of institutions) have similar results.

In order to present the results more clearly, we merge these positions into a single group named "managers". Similarly, lower level positions in organizations (e.g. various specialists) are grouped under the label "non-manager". The majority of the male respondents were managers with a ratio of 70% and the women were mostly non-managers. On average, the participants were 33 years old (*SD* 6.6), with the youngest being 22 and the oldest 51 years of age. The majority of the organizations (49%) were small and the average size of the organization (institution or private organization) was 268 (*SD* 36) employees. Small and large organizations show significant differences in their respective behaviour in our further analysis. Henceforth, we form two groups, small organizations with 50 or less employees, and large organizations with more than 50 employees. Seventy percent of the participants worked in private organizations.

Our questionnaire consisted of three parts respectively measuring CMM, LS and background variables.

- CMMs were measured using the Thomas-Kilmann's CMI (Thomas and Kilmann, 1974). This is considered to be one of the best and most widely used tools for measuring the five CMMs (Volkema and Bergman, 1995). The instrument contains 30 pairs of forced choice statements. The respondent has to identify one of the statements that is most characteristic to his or her behaviour in the case of a conflict. Thirty pairs of questions were asked in ten different combinations of CMMs. This means every combination of modes occurred three times. For example, the combination of avoiding and collaborating modes occurred three times. The maximum score of the modes describes the dominant tendency of using the mode in a conflict situation. It could also occur that one respondent prefers two modes and, depending on the situation, chooses one over the other.

- LS was measured using the Fiedler's Least Preferred Co-worker (LPC) test (Hayes, 1977). The respondents were asked to describe the person he or she has worked the least well with through an eight-point Likert scale, on a series of 18 bipolar scales. The responses to the scales were aggregated. The more positively the person was rated, the higher the score on the LPC scale. A high LPC score indicates that the person is more relationship-oriented in conflict situations than concerned with achieving the task. A lower LPC score, in contrast, indicates task-orientation. According to Fiedler, depending on the country where the LPC test is being used, the results must be adjusted to suit the country and cultural background. With our results, the controls for the lowest and highest LPC quartiles (below the LPC score 70 and above 89 respectively) are included. The two middle quartiles (LPC between 71 and 88) we considered to be middle-LPC where the respondent is equally task and relationship-oriented.

- In addition, socio-demographic questions were asked about gender, age, organizational level, type of organization, number of employees and number of subordinates.

The descriptive analysis included measures such as mean, mode, quartiles, percentages,

Table 1: Conflict Management Modes by gender and generally

	General		Female (N=196)		Male (N=144)	
	Average	*SD*	*Average*	*SD*	*Average*	*SD*
Competing	4.94	2.67	5.02	2.76	4.89	2.55
Collaborating	6.63	2.05	6.88	2.10	6.27	1.93
Compromising	7.97	1.97	7.91	1.95	8.06	2.01
Avoiding	4.33	2.33	4.14	2.31	4.59	2.35
Accommodating	5.94	2.13	5.81	2.14	6.12	2.12

standard deviations and several regression analyses. A CMM was identified by calculating the frequency count for each mode for each respondent. To define the LS for each respondent, the LPC score was calculated from the responses in the questionnaire.

Results

Conflict Management Mode

The general CMM scores for the respondents are described in Table 1 with an average and a standard deviation (*SD*). Within this study, the most frequent mode chosen in conflict management was compromising (144 respondents from 341, 42.2%). Tendency to avoid a conflict was the least frequent mode. It is also noted that 11.7% of the respondents were found to have two and 2% had three equally dominant modes in conflict management with different combinations.

Table 1 also depicts the average CMM scores by gender. The most interesting and surprising result was that Estonian women tend to use the competing mode more than Estonian men. It can also be seen that men tend to use the avoiding mode more than women. The results of the Thomas-Kilmann regression analysis are shown in Table 2.

The regression analysis confirmed that Estonian women tend to use the **competing mode** more than men (r = 0.66; p = 0.1). The position in an organization also plays a significant part in the use of the competing mode. The results show that the higher the persons position, the greater the tendency to use the competing mode in conflict situations. When adding the gender and position cross effect to the regression analysis, the difference in female managers' behaviour is revealed. Male non-managers tended to use the competing mode significantly less than female managers (r = –1.54; p = 0.05).

As seen in Table 1, Estonian women are more **collaborative** than men, Table 2 confirms this with a coefficient of 0.77 and a significance of p = 0.05. Looking at gender and collaboration with position, significant differences occurred between female and male managers. Female managers tended to use the collaborating mode in conflict situations significantly more than male managers (r = 1.03; p = 0.01). Male managers and male non-managers did not have significant differences in their tendency to use collaboration. In the collaborating mode, significance appeared when the cross effect of gender and organizational size was added to the model. Women in small organizations tended to use the collaborating mode significantly more than men in small organizations (r = 0.91; p = 0.5). The impact of the age and gender cross effect on the tendency to use collaborating can also be seen. Table 2 also shows that younger women tend to use the collaborating mode significantly more than older Estonian men (r = 1.04; p = 0.05).

The most widely used conflict management mode was the compromising mode. Both Estonian women and men tend to use it the most. The regression analysis did not reveal any significant differences in the compromising mode

Table 2: The results of Thomas-Kilmann's regression analysis

	Competing		Collaborating		Compromising		Avoiding		Accommodating	
	Coef.	*SD*	*Coef.*	*SD*	*Coef.*	*SD*	*Coef.*	*SD*	*Coef.*	*SD*
Constant	4.23	0.73***	5.58	0.55***	8.36	0.54***	5.90	0.63***	6.58	0.58***
Gender (Female) [1]	0.66	0.40.	0.77	0.30 *	-0.40	0.29	-0.64	0.34.	-0.71	0.31 *
Age (Younger) [1]	0.31	0.41	0.40	0.31	-0.04	0.31	-1.12	0.36 **	0.02	0.33
Position (Manager) [1]	0.84	0.40 *	0.17	0.30	-0.01	0.30	-0.50	0.35	-0.52	0.32
Org type (Private) [1]	0.35	0.43	0.30	0.32	-0.32	0.32	-0.19	0.37	-0.47	0.34
Org size (Small) [1]	0.49	0.37	0.24	0.28	0.13	0.27	-0.77	0.32 *	-0.31	0.30
Manager & gender (Female manager)										
Female non-manager	-0.77	0.49	-0.43	0.36	0.08	0.36	0.48	0.42	0.47	0.38
Male manager	-0.73	0.51	-1.03	0.38 **	0.48	0.37	0.59	0.44	0.76	0.40.
Male non-manager	-1.54	0.67 *	-0.83	0.50.	0.38	0.49	1.23	0.57 *	1.11	0.53 *
Age & gender (Young female)										
Young male	-0.03	0.65	-0.59	0.48	0.44	0.47	0.61	0.55	0.31	0.50
Older female	0.33	0.51	-0.27	0.38	0.06	0.37	1.00	0.43 *	-0.40	0.40
Older male	-0.45	0.57	-1.04	0.42 *	0.44	0.42	1.44	0.49 **	0.36	0.45
Age & org size (Older employees in smaller organizations)										
Older & large org	0.62	0.45	0.15	0.34	0.21	0.33	-0.42	0.38	-0.50	0.35
Younger & small org	0.39	0.55	0.24	0.41	0.08	0.40	-0.51	0.47	-0.18	0.43
Younger & large org	0.17	0.58	0.59	0.43	0.06	0.42	-1.78	0.49***	0.12	0.45
Gender & org size (Female in smaller organizations)										
Male & small org	-0.02	0.54	-0.91	0.4 *	0.56	0.39	0.14	0.45	0.24	0.42
Female & large org	0.74	0.47	0.06	0.35	0.20	0.35	-0.99	0.40 *	-0.52	0.37
Male & large org	-0.29	0.55	-0.45	0.41	0.50	0.40	-0.12	0.47	0.45	0.43

Signif. codes: '***' 0.001, '**' 0.01, '*' 0.05, '.' 0.1   [1] excluded when cross effects include this variable usage in relation to age, gender, position or the size of the organization. Instead, the regression analysis highlighted several significant impacts on the use of the avoiding mode in conflict situations.

The average frequency of avoiding among females was 4.14 and among males 4.59 (Table 1). According to the regression analysis (Table 2), women were significantly less conflict avoiding than men (*r* = –0.64; *p* = 0.1). In order to clarify the difference between gender and the avoiding mode, age was taken into account. When analyzing the impact of age on the avoiding mode, it appeared that older respondents tended to avoid conflicts significantly more than younger ones (*r* = 1.12; *p* = 0.01). It was also revealed that younger women (up to 30 years of age) had a significantly lower tendency for avoiding in conflict situations than older women (over 30 years of age) (*r* = –1.00; *p* = 0.05). Older men tended to use the avoiding mode significantly more compared to younger women (*r* = 1.44; p = 0.01). Comparing younger men with younger women's behaviour, there seemed to be a significant difference in usage of the avoiding mode, as they tended to avoid conflicts more than younger women.

The size of an organization only played an important role in the avoiding CMM. The study highlighted that in small organizations (up to 50 employees) the avoiding mode was used significantly less than in large organizations (*r* = –0.77; *p* = 0.05). Women in small organizations tended to use the avoiding mode significantly more than women in large organizations (*r* = 0.99; *p* = 0.05). Looking at the impact of age on the size of an organization and the avoiding mode, some significant results were revealed. The regression analysis highlighted that younger employees from large organizations tend to use the avoiding mode significantly less than older employees from small organizations (*r* = –1.78; *p* = 0.01).

Table 1 indicates average usage of the accommodating mode in both Estonian men and women. The regression analysis highlighted the importance of gender in the use of the accommodating mode in conflict situations. It revealed that women were significantly less accommodating than men (*r* = 0.71; *p* = 0.05). The cross effect of gender and position showed that male managers tend to use the **accommodating** mode significantly more than female managers (*r* = 0.76; *p* = 0.1) and male non-managers (*r* = 1.11; *p* = 0.05).

In addition, a brief analysis of the relationship between the conflict management modes and leadership styles was carried out. The analysis revealed that managers and specialists with low LPC scores tend to use the competing mode more than employees with medium and high LPC scores. Relationship-oriented respondents who tend to use the accommodating mode as their dominant CMM have higher LPC scores than the respondents who are task-oriented.

Leadership style (LS)

The LPC scores for most of the respondents were evenly spread around the average score (79.5, *SD* = 14.93). The results of Fiedler's LPC test regression analysis are shown in Table 3. Looking closer at the results in relation to gender, the LPC score for the female respondents was lower than the male score, but only just (Table 3).

Table 3: The results of Fiedler's LPC test regression analysis

	Coef.	*SD*
Constant	77.09	12.85 ***
Gender (Female)	-2.41	2.30
Age (Younger)	-5.70	2.41 *
Position (Manager)	-4.14	2.30
Org size (Large)	-0.60	2.14
Org type (Private)	4.43	2.44
Signif. codes: '***' 0.001, '**' 0.01, '*' 0.05, '.' 0.1		

The most important result of Fiedler's test regression analysis was the impact of age on the LPC score. The average LPC score of the younger respondents was significantly lower than that of older respondents (*r* = –5.70; *p* = 0.05). The importance of position in an organization was also analyzed. The LPC score of Estonian managers was significantly lower than the LPC score for non-managers (*r* = –4.14; *p* = 0.1). Younger managers and younger non-managers had lower LPC scores than older managers. Also, older non-managers had significantly higher LPC scores than other respondents (*r* = 1.2; *p* = 0.01).

The importance of the size of an organization was not significant, but there was tendency for the female LPC median value to be lower in large organizations. Also, the managers of large organizations proved to have lower LPC scores than those working in small organizations. In addition, managers of large organizations also have significantly lower scores than non-managers of small organizations. The type of organization has an insignificant influence on LPC scores. The regression analysis revealed that employees from private organizations have higher LPC scores than employees from institutions (*r* = 4.43; *p* = 0.1).

Discussion and Conclusions

The present study assessed the impact of individual characteristics on Thomas Kilmann Conflict Management Modes and Fiedler's Leadership Style measures. The study discovered that Estonian managers and specialists were more relationship-oriented than employees from other countries. This conclusion was proved by their slightly higher average LPC scores.

The main finding of this study is that there are some factors that influence employee behaviour in conflict situations. The current study also found several results that contradicted existing literature. Previous studies, for example, (Nemeth *et al.,* 1976; McKenna and Richardson, 1995; Brahnam *et al.,* 2005) have concluded that gender does not play a role in the use of competing, accommodating or compromising modes. However, the results of our study showed that this was not so clear. Our study revealed that whereas gender does not play a great role in the use of the compromising mode, significant differences were discovered in accommodating and competing between men and women. Contrary to Thomas et al. (2008), Brahnam et al. (2005) and Rosenthal and Hautaluoma (1988), we found that women used the competing mode more often than men.

Our study also confirmed that in conflict situations, men tend to use the accommodating mode more often than women. We believe that these differences may be caused by different cultural and historical backgrounds, as the Estonian people have been living on the coast of the Baltic Sea and the Estonian national culture has been influenced by both, the West and the East. This twofold geopolitical dimension has had a significant influence on the culture, entrepreneurship and the management of enterprises in Estonia. According to research, Estonians are more collectivistic in their nature, especially in their family relations, than people of Anglo-Saxon countries (Vadi, Allik, Realo, 2002; Realo, Allik, Vadi, 1997).

According to Rosenthal and Hautaluoma (1988), employees in higher positions tend to use collaboration as their dominant CMM, and their least favourite is the compromising mode. Several recent studies indicate that the use of competing and collaboration modes increased steadily at higher organizational levels whereas the use of avoiding and accommodating modes decreased (Thomas *et al.,* 2008). The results of recent studies showed that employees in leading positions tended to use the competing mode as their dominant CMM. Therefore, not surprisingly, managers tended to use the competing mode significantly more often than non-managers. It is important to note that type of organization can have a significant influence when choosing the CMM. For example, our results showed a clear correlation between large organizations and the use of the avoiding mode in a conflict situation – the larger the organization, the more managers try to avoid conflicts.

Our study revealed that female managers and non-managers tend to avoid conflict less than male managers and non-managers. These conclusions are in line with other research (Rubin and Brown, 1975; Haferkamp, 1991; Brahnam *et al.,* 2005; Holt and DeVore, 2005). This occurrence may be caused by the belief that dealing with the conflicts and finding the best solution for both sides can be more profitable than just avoiding them.

When analyzing the relationship between the size of an organization and the use of the avoiding mode, our studies revealed that younger employees in large organizations tend to use the avoiding mode significantly less than older employees. However, this finding might be affected by the relatively higher proportion of younger employees in large organizations. When examining gender and size of organization side by side, we were able to conclude that women in large organizations try to solve conflicts instead of avoiding them. At the same time men who worked in small organizations tended to use the collaborating mode markedly less than women.

Additional analysis revealed a relationship between conflict management modes and leadership styles. Managers and specialists with low LPC scores tend to use the competing mode more than relationship-oriented employees with high LPC scores. However, it is important to carry out more accurate and in depth analysis in this area.

When comparing the results of the **LPC** test with other countries, we found that the LPC score for Estonian managers and specialists was slightly higher than the LPC score in other countries. This finding suggests that managers and specialists in Estonia are more relationship-oriented, which could be, for example, due to our specific cultural background. There were no significant differences between the LPC scores of male and female respondents. The average female LPC score was only fractionally lower than the average male score.

In keeping with other studies, this paper shows that age and position in an organization have an important impact on leadership style and that gender alone has no significant effect on it. For example, younger managers in Estonia are more task-oriented and do not consider good relations to be as important in achieving goals as older managers. The study found that younger employees are markedly more task-oriented and older non-managers have significantly higher LPC scores. This indicates that as an employee gets older, he/she becomes increasingly more relationship-oriented. In addition, the size of an organization has a slight impact on the LPC score. It seems that larger organizations attract employees who are more task-oriented and small organizations have employees who are more relationship-oriented. The reason for this could be due to the large number of employees in large organizations who do not know each other, so it is easier to concentrate on the task. Our results show that the smaller the organization, the more important the relationships between employees and thus the managers pay more attention to communication and the working environment.

The present study also showed that non-managers were more relationship-oriented and managers more task-oriented. This claim was supported by non-managers having higher LPC scores than managers.

Several results in our study corresponded with the results stated in the literature. We would like to point out that we used a relatively large sample and consider this as one of the strengths of the study compared with previous studies. However, as the sample was not random it would be erroneous to make fundamental generalizations from the current analysis. It is clear that more research is needed in order to do that and we need to use samples from various organizations and include employees from all organizational levels.

Balancing interests and goals in the organization is one of the fundamental basics in leadership. The parallel handling of conflict management modes and leadership styles enables us to provide a complex overview of changes in leadership and allows us to better understand the influence of cultural peculiarities on leadership in Estonian organizations. Balanced use of the cooperation, compromising, collaborating, avoiding and competing modes together with task- and relationship-orientation, as leadership styles, enables us to consider the goals and interests of the organization and the individual. According to our study, Estonian managers and specialists tend to use compromising, collaborating and accommodating modes the most.

It is helpful to know the tendency of CMM use as it helps draw conclusions about whether an individual will be successful in a particular situation. The LPC score on the other hand indicates whether the employee is more task-oriented (low LPC score) or relationship-oriented (high LPC score). It is also helpful for international organizations who want to start or want to increase enterprise efficiency in Estonia.

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Innovation Obstacles and Management Focus in Estonian Enterprises

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Abstract

This paper studies the focus of innovative activities. Obstacles in the innovation process and innovation performance management principles in Estonian enterprises are revealed by applying the Henley SME innovation study 2007 questionnaire. The Estonian survey involved 102 enterprises from 11 business sectors, but retailing, financial services and manufacturing industries dominated the sample. The main research question is: which high priority principles of innovation performance management and obstacles to innovation in Estonian enterprises differentiate the focus of the innovation when compared to more advanced European market economies? The conceptual basis of the paper links innovation to capabilities and development priorities in enterprises in an economic environment where the cost advantages of Estonian enterprises are decreasing and future competitive advantages in Europe depend on following innovation-driven strategic priorities. Financial service enterprises had the strongest product and service innovation outlook, while retailers focused more on reducing costs. Production enterprises were more interested in innovations for foreign markets. Innovation resourcing relies too much on internal expertise and makes limited use of networking opportunities. Estonian enterprises share many perceptions of innovation outcomes and innovation management with "old Europe", but the survey results indicate that a risk-adverse culture is not seen as a serious innovation obstacle, while a lack of co-ordination and a shortage of great ideas appear to be more serious challenges.

Keywords: Estonia, innovation, change management, obstacles to innovation, innovation management, survey

Introduction

Integration processes before and after joining the European Union have intensified the discourse on international competitiveness gaps in Estonia in the structure of industry and productivity of Estonian enterprises (Tiits *et al.,* 2003). The need to move towards knowledge-based innovative business activities has been highlighted among key economic development priorities (Kattel and Kalvet, 2006). GDP growth, which skyrocketed to 10.2% in 2005 and to 11.2% in 2006, declined to 7.1 in 2007 (Estonian Bank, 2008). In the first quarter of 2008, compared to the previous year, GDP growth decelerated steeply to 0.1%. Estonia's GDP growth in the first quarter of 2008 was the lowest among EU Member States (Statistics Estonia, 2008). The "hard landing" that followed the years of rapid

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economic growth has created pressure to re-assess the role of innovative activities in business development efforts that so far in many sectors have been driven by cheap labour as a source of competitive advantage for international sub-contracting or by high domestic demand fuelled by cheap loans.

The Estonian Development Fund has initiated discussions on the future of the Estonian economy and commissioned a report from a working group headed by Urmas Varblane (Estonian Development Fund, 2008) that assesses the current status of competitiveness and highlights possible development scenarios. This report looks at the active versus the passive role of the state and compares the relative ability of enterprises and people to change as the main aspects of future scenarios that may transform Estonia into a rapidly developing "Northern Star". It also assumes that smart active policies from state institutions match the ability of Estonian enterprises to change or lead the economy along a path of "Natural Selection". If the state follows a more passive role, co-operation opportunities will not be utilized and less adaptive enterprises will have to close their business.

Alternatively, an "Idling Speed" scenario may evolve if the ability of enterprises to change turns out to be low in the coming years despite more active innovative policy efforts. Under this scenario, the active efforts of the state would not match the initiative of enterprises and it will be ineffective. "Stagnant water" is the label for yet another scenario, where enterprises demonstrate a low ability to change and the state remains passive. Using evidence from 14 interviews and 25 expert opinions, the report also discussed the readiness of enterprises to change, pointing out that enterprises in economic sectors with high productivity have a higher readiness to improve their position in international value chains. An established role in the value chain and opportunities to increase productivity are indeed important departure points for understanding the behavioural patterns of enterprises.

In order to deepen this understanding, additional research on the management focus of innovative activities in Estonian enterprises, and on perceptions of obstacles in the innovation process is needed. In this paper we review the results of using the Henley SME innovation study 2007 questionnaire in 102 Estonian enterprises. We applied the survey tool developed by George Tovstiga and David Birchall at the Henley Management College in order to compare innovative activity priorities in Estonian enterprises with enterprises that operate in more advanced and stable market economies of the "old" Europe.

The next section of the paper discusses theoretical approaches that are essential for understanding the relationships between innovation, dynamic strategic capabilities, markets and change management in order to analyse innovative activities in a transition economy. The structure of the innovation study questionnaire is then presented. As the next step, Estonian survey results are compared with results of the survey conducted in the United Kingdom, also involving some enterprises from other EU member states from Western and Northern Europe. In order to deepen the analysis of the Estonian sample, comparisons between different business sectors and respondents that report higher or lower contributions from innovation to the profitability of their enterprise are presented. Correlation and cluster analyses were used to reveal relationships between input-, process- and outcome-related variables of innovative activities.

The survey results allow us to present some conclusions about the priorities of innovative activities and the relationship between innovation obstacles and outcomes in Estonian enterprises represented in the survey.

Innovation and Change Management Capabilities in the Transition Economy Context

In entrepreneurship literature the emergence of the innovation concept is often linked to the ideas of Joseph Schumpeter (1883-1950), the Austrian economist that stressed the crucial role of the "creative destruction" of the existing market structure by devising new technologies, introducing new products and developing new markets (Link and Siegel, 2007). Schumpeter (1928), in his classical work, has stressed the difference between invention and innovation, the latter requiring leadership. The innovative leader distances himself from the manager by virtue of his aptitude. Tidd et al. (2001) define innovation as a process of turning opportunity into new ideas and of putting these ideas broadly into practice. Malerba (2006) discusses intellectual property in the context of the struggle between innovative new firms and relatively conservative firms as industries evolve over time. In a transition economy innovation leadership in the Schumpeterian sense can be represented by new entrepreneurial firms. Such firms that tend to have a limited capital base can still choose to apply a more opportunist strategy by exploiting cheap production factors in order to achieve short-term profit gains.

Shane (2000) stresses that the prior knowledge of decision-makers modifies the perception of opportunities that could be developed from a specific technological basis. Holmén et al. (2007) conceptualize innovative opportunities as consisting of three elements: economic value, mobilization of resources and appropriability. This means a new combination of resources and market needs. Mobilization of resources is not limited to a focus on internal resources, but assumes linking strategic assets internal to the firm and strategic industry factors found in the business environment. Estonia is a small open economy where the business actors that try to appropriate the value generated from their new innovative solutions have to consider broader industry factors outside their small domestic market. Enterprises collaborating with research centres and universities has been found to increase the probability of introducing new products in some emerging markets (Morotta *et al.,* 2007). A comparison of the results from the EU Community Innovation Survey demonstrates that while the share of innovating enterprises is quite similar in such advanced market economies as Austria and Finland, the number of cooperating enterprises is considerably higher in Finland and cooperative behaviour of innovators depends on national factors (Dachs *et al.,* 2008). The science, technology and innovation mode, based on production and the use of codified scientific and technological knowledge has been contrasted with the doing, using and interacting innovation mode. Jensen et al. (2007) conclude from their Danish survey that firms combining these two innovation modes are more likely to innovate products and services than enterprises that apply only one mode. Finding the best ways to link learning by doing, customer-driven and research-based innovative ideas and their applications has also become an important challenge for enterprises in transition economies. It is essential to understand managerial cognitions (Chen and Miller, 2007) that guide their search for innovative opportunities and ways of overcoming obstacles in innovative activities.

The resource-based view of the firm (Barney, 1991; Wright *et al.,* 2001) has been instrumental in explaining differences in innovation activities among firms. Fiol (2001) has stressed that even unique capabilities cannot sustain a competitive advantage. Dynamic capabilities mean the ability to continuously reconfigure resources (Teece *et al.,* 1997). In addition to the firm's knowledge stock, its knowledge flows are also crucial for sustaining innovative performance (Jantunen, 2005).

The survey tool that has been used for collecting empirical data reported in this paper is designed for studying strategic capabilities and innovation in the continuously changing business environment and market context (Birchall and Tovstiga, 2005).

Innovative Capabilities and the Market

Innovation supports exports, especially in technology-intensive sectors (Lachenmaier and Wößmann, 2006). Some high-technology firms follow a global focus from the outset in their marketing efforts and have innovative products or services that can serve as the basis for rapid international sales growth. The main source of competitive advantage in such “born globals” is often related to their advanced knowledge base (Bell *et al.,* 2001). Enterprises that develop their products in a transition economy may lack financial resources and international credibility when offering their own new products for overseas markets even if they have access to new technological solutions. Radical Schumpeterian innovation for international markets may assume even more change management, networking and organizational learning capabilities from an enterprise in a transition country than from an enterprise in an advanced market economy.

Innovation that is fully dependent on the knowledge inside an enterprise faces the risk of incompatibility with market demand and a lack of resources from other stakeholders. In a rapidly changing and globalizing business environment, networking is a way to broaden the resource base for entrepreneurship. Participation in formal and informal entrepreneurial networks has been discussed as a factor of successful entrepreneurship since the last decades of the 20th century (Sweeney, 1987; Breschi and Malerba, 2005). Relational capital as the stock of relationships that enterprises entertain with other enterprises and institutions acts as a determinant of innovative activities (Capello, 2002).

Wang and Ahmed (2004) have developed the Organizational innovativeness construct by reviewing earlier research and specifying the following components: behavioural innovativeness, product innovativeness, process innovativeness, market innovativeness and strategic innovativeness. The European Excellence Model (EFQM) has been used to specify the enablers of innovation excellence in enterprises, such as leadership, innovativeness, people, strategies and plans, partnership and resources, innovation processes and customer orientation. Strategies and plans appeared to have an indirect effect on the innovation process through resources when testing such a conceptual model (Martensen *et al.,* 2007).

Market orientation means organization-wide generation, dissemination and responsiveness to market intelligence (Kohli and Jaworski, 1990). The development of market orientation is a logical implication of the transition to a market economy. The link between strong market orientation and innovation activity can be either negative or positive depending on the existing level of innovativeness in an enterprise (Verhees and Meulenberg, 2004). There are several studies that suggest an increased level of market orientation can lead to improvements in firm innovative performance (Low *et al.,* 2007), but it has also been found that strong market orientation reduces the chances of enterprises introducing innovations that require major behavioural changes on the part of potential customers (Atuahene-Gima, 1996). In the transition economy context it is not guaranteed that long-term technology-driven innovative product development can be aligned with short-term market pro-activeness.

Integrating technological, market and organizational change has been a key issue in innovation management literature (Van de Ven *et al.,* 1999; Tidd *et al.,* 2001). The innovator’s dilemma of incremental innovation for improving the existing business versus focusing on new business opportunities created by the emergence of new technologies and/or new markets (Christenson, 1997) has specific value in a transition economy. Transition from a closed command economy to a market economy that is open to global competition at the end of the 20th century meant radical transformational change for Estonian enterprises, where the organizational vision and strategy had to be aligned with the new institutions of the market economy (Alas, 2004). Values that support organizational learning appeared to be among the crucial success factors in Organizational change (Alas and Vadi, 2006).

Relatively rapid macro-economic stabilization at the beginning of the 90s, however, allowed many enterprises in Estonia to follow the cost leadership logic in the role of sub-contractors for business partners from Finland, Sweden, Germany and other "high-cost" countries. Many privatized enterprises and new entrepreneurial ventures that started exporting in the 90s were in fact simply found by foreign entrepreneurial business people who engaged them as subcontractors (Elenurm, 2000). That was different from the situation for enterprises initiated during this decade in advanced market economies. For instance, in the USA the use of cost leadership was not found to assist a venture in internationalizing its operations (Bloodgood, 2006). Developing new knowledge-intensive products and services that could be internationally competitive in the coming years assumes a strategically more advanced approach to product and process innovations than the last decade of the 20th century, when filling some empty market niches by importing foreign products or acting as a cheap sub-contractor dependent on the product ideas of a foreign partner were, for many Estonian entrepreneurs, profitable business models.

After joining the European Union in 2004, Estonian enterprises have had to develop their own vision of long-term competitiveness in the EU economic space. The innovation focus and enterprises management capabilities needed for successful innovation performance management depend on the choice between such strategic priorities as subcontracting efficiency, using diversified internationalization opportunities and establishing the enterprise as a member of an international value chain (Elenurm, 2007).
The EU Community Innovation Survey (CIS 4) collected comparative information about both product and process innovation and also non-technical innovations such as in the organization and the marketing during the period 2002 to 2004. Product or process innovations have been introduced by 49% of Estonian enterprises involved in the CIS 4 survey, whereas the EU-27 average was 42%. In the United Kingdom, 43% of enterprises were involved in innovation activity (Eurostat, 2007). A peculiarity of the Estonian CIS 4 results was that there were more innovative service enterprises (51%) than processing industry enterprises (48%) (Viia *et al.,* 2007).

Recent Estonian data about CIS 2006 results however, indicate that while the general level of innovative activity has changed only marginally, in 2006, 55% of industrial enterprises and 40% of service enterprises were qualified as innovative. The CIS 2006 survey is based on a large sample of 2185 production and 1839 service enterprises (Eesti Statistika, 2008), and was conducted as an obligatory statistical observation. The general results of the Estonian CIS surveys indicate a high intensity of innovative activity, although some bottlenecks, including low levels of co-operation between enterprises and universities and excessive investments in purchasing equipment compared to other innovation costs were revealed (Viia *et al.,* 2007). The survey, which is part of a compulsory statistical observation, has limitations however, from the point of view of understanding the internal capabilities and weaknesses of innovation management inside organizations.

In order to reveal the contradictions and challenges in innovative activities in enterprises, additional surveys are needed that highlight the strategic positioning of innovation and link the priorities of innovative activities to obstacles in the innovation process and innovation performance management tools.

Empirical Study

The survey tool and sample for the innovation study

The survey tool that was used for studying innovation activities in Estonian enterprises was originally developed by George Tovstiga and David Birchall at Henley Management College. The online version of the survey was introduced in summer 2007 for small and medium-sized enterprises in the United Kingdom, but it was also available for enterprises in other countries.

A conceptual basis of the survey is Henley-Incubator's innovation ecosystem framework that addresses innovation performance measurement in five broad areas: innovation climate, strategic filtering of innovative ideas, innovation project management, team effectiveness, innovation portfolio measurement and valuation (Birchall *et al.,* 2004). The questionnaire follows a resource-based view for studying the dynamic capabilities that are related to innovative activities, inputs and outcomes of innovations. The questionnaire focuses on the following categories of questions:

- How important is innovation for the competitive wellbeing of the enterprise? What is the strategic positioning of innovation?
- Where are they focusing their efforts on innovation? How important among the innovative activities are new product and services offerings for existing and new customers, offerings for overseas markets, innovations for reducing costs and innovations for better use of information and communication technology?
- What is the nature of innovation resourcing? How important are the internal expertise and the co-operation with research institutions, consultants and public development agencies?
- What are the most important obstacles to innovation?
- What are the innovation outcomes in the strategic context: differentiation, organizational learning, neutralization or waste of resources?
- What are the obstacles to innovation?
- How important are different innovation performance management principles?
- Who are the competitive benchmarks and innovation drivers for enterprises?

The Henley Management School 2007 innovation survey enterprise sample (HES) that we used to compare with the Estonian results involved 156 enterprises, 38% of them operating in the United Kingdom. The other enterprises were predominantly from advanced market economies in the European Union, mainly from Germany, Denmark and Sweden. Enterprises from the United Kingdom ranked innovation slightly higher in terms of their priorities than the average in the HES, but there were no significant differences concerning innovation outcome assessments between the UK and other EU countries in this sample (Tovstiga and Birchall, 2007).

Earlier research experience has demonstrated that Estonian enterprises are quite passive in completing online questionnaires, especially if it is not in their native language. In order to diminish the bias towards respondents of enterprises that volunteer to fill in the survey because of their good track record of international innovative activities, the questionnaire was translated into the Estonian language. Entrepreneurs and MBA students studying at the Estonian Business School were asked to fill in the survey about the enterprise they represent, or to interview a manager of an enterprise in the business sector with which they are most familiar. The Estonian survey was conducted at the end of 2007 and during the first months of 2008. The Henley Management School 2007 innovation survey is developed for cross-border use, so only minor adaptations for the Estonian context was needed. In the question about regional and government development agencies as innovation resources a relevant Estonian agency, Enterprise Estonia, was mentioned.

The Estonian sample consisted of 102 enterprises, mainly from retailing, processing industry, financial services and some other business sectors (Figure 1).

A total of 24.5% of enterprises in the Estonian sample had more than 250 employees and can be considered large enterprises; 18.6% of enterprises were medium-sized with 50 – 249 employees and 56.9% were small enterprises with less than 50 employees. Among the respondents, 40.6% were executives and top managers, 30.7% middle managers and 28.7% junior managers.

Comparing the results of Estonian business sectors involved in the survey demonstrates a positive approach to innovation among respondents in financial services. Fifty-six percent of

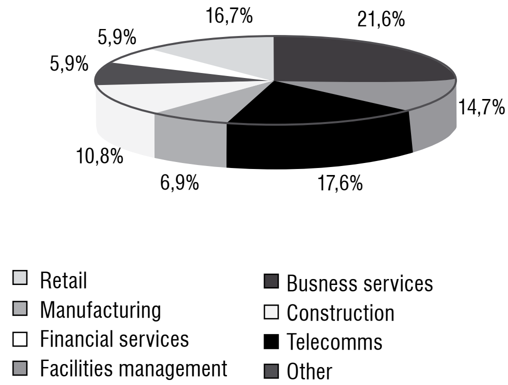

Figure 1: Business sectors involved to Estonian sample

representatives from this sector assessed that the contribution of innovation to the business profitability of their organizations in 2007 was very high or high. The number of respondents that were very satisfied with the financial return on their investment in innovation was, however, the highest among production companies (13.3%) and was a bit lower in financial services (11.1%) and the retail sector (9.1%). Innovating by introducing new products for new customers was rated as extremely important by 38.9% of financial service providers and by 36.4% of retailers, whereas only 26.7% of respondents from production enterprises gave such a rating.

The share of enterprises that rated offering new products to existing customers as extremely important was, however, the highest among production firms – 60.0%, whereas in the retail sector it was 36.4%, the same as the importance of new products for new customers, and in financial services 36.4%, slightly lower than the share of enterprises focusing on new products for new customers. Financial service enterprises also rated new services for existing customers extremely important (38.9%) and especially innovations for better use of communication and information technology (77.8%) and for improving existing products/services (61.1%). These results indicate the quite strong product and services innovation focus in the financial sector, where several large enterprises in the sample also come from.

The largest share of enterprises that rated reducing product/service costs as extremely important was found among retailers – 63.6%. Product/service offerings for overseas markets were rated extremely important by 66.7% of production enterprises whereas only 36.3% of the total sample considered this innovation focus extremely important. When assessing the latter rating, the open nature of the Estonian economy should be taken into consideration. In 2007, the share of exports in Estonian GDP was 79.8% (Statistics Estonia, 2007). Compared to the role of exports in the Estonian economy, innovation focus for exports is still low as many enterprises are focused on subcontracting and do not develop their own branded products.

Sixty percent of production enterprises and 54.5% of retailers consider relying entirely on internal expertise and capabilities very important when solving innovation problems. Engaging management consultants was seen as being very important by only 6.7% of production, 5.6% of financial and 4.5% of retail sector respondents. Engaging public research institutions was considered to be very important by 6.9% of all respondents. Among production firms, this type of partner in innovation activities was, however, rated as very important by 13.3% of firms.

Comparing Estonian results with the Henley SME Innovation Study 2007

Only 36% of respondents in the total sample of Estonian enterprises considered the contribution of innovation to the business profitability of their organisations in 2007 very high or high, whereas among enterprises in the Henley Management College enterprise sample (HES) such assessment was given by 44% of survey participants. Among enterprises in the Estonian sample, only 5% rank innovation as the top strategic priority whereas in the HES 21% of enterprises gave innovation the top rating. However, more than half of the enterprises in the Estonian sample consider innovation to be one of the top 3 strategic priorities. Both HES enterprises and

Estonian enterprises see innovation outcomes mainly in terms of differentiation in order to gain competitive advantage. HES enterprises expect 37% and Estonian enterprises 39% of their innovation yield through this outcome. Estonian enterprises point out a slightly higher impact on organizational learning (28%) than HES enterprises (24%) and less waste of innovation efforts (13%) than HES enterprises (21%). The share of competitors' first move neutralisation outcome – 20% in the Estonian and 21% in the HES sample – is practically equal. More significant differences can be found in the questionnaire results concerning innovation obstacles and innovation management.

Innovation Obstacles

When comparing innovation obstacles for Estonian and HSE enterprises, Estonian enterprises gave more optimistic assessments to the majority of obstacles. A risk-averse culture was especially rated as a greater obstacle by HES enterprises than Estonian enterprises. The shortage of great ideas, lack of access to new technology and lack of coordination are, however, seen as greater obstacles in Estonian enterprises than in enterprises in the HES sample (Figure 2).

Stressing the shortage of great ideas provides evidence of the desire to focus on more radical innovations. Lack of co-ordination, which was considered by Estonian enterprises as one of the most serious obstacles, may be explained by the emerging nature of product and process innovation management practices in many Estonian enterprises.

These priorities correspond to the perception of the need to overcome co-ordination obstacles.

A high priority given to developing an understanding of customer needs by Estonian respondents is, however, lower than the priority given to this management issue by enterprises in the HES sample. Estonian enterprises assign quite a low priority to leveraging suppliers for ideas when compared with HES, indicating their inexperience in the role of innovative value chain leaders.

The largest gap between importance and performance can be found both in Estonian and HES samples in the field of understanding customer needs and providing sufficient funds for projects. Encouraging experimentation with new ideas is also an innovation management field for Estonian enterprises, where performance does

Obstacles to innovation

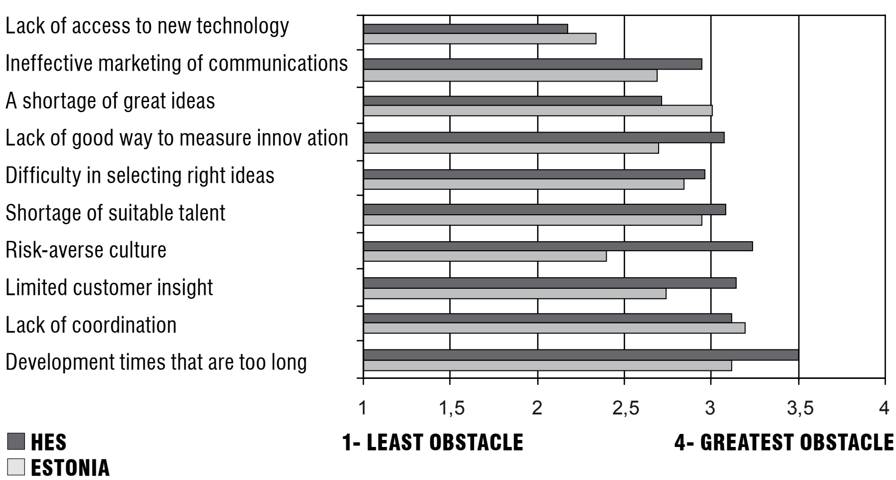

Figure 2: Obstacles to innovation in Estonia and the HES sample

not match priorities, while in the HES sample providing an innovative culture that regards honest failures is the third largest gap.

Clustering and Correlation Analysis

Clustering was applied using the nearest neighbour algorithm in the statistical package SPSS. Three significant clusters that have different combinations of innovation inputs, process features and outcomes were identified.

The first cluster includes many business and financial service enterprises, but also half the manufacturers and retailers. New products for new customers is a stronger innovation focus in the first cluster, and enterprises in this cluster anticipate a higher contribution of innovation to their business profitability than the other two clusters. Enterprises in this cluster are slightly more interested to engaging in co-operation with public research institutions and regional and governmental development agencies than enterprises in other clusters. Enterprises in all clusters however, consider relying entirely on their internal expertise and capability rather than engaging public research institutions or consulting firms to solve innovation problems most important. Enterprises of the first cluster rate such obstacles to innovation as limited customer insight, risk-adverse culture, shortage of suitable talent and a lack of access to new technology lower than the other two clusters. Their innovation management priorities focus on developing an understanding of customer needs, senior management team sponsorship of projects and having a clear innovation process for moving from idea generation to sales, but in absolute terms these ratings are lower than in the third cluster.

Eighteen enterprises in the second cluster have a diversified sectorial background. There are several retailers, but no facilities and business service operators in this cluster. Enterprises in the second cluster are most pessimistic when anticipating the contribution of innovation to their business profitability compared to enterprises in the first cluster, but slightly more pessimistic also compared to the third cluster. Ratings of obstacles to innovation among enterprises in the second cluster, position it between the first and the third cluster. Only the lack of a good way to measure innovation has the lowest obstacle rating in this cluster. At the same time, all innovation management issues are considered less important in the second cluster than in the first and in the third cluster.

Twenty-seven enterprises in the third cluster are mainly involved in manufacturing and retailing.

Innovation perfomance management - How important is the following to your company's innovation effort?

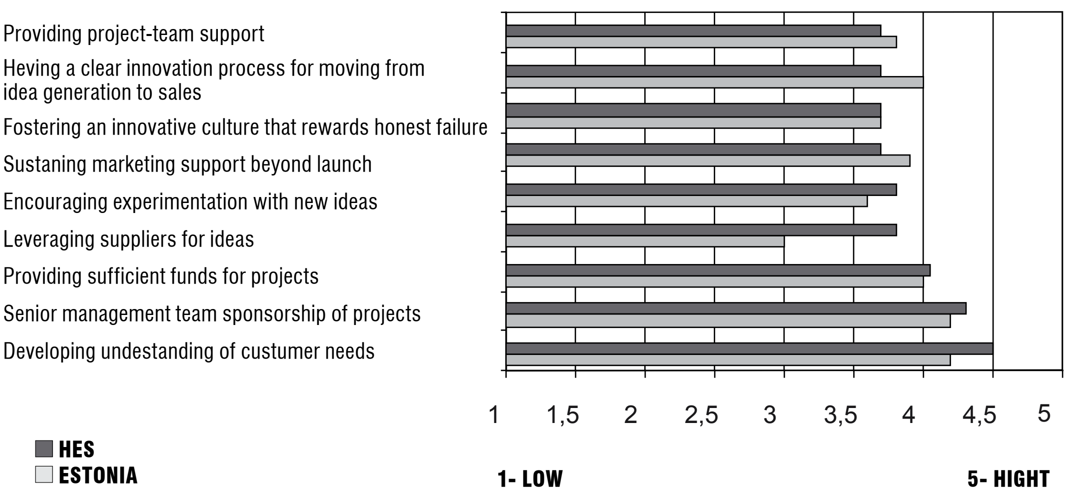

Figure 3: Importance of innovation management

In the third cluster, several obstacles to innovation, including risk-adverse culture, lack of coordination, shortage of suitable talent, limited customer insight and ineffective marketing of communications are substantially higher than in the other clusters. At the same time, encouraging innovation with new ideas, rewarding honest failure and balancing risks, time frames, and returns across the portfolio of innovation projects and measuring innovation performance also received highest priority in this cluster. The pattern of survey answers in the third cluster is most similar to the HES survey results.

The cluster analysis results do not allow us to assign clear "labels" to clusters that are quite diversified according to their business sector background. In the first cluster enterprises appear to be more satisfied with present innovation activities than in the other two clusters. The third cluster tends to represent a more critical managerial mindset that has identified serious obstacles to innovation and gives a high priority to innovation activities potentially supporting radical innovation in the next development stages of these organisations.

Table 1 highlights statistically significant correlations between some innovation input and process variables with the following outcome variables: profit growth trend in 2006, contribution of innovation to recent profitability in 2007 and anticipated profitability of the business for the next five years.

Profitability growth trend in 2006 in fact shows negative correlations with high rankings to such innovation management principles as balancing risk, time frames, returns across the portfolio of innovative projects, supporting marketing beyond new product launch and fostering an innovative culture that rewards honest failure.

An explanation for this could be that in 2006, when the Estonian economy was still enjoying double-digit GDP growth, most profitable enterprises among beneficiaries of this economic boom did not have any incentive to focus on balancing risks, rewarding failure or being worried about sustaining marketing support for products in a high demand environment. Experiencing easy profit making is not a driver for sustainable innovative thinking.

Significant positive correlations between high contributions of innovation to business profitability in 2007 were established both with the innovation focus of offering new services to existing customers and innovative profits/services offerings for overseas markets. Making better use of information and communication technology had an even stronger correlation with the contribution of innovation to business profitability.

It is logical that a positive correlation also exists between satisfaction with the financial return on investment to innovation and high contribution of innovation to profitability in 2007. The correlation of r=0.337 is, however, moderate indicating the potentially higher ambitions of some respondents.

Negative correlations between the contribution of innovation in 2007 and the shortage of great ideas and the shortage of suitable talent point to the strategic importance of human capital for enterprises that have managed to gain from innovations in a business environment where economic growth started to cool down.

A significant increase in profit anticipated for the next five years is negatively correlated with a risk-averse culture as an obstacle to innovation. Those enterprises that anticipate significant long-term increase in profitability, rate such innovation management principles as sustaining marketing support beyond new product launch and securing early involvement of other departments that are affected by innovation lower than enterprises presenting more pessimistic profitability forecasts. The same applies to balancing risk, time frames and returns across the portfolio of innovative projects and measuring innovation performance. These negative correlations can be interpreted as evidence of the contradiction between the strategic positioning of innovative activities and beliefs concerning long-term profitability growth. Evidently, the majority of Estonian respondents do not yet see the systematic approach to selecting and managing innovative projects and innovative performance measurement as a key to sustainable competitiveness.

Conclusions

The survey highlighted a positive innovation outlook among Estonian managers, especially in the service sector, which is in line with the results of the EU Community Innovation Survey 4, reflecting more active involvement of service enterprises in innovative activities compared to production enterprises (Viia *et al.,* 2007). Although the recent Community Innovation Survey 2006 data indicates more active involvement of production companies in innovation. Our research demonstrated that production firms focus more on offering new products to existing customers, but also consider product/service offerings for overseas markets important, while financial service providers continuously focus on innovations for the better use of communication and information technology. Retailers focused more on innovation for reducing costs.

Estonian enterprises involved in the survey did not rank innovation as a top strategic priority as

Table 1: Correlation between innovation outcomes and some innovation input and process variables

Innovation input and process variables	Significant increase in business profit the last year (2006)?	High contribution of innovation to your business's profitability in 2007	Significant increase in profitability anticipated for the next 5 years?
Are you satisfied with the financial return on your investments to innovation?		r = 0.337 Sig= 0.001	
New services offering for excisting customers		r = 0.246 Sig= 0.013	
Product/service offerings for overseas markets		r = 0.238 Sig= 0.016	
Making better use of information and communication technologies		r = 0.280 Sig= 0.004	
Risk - averse culture			r = - 0,220 Sig= 0.027
A shortage of great ideas		r = - 0.306 Sig= 0.002	
Shortage of suitable talent		r = - 0.213 Sig=0.032	
Fostering an innovative culture that rewards honest failure	r = - 0.217 Sig= 0.028		
Securing early involvment of other departments			r = - 0.283 Sig=0.004
Sustaining marketing support beyond launch	r = - 0.248 Sig= 0,012		r = - 0.308 Sig= 0.002
Balancing risks, time frames and returns across innovation projects	r = - 0.271 Sig= 0.006		r = - 0.240 Sig= 0.015
Measuring innovation performance			r = - 0.205 Sig= 0.039
r=Pearson's correlation coefficient, measure of strenght of the association between the two variables. Sig= shows on which level (0.005 or 0.01) is the correlation significant.			

often as enterprises from the United Kingdom and other "old" EU countries, but the majority of enterprises rated innovation as one of the top 3 strategic priorities. Estonian enterprises however, share perceptions of possible innovation outcomes such as differentiation for competitive advantage and Organizational learning with enterprises in the more advanced EU market economies. The largest gap between importance and performance in innovation management activities can be found in both the Estonian and HES samples in the field of understanding customer needs and providing sufficient funds for projects.

Estonian respondents were in general more optimistic about obstacles to innovation than respondents from the Henley Management School 2007 innovation survey sample. Risk-averse culture is not seen by Estonian enterprises as a major innovation obstacle but shortage of ideas, lack of access to new technology and lack of co-ordination are perceived by Estonian managers as greater obstacles than by the managers of the "old" EU Member States that participated in the Henley Management School survey. In earlier research projects, a lack of time, effort and/or money have often been identified as barriers to innovation, although overcoming the influence of these factors in no way guarantees successful innovation (Pohlmann, 2005). The present survey did not specify lack of money as a specific obstacle, but rather compared obstacles that are related to innovative activities inside organisations.

Correlation analysis in the Estonian sample demonstrated that while a high contribution of innovation to business profitability in 2007 correlates positively with an innovation focus on products/services and information technology development and negatively with such innovation obstacles as shortage of great ideas and talents, long-term profitability visions of enterprises in general are not based on a systematic approach to managing the risks in the innovation project portfolio, supporting post-launch marketing activities and measuring results of innovation performance. Innovating by offering new products and services that had positive correlations with high profitability contribution of innovation in 2007 did not have significant positive correlations with a profitability increase anticipated for the next 5 years. "Creative destruction" in the Schumpeterian (1928) sense and the scenario of rapid knowledge-based innovative development highlighted by the Estonian Development Fund report (2008) have so far not been incorporated in the long-term profitability visions of enterprises.

Attitudes towards innovation obstacles and innovation management priorities are influenced by the economic cycle and the catching-up success of new EU member states that may quite rapidly diminish their cost advantage. Short-term market orientation that is driven only by existing domestic demand without anticipating new ways to solve problems for customers and without attracting new more demanding overseas clients may produce short-term profit, but is not able to support a long-term strategic approach to developing dynamic capabilities for the strategic positioning of innovation. Two-thirds of Estonian production enterprises however, considered innovation focus on products and services for export extremely important. On the assumption that innovation supports exports (Lachenmaier and Wößmann, 2006), such enterprises may have opportunities to adapt to the declining demand of the domestic market during the economic crisis.

A future challenge for innovative Estonian entrepreneurs and managers is to develop networks and knowledge flows that could lead to long-term value growth through technology-driven innovations that also match new trends in global markets. Limited co-operation between enterprises and universities and public research institutions as pointed out in the EU Community Innovation Survey (Viia *et al.,* 2007) was also revealed in this research. The doing and using mode of innovation dominates, but interaction with external innovative resource providers is not sufficient for combining such a mode with the science-based innovation mode in a way that could lead to more intensive product innovation in line with the research results of Jensen et al. (2007).

The cluster analysis revealed different patterns of dealing with innovation obstacles and innovation management challenges. The clusters appeared to be quite diversified in terms of business sectors and demonstrate cross-sector mindsets that would need further research.

The innovation survey sample in Estonia does not represent all industries involved in innovative activities. Larger enterprises are to some extent over-represented in this sample. The limitations of the representativeness of the survey sample also result from selecting enterprises that are linked to managers and entrepreneurs involved in business studies. The self-selection of respondents for the HES online survey sample may, however, have also led to a bias towards respondents that are more interested than other entrepreneurs in reflecting their innovative activity priorities.

Deepening research into innovation obstacles and innovation management focus assumes the need to integrate quantitative and qualitative research by using learning processes as the environment for reflecting innovative activities. Experiential learning as the process of creating knowledge through the transformation of experience in the learning cycle of experiencing, reflecting, thinking and acting (Kolb and Kolb, 2005) could be one possible framework for developing qualitative research, where the innovation survey can be used as the first step for comparing the innovative experiences and innovative action priorities of entrepreneurs that participate in a multi-module training programme.

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EBS REVIEW
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A Test of Retail Service Brand Extensions in Estonia: Tallinna Kaubamaja and Selver

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Abstract

With the service sector representing the fastest growing economic sector within newly ascended European Union countries such as Estonia, this study presents the development and testing of a model to measure the value of brand extensions. Line extension, or the expansion of established brands into related and non-related fields, has been studied extensively in the product brand literature. Such practices have been examined to a lesser extent in the service sector, although they are not uncommon (for example, the hotel and credit card fields). Furthermore, there has been little attention paid to the value of such practices within the retail sector, and no known studies have addressed this question outside of western markets.

The concept of retail brand extension is examined through the use of an empirical study that looks at one of Estonia's more successful retail brand extensions, Tallinna Kaubamaja and Selver. This study develops a model to measure the drivers of retail success for both the main brand and the step-down1 extension within Estonia, and empirically tests the model based on Estonian consumer survey data. Consumer retail expectations are explained by testing the significance of shopping behaviour constructs on consumer attitudes towards the retail brand, and customer loyalty measures. The results suggest that retailers must both duplicate and alter existing retail practices to succeed when extending their retail brand. This is the first known study to empirically test the link between brand attitudes, merchandise factors and customer loyalty in Estonia. Therefore, implications for both retail study and practice within and outside Estonia are also discussed.

Introduction

Just as the services sector represents the majority of economic output and growth in the West (World Bank, 2003), the services sector has begun to lead economic development in newly ascended EU markets such as Estonia. The choice of the retail sector is deliberate. The number of retailers has increased rapidly in Estonia since the end of the communist period (Drtina, 1995; Robinson, 1998; Dawson, 2000), and as the Estonian economy grew and the political and social environments changed, more modern, larger and foreign-owned retailers entered the marketplace (Dawson, 1999; Eesti Konjunktuurlinstituut, 2002). Price was no longer the sole criterion for retail competition and there was a need for retailers to have a greater understanding of additional retail practices and retail drivers from a local perspective.

In addition, a stronger awareness of how retailers should make marketing strategy and operational

The "Main" brand is the retail brand that first exists, from which subsequent retail brands emerge – the term "step-down" brand in contrast to "step-up" brand refers to the fact that the subsequent brand is "lesser" in certain ways – for this study, Tallinna Kaubamaja as a traditional department store would provide a greater degree of retail service, and on average for similar products, higher quality products, and higher priced products than the "step-down" brand Selver.

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decisions has important managerial implications in terms of retailing, educational development and East/West business opportunities (Smith, 1990; Lempert, 1996; Cyr, 1997). The research findings of this study, using Estonia as an exemplar of a new EU state, is expected to be of interest to retailers looking at expanding operations into Estonia and similar growing markets, who would have historically had less experience and access to retail research of this type.

Thus by examining one known driver of marketing success in one market and in one service sector, the goal of this study is to produce a tool that has meaning and relevance to retailers in Estonia specifically, and a greater understanding of the positives and negatives of retail brand extension in general. The remainder of the paper is as follows. The following section provides the background and theoretical perspective used in developing a model to test the relationships between shopping behaviour constructs and those arising from the extension of an existing retail brand. Next there is a review of the methodology used to empirically test the model, including the administration and collection of consumer data, while the remainder of the paper reviews and interprets the findings, and discusses contributions to the brand extension literature, its role in retail practice and the significance of these types of studies in emerging markets. The paper concludes with suggestions for future study.

Research Background

The study of brand extensions, as the name implies, has grown out of branding literature. Although the long history of brand research has mainly focused on the study of branding as it relates to products (Gardner and Levy, 1955), research on the branding of services has developed more recently (see Dibb and Simkin, 1993). The added complexity of the intangible nature of services has resulted in different perspectives on how to brand services (Moorthi 2002).

Specific research on brand extensions, or the expansion of an existing brand into a different field (Aaker and Keller 1990), has received an increasing level of interest in the past two decades as both researchers and practitioners better understand the benefits from extending an existing brand, versus new brand creation. In brief, the extension of a brand is based upon assumptions or associations in consumers' minds that extend the perceived benefits (although in theory, also disadvantages) of the parent brand to that of the brand extension (Keller 1993). General interest in brand extensions has been based on research findings that have supported the position that the extended brand can enhance sales growth (Ambler and Styles, 1997), lessen consumer buying risk (Seines, 1998), imply quality associations (Keller and Aaker, 1992), economies of scale in marketing practices such as advertising (Roberts and McDonald, 1989), and others (see Jobber, 2004: 279-281).

In terms of research into brand extension in services, the research is less plentiful. Although services represent a large and growing share of the world's economy, there have been fewer studies that have researched the degree that the product brand extension literature also applies to services. One such study by Van Riel, Lemmink and Ouwersloot (2001) replicated the product brand extension work of Aaker and Keller (1990) and found that for service brand extensions, as in product brand extensions, consumers use the main brand as a cue to evaluate the extension, and recommend service brand extensions when service delivery processes can be duplicated.

With respect to brand extensions in the retail sector, although research has looked at retail loyalty and product brand loyalty, and that the brand of the retailer is an important concept in shaping that loyalty (Dawson, 2001) no studies were found that have focused on the why's and how's of retailer brand extension. Finally, the leading research in service brand extensions has solely focused on studied practices within the West. Thus, this study attempts to address this gap in the literature by developing and testing a model of service brand extensions, as it applies within a retail setting, as well as exploring the significance of such practices within a non-western or emerging market such as Estonia.

Model Development

As the value of retail brand extension for a firm's success is the main focus of this study, this study also theorizes which retail constructs play a role in the overall shopping behaviour of consumers in Estonia. This is measured by establishing the predictive validity of shopping behaviour constructs within a broader framework that best explains patronage loyalty behaviour (i.e. customer loyalty) and the attitude of consumers to the main and step-down store brand (i.e. attitude to the retail brand).

One approach in modelling customer store loyalty is to use variables that represent future purchase intentions. The position of this study is to suggest that those intentions are mediated by how the customer evaluates the specific store brand (Low and Lamb, 2000). The constructs used to indicate that attitude are judged to differ for the main and the step-down brand, with the resulting measure of attitude to the retail brand linked to customer store loyalty. The suggestion is that if a retailer delivers a certain level of retail service, then a level of trust that this performance will continue in the future develops (Morgan and Hunt, 1994). This view is that trust is represented by different drivers of shopping behaviour, depending on the type of store brand (see Merrilees and Fry, 2002), with retail service as an attitude that carries over into the future.

Furthermore, the main constructs that determine the attitude to the retail brand will also have an indirect effect on customer loyalty. In addition to the attitude to the retail brand and customer loyalty constructs, additional indicators of shopping behaviour must also be evaluated. These include merchandise selection, merchandise price, retail service and store location (Lindquist, 1975; Lichtenstein, Ridgway, and Netemeyer, 1993; Rinne and Swinyard, 1995). The proposed linkage between attitudes to the brand, the constructs of merchandise price and merchandise selection, and retail service as indicators of retail shopping behaviour has empirical support in the research literature (Bei and Chiao, 2001). Furthermore, the measurement of customer store loyalty, as the dependent variable in modelling shopping behaviour, is also maintained (Hansen and Deutscher, 1978; Yoo, Park and MacInnis, 1998). These relationships are depicted in Figure 1.

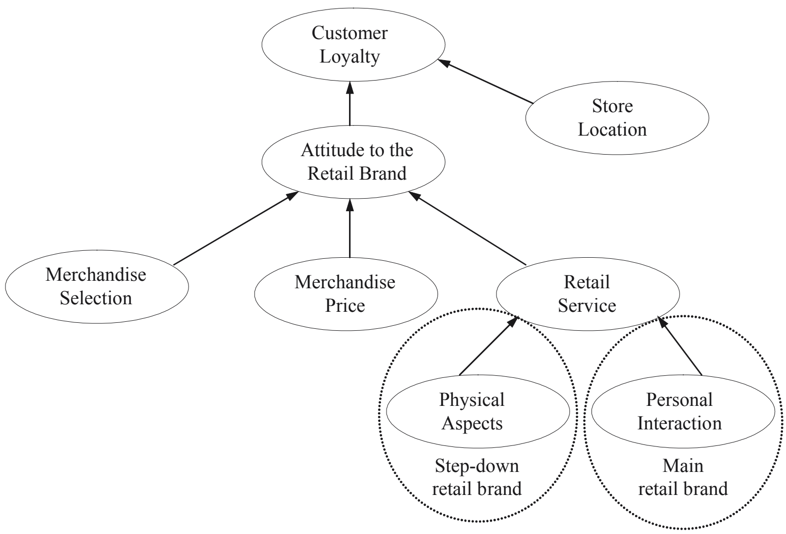

Figure 1: A model of retail brand extension in Estonia

The construct of merchandise selection includes both physical, objective measures of the quality of the merchandise (Wheatley, Chiu and Goldman, 1981) and indicators that represent the styles and brands of merchandise that the store carries (Rinne and Swinyard, 1995). Furthermore, merchandise selection evaluates how well a store performs at matching the types of goods carried with what consumers actually want (i.e. the "fit" of the selection to the perceptions of the consumers).

For merchandise price, there is a lengthy research history into the relationship between price and shopping behaviour (Dodds, 1991), and that merchandise price has an influence on customer loyalty (Cronin and Taylor, 1992). Merchandise price is defined as the part of the shopping experience where the evaluation of the price of goods relative to the type of retail store has a measurable affect on shopping behaviour (Kerin *et al.,* 1992). Within the retailing research literature, measures to operationalize the merchandise price construct have focused on two types of pricing concepts. The first concerns how shoppers form attitudes about a store based on the price of the products sold (Kerin *et al.,* 1992), and the second is the impact that temporary price discounts or sales have on purchase behaviour (Blattberg and Wisniewski, 1989).

Customer loyalty has been previously purported in the literature as a measure to capture the degree of future purchases (Heskett *et al.,* 1994; Berman and Evans, 2001). In this study the construct is viewed as a non-random (biased) behavioural response with respect to store choice (Jacoby and Chestnut, 1978), as well as an attitude of the consumer's cognitive intent in terms of loyalty, which in a retail environment is measured by a customer's stated loyalty to shop at a store. From a behavioural perspective, customer loyalty is defined as the consumer's future intent. In a retail setting, intent is measured as the frequency of shopping a store in the future, or the intent to recommend the store to others (Boulding *et al.,* 1993).

Finally, the store location construct is well established in the retail literature in terms of its impact on retailer patronage (Huff, 1964). The location construct has been studied in terms of its impact on convenience for shopping (Lindquist, 1975), and although research has shown that a consumer may visit an arguably less convenient, or more distant store for personal reasons (Burns and Warren, 1995), this is judged to be of lesser relevance in a country such as Estonia where the costs and distances involved in such travel would be a limiting factor. Thus, the store location construct for this study is conceived in terms of convenience measures.

Thus, in order to test these proposed relationships, a series of equations are developed. The first proposition is that a consumer's attitude towards the main retail brand, when a step-down brand extension exists, will be defined by constructs of merchandise selection, merchandise price and a measure of retail service. As suggested in the branding literature, the main brand must provide something different (i.e. better) than the step-down brand if differentiation in the customer's mind is to be established. As the retail literature views the intangible or more subjective measures of service as more difficult to achieve in comparison to tangible or objective aspects of service, then the attitude to the main retail brand will be more heavily influenced by the former and the attitude to the step-down brand by the latter. Because retail service consists of both tangible and intangible aspects, we suggest that the intangible or personal service aspects of retail service dominate for the main retail brand, and the tangible or physical aspects of service for the step-down brand.

Personal service, or what we refer to as personal interaction measures of service, is defined as the actions of the retail service personnel and how they interact with store customers (Dabholkar *et al.,* 1996). In contrast, the tangible aspects of service, what is labelled as physical aspects, is defined as a measure of the physical indicators of the retail experience. Thus, the first set of equations that theorize the relationship between shopping behaviour constructs and the attitude to the retail brand are:

(1a) MRB = f (MP; MS; PI)
(1b) *SD*B = f (MP; MS; PA)

The attitude towards the retail brand (MRB for the main brand, and SDB for the step-down brand) is a function of merchandise price (MP) and merchandise selection (MS) and a retail service construct. For the main brand it is a personal interaction construct (PI) and for the step-down brand a physical aspects construct (PA).

The second set of equations places the construct of attitude to the retail brand (both MRB and SDB) within the realm of future shopping behaviour, or customer loyalty. Although attitude to the retail brand is theorized to dominate this relationship, there is also an expectation that the store location (LO) can influence one's willingness to revisit a store (however, the store location is not likely to influence brand attitudes about the store). Different locations would be valued differently so there would not be a constant relation to brand attitude. In this case, the theorized relationship to customer loyalty (CL) is the same for both the main and step-down brand, and is represented by the following equations:

(2a) CL = f (MRB; LO)
(2b) CL = f (SDB; LO)

When taken together, the testing of these two sets of equations will best indicate the similar and dissimilar relationships that the consumers attitude towards the main and step-down brands have towards current and future shopping behaviour.

Data Collection

The testing of the model in Figure 1 and related equations presented in the previous section require the use of multiple item scales, as each of the constructs is better defined using multiple indicators (Jacoby, 1978; Churchill, 1979). Each of shopping behaviour scales are developed using existing and proposed scale measures (Baker *et al.,* 1992; Rinne and Swinyard, 1995; Merrilees and Miller, 2001).

The merchandise selection (MS) construct is defined by objective measures of merchandise quality such as durability and reliability (Garvin 1987), and subjective measures of merchandise quality such as product brands and styles (Merrilees and Miller, 2001). The merchandise price (MS) construct is defined by two types of consumer price perceptions as discussed by Dickson and MacLaclan (1990). The first is the reasonableness of product prices with respect to value received, and the second is how significant consumers perceive a store's sale prices, or specials. Finally, for the retail service construct, the personal interaction elements (PI) included the presence of knowledgeable, courteous salespeople, and the speed of the service provided (Dabholkar *et al.,* 1996). For the physical aspects of service (PA), the look or aesthetics of the store as well as the layout of the store were the focus of the construct (Rinne and Swinyard, 1995; Dabholkar *et al.,* 1996).

For attitude to the retail brand, measures of consumer views of both personal perceptions and how others feel about the store are included. For the location construct a sense of convenience and proximity to one's home are considered. Finally, for customer loyalty, items that estimate both a customer's intention of future shopping behaviour and the extent of that shopping behaviour are included.

In total, twenty-three retail shopping questions were developed. A list of these items can be found in Appendix 1. There were three items to measure attitude to the retail brand, three items for merchandise selection, two for merchandise price, twelve (six for physical aspects, and six for personal interaction) for retail service, two for location and four for customer loyalty.

The next step in the research was to create a survey instrument in order to collect empirical data to test the proposed relationships. A paper and pencil survey questionnaire was selected for this purpose. As the study was to be conducted outside the country of the author, the administration and collection of the surveys was conducted by contacts that had been previously established during field research in Estonia as part of a larger study of retailing in Estonia. The sample respondents consisted of consumers at the sole retail brand operating in Estonia at the time of the study that had both a main and step-down brand. The main brand, Tallinna Kaubamaja, is the "central department store" located in the capital city of Tallinn, and which opened in 1960 as a state enterprise. It is the oldest department store in Estonia and sells both traditional department store goods as well as foodstuffs. It was privatized in 1994, and in 1995 opened its first brand extension, Selver. The retail (step-down) brand, Selver, consists of both hypermarkets and supermarkets.

For this study, a non-probability sample of Estonian shoppers was determined to provide an acceptable level of information about shopping behaviour because of a lack of official data, or private data that defines the population of shoppers. As a control measure, only those respondents that had visited the sample stores within the last six months were desired in order to provide consistency about store performance knowledge.

The respondents could complete the survey in either Estonian or English, and general demographic information was also collected. It is suggested in the literature, with respect to the purpose of this type of study, that a sample size of 100–200 is adequate for statistical analysis (Clark and Watson, 1995). It was decided that a minimum of 100 surveys for each store would be an acceptable number for the analysis. The respondents were contacted by telephone, e-mail, or mall/street intercepts, and asked to answer a series of questions about shopping behaviour. The rating scale used a 9-point scale, with scores of "1" if the respondent strongly agreed with the statement and "9" if they strongly disagreed. A score of "5" would be representative of a neutral feeling. The responses to all questions were recorded by the survey administrator, and the completed data was sent to the author for analysis.

In total, 255 completed surveys were collected and used for the subsequent analysis stage of the study. There were 137 surveys for Tallinna Kaubamaja, and 118 surveys for Selver. The individual responses to the questions asked varied (as indicated by the standard deviation values), and respondents tended towards the agreement side with statements, as indicated by the vast majority of mean scores of between two and five (see Appendix I).

Table 1: Scale reliability measures

Scale		Main Brand	Step-down Brand
Attitude to the Retail Brand (3 Items)	**alpha =**	0,71	0,73
Merchandise Selection (3 Items)	**alpha =**	0,84	0,77
Merchandise Price (2 Items)	**alpha =**	0,76	0,79
Personal Interaction (6 Items)	**alpha =**	0,89	0,910
Physical Aspects (6 Items)	**alpha =**	0,86	0,9
Customer Loyalty (4 Items)	**alpha =**	0,84	0,86
Location (2 Items)	**alpha =**	0,73	0,82
Note: Main Brand = Tallinna Kaubamaja, Step-down Brand = Selver			

Data Analysis and Model Testing

The first step in the data analysis was to determine the degree to which each of the proposed items represented the proposed constructs of shopping behaviour. This was determined using the Cronbach Alpha (Cronbach, 1951) of the proposed scales. The Cronbach Alpha values were calculated using SPSS 15.00, and as shown in Table 1, all proposed scales were above the generally accepted level of 0.70 (Hair *et al.,* 2003), indicating the inter-relatedness of the set of items.

The second step in the analysis was the testing of the proposed equations, which was done using path analysis (Kline, 1998). Path analysis was used to attest the level of the variance between dependent and independent variables. In this case, the level of customers' attitudes to the retail brand, and in turn customers' attitudes to the retail brand was used as the main determinant of customer store loyalty, with support from the location attribute. When taken together, a better understanding of both the indirect effects of merchandise selection, merchandise price and retail service measures on the consumers' attitudes to the main and step-down brand can be evaluated and their impact on customer store loyalty.

Each of the constructs was tested in terms of the significance of each for the proposed dependent variable. Table 2 provides this information for the four equations (two for the main retail brand, Tallinna Kaubamaja, and two for the step-down brand, Selver). As indicated in Table 2, the regression coefficients for the three proposed constructs are all high and significant. Merchandise selection, merchandise price and retail service as indicated by personal interaction measures all had a significant effect on the attitude to the main brand. For the step-down brand, the three constructs were also high and significant. As noted, the difference was that retail service was now represented by physical aspects of the service provided.

In order to check if alternative retail service relationships could also be viewed as significant (i.e. were both measures of physical aspects and personal interaction significant in terms of retail service for both the major brand and step-down brand), two additional sets of analysis were conducted. As found in Tables 3a when both physical aspects and personal interaction items were collapsed into a composite measure of retail service, the path analysis indicated that "retail service" is a significant indicator of attitude to the retail brand. But when each of the two constructs of retail service is entered separately, the

Table 2: Scale reliability measures

PATH		Attitude to the Retail Brand	
		Main Brand	Step-down Brand
Pesonal Interaction	➤	0.291** (4.04)	
Physical Aspects	➤		0.332** (4.20)
Merchandise Selection	➤	0.361** (5.21)	0.359** (5.24)
Merchandise Price	➤	0.284** (4.25)	0.258** (3.30)
Adjusted R-square	➤	0,460	0,56
(t-values in parentheses) ** significance p<.01			

Table 3 a: Scale reliability measures

PATH		Attitude to the Retail Brand	
		Main Brand	Step-down Brand
Retail Service	➤	0.324**	0.372**
(Physical Aspects+Perssonal Interaction)	➤	(4.25)	(4.53)
Merchandise Selection	➤	0.318** (4.40)	0.316** (4.51)
Merchandise Price	➤	0.273** (4.09)	0.235** (2.95)
Adjusted R-square	➤	0,466	0,56
(t-values in parentheses) ** significance p<.01			

Table 3 b: Scale reliability measures

PATH		Attitude to the Retail Brand	
		Main Brand	Step-down Brand
Pesonal Interaction	➤	0.207* (2.18)	0,14 (1.45)
Physical Aspects	➤	0,14 (1.30)	0.260** (2.84)
Merchandise Selection	➤	0.324** (4.35)	0.326** (4.55)
Merchandise Price	➤	0.273** (4.08)	0.233** (2.92)
Adjusted R-square	➤	0,46	0,56
(t-values in parentheses) ** significance p<.01 * siginificance p<.05			

Table 4: Scale reliability measures

PATH		Customer Loyalty	
		Main Brand	Step-down Brand
Attitude to the Retail Brand	➤	0.662** (10.65)	0.522** (8.25)
Location	➤	0.167 ** (2.68)	0.410** (6.47)
Adjusted R-square	➤	0.530	0.65
(t-values in parentheses) ** significance p<.01			

physical aspects construct does not significantly relate to attitude to the main brand. Correspondingly, for the step-down brand, when the two retail constructs are run separately, the personal aspects construct is not significant (Table 3b). This additional test provides further support for the proposed relationship that consumers develop an attitude to a retail brand differently for the main versus a step-down brand.

The last step in the analysis was to determine the impact on customer loyalty of the consumer's attitudes towards the retail brand. As indicated above, the inclusion of a location construct was to account for the constraint that a store faces based on its physical location. As shown in Table 4 for both the main retail brand and the step-down brand, both attitudes towards the brand and the location were significant indicators of customer loyalty.

Interpretation of the Research Findings

As found in existing retail literature, the price and selection of the merchandise represent key drivers in how a consumer interprets a retail brand (Grewa *et al.,* 1998), and this study has extended that finding in the measurement of such drivers in Estonia. The findings also support the position that the attitude toward the retail brand has a non-trivial impact on future shopping behaviour as defined by customer loyalty measures.

Based on the analysis of the empirical data, the three proposed shopping behaviour constructs account for approximately 46.0% of the variance in Estonian customers' attitudes towards the main retail brand. For the step-down brand, it was 55.5%. This finding aligns with existing retail literature that suggests that consumers have a multi-level perception about a store, but also that their perception is different if it is towards a main or a step-down brand. The implication of this finding relates to the extent to which the positive (or negative) image that a consumer has of the parent or main store brand carries over into its subsequent step-up or step-down brands. Although this study did not test this relationship statistically, an analysis of the responses to a question that asked respondents to list other stores at which they shop indicated that approximately 49% of Tallinna Kaubamaja respondents listed Selver, and 52% of Selver respondents listed Tallinna Kaubamaja. The implication would be that brand extension certainly can have an impact on increasing the total share of a consumers shopping basket, and that a positive (or negative) perception may extend to the other brands. Thus, a key finding for retailers wishing to extend their brand within markets such as Estonia is to be aware that these consumers are more apt to shop at more stores than ones home market.

A further implication of the findings is that a different focus is required if a retail brand is going to extend their reach into a higher or lower field of retailing, and the major focus for that difference is on the level of service. Although previous studies have looked at the appropriate level of service to provide in different types of retail settings (Tordjman, 1994), this study represents the first known attempt to empirically test that notion, as well as to extend the understanding of these differences within a retail brand extension environment.

Conclusions and Future Study

Within the branding literature, one of the limitations has been that the research has often used hypothetical extensions to test for relationships. This is suggested as a critical limitation in retailing research as consumers are generally aware of both the main and extended brands, and findings may be erroneous based on their past knowledge and experiences. Thus, as suggested by Zimmer and Bhat (2004), real consumers may have more exaggerated reactions to the main brand limiting the contribution from such experimental research. Therefore, as stated at the outset of this paper, the main focus of this research was to empirically examine and test a proposed model of shopping behaviour that examines the similarities and differences in terms of real consumer perceptions for a retailer that has extended their retail brand. This was accomplished by both developing a theoretical model supported by the branding literature, and empirically testing it using actual consumer perceptions, which helps to advance both the academic and retail practice literature in this field.

In terms of academic research, there was support that the existing shopping behaviour constructs and measures can also be employed in Estonia, and that as in the product brand literature, adaptation and different perspectives are required in theorizing the formation of alternative retail brands. Although previous research has demonstrated a strong linkage between brand attitude and customer loyalty (Delgado-Ballester and Munuera-Aleman, 2001; Taylor and Hunter, 2003), this is the first known study to empirically test this concept within a country such as Estonia. In terms of the predictive validity of the retail drivers, this study advocates the separation of the construct into measures of physical aspects and measures of personal interaction as they have a different level of significance in terms of attitudes towards the retail brand depending upon if it is the main brand or step-down brand. The contribution of this finding results from the adding of two merchandise factors in order to better understand how Estonian customers' attitudes to the retail brand is formed.

For retail practitioners (both domestic and those wishing to expand into markets such as Estonia), this research provides a greater depth of understanding of how the measures of retail service are perceived by consumers, and how these measures can be linked to shopping behaviour (Dick and Basu, 1994; Sirohi *et al.,* 1998). For retailers thinking of extending their retail brand within a non-western market, this requires both a focus on existing drivers, but also different perspectives in terms of retail service depending on if a step-up or step-down extension is planned. As shown in this Estonian case, in both instances a measure of retail service was deemed significant in impacting how a consumer evaluates the overall retail brand, but that it is at a lower, or dimensional, level where differences need to exist. Although this study was based on one retailer in one market, it none-the-less indicates that a retailer need not, and should not, merely extend all retail practices to the extended brand, but rather focus on a different perspective of service if stepping up or down.

Finally, if as purported that brands drive nearly two-thirds of consumer purchases (Davis and Halligan, 2002), the application of this study in further research should look at testing this type of empirical research in similar markets, and possibly examine a step-up retail brand, or other service step-up or step-down extensions. It is further suggested that exploring these types of questions in markets such as Estonia where fewer examples exist can enhance both academic research and retail practice as these markets represent increasingly important areas for service industry growth.

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Appendix 1: Scale measures of shopping behaviour

Scale Items	Main Brand (n=137)		Step-down Brand (n=118)	
Attitude to the Retail Brand (3 Items)	**Mean**	**Std. Dev.**	**Mean**	**Std. Dev.**
This store has a good reputation among customers	3,20	2,07	3,36	2,05
There is something special about this store	4,48	2,15	4,08	2,13
I really admire this store	4,41	2,34	4,53	2,56
Merchandise Selection (3 Items)				
The merchandise at this store is of high quality	3,61	2,00	4,21	2,18
This store has clothing of the latest trends and styles	3,22	2,24	5,24	2,35
The product brands in this store are really good	3,01	2,18	5,04	2,31
Merchandise Price (2 Items)				
This store's "sales" and specials are real bargains	4,09	2,29	3,94	2,38
This store has reasonable prices (value for money)	4,76	2,25	3,82	2,27
Personal Interaction (6 Items)				
Selling staff are always courteous with customers	3,31	2,32	2,98	2,21
This store has a fast check-out	3,49	2,29	3,17	2,05
The selling staff at this store treat me with respect	2,49	2..27	3,27	2,11
This store has knowledgeable staff who can answer customer queries	3,56	2,21	3,53	1,91
The employees at this store give you confidence for your shopping	3,79	2,02	3,68	1,96
Selling staff are available and quick to help	3,74	2,40	4,05	2,42
Physical Aspects (6 Items)				
This store is clean and tidy	2,57	2,23	3,10	2,22
The merchandise displays at this store look good visually	2,87	2,32	3,20	2,22
This store has a modern look about it	2,90	2,45	3,55	2,20
This store provides helpful signs so I can find the products I am looking for	3,84	2,41	3,29	2,36
Self-selection at this store is easy and well guided	3,72	2,24	3,55	2,08
This store is rarely out of stock on items	3,64	2,45	3,79	2,38
Customer Loyalty (4 Items)				
I plan to shop at this store (again) in the next 6 months	3,05	2,41	3,18	2,54
I plan to recommend this store to others in the next 6 months	3,80	2,23	3,92	2,43
My next purchase is likely to be from this store	4,97	2,58	4,39	2,62
I am likely to spend the same (or more) amount of money in this store in the next 6 months compared to the last 6 months	4,48	2,56	4,22	2,70
Location (2 Items)				
The store location is convenient for me	3,79	2,55	3,78	2,75
The store is close to my home	5,18	2,98	4,02	2,94

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Financial Management and Financial Analysis in Libraries: the Case of the National Library of Estonia

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Abstract

The National Library of Estonia (NLE) has a responsible role before the state and the nation of Estonia and the international cultural public to preserve cultural memory and heritage, Estonian literature, the centre of national bibliography and the parliamentary library. The successful work of the library under economic pressure requires better planning in the use of all resources. Although libraries are not enterprises that earn a profit there is still a need to find additional resources for activities and development by raising funds and participating in an international projects. The current study focuses on mapping the principles of financial planning and the needs of contemporary libraries and information institutions, and analysing the financial economic activities, financing principles and likewise analysing statistical economic indicators from the most important articles about income-expenses from 1996 to 2006 for the National Library of Estonia.

Keywords: financial management, libraries, library finance, national libraries, financial analysis, resource management, cost-benefit analysis

Introduction

A library, as with any other public sector organization, should be handled as a part of the state system and the social model of society. The resources and services offered by the library have to correspond with the needs of information consumers and society at large.

Libraries are public sector organizations whose activity is important for many people and society as a whole. The financial management of the library as a public sector organization differs significantly from the economics of the private sector, and it is important for the management and financers of the library to understand this difference in order to make the best decisions.

Measuring the results of the work of a library via analysing the statistical economic indicators – income and expenses – is one way to assure the effective work of a library. The economic situation and a library's results nowadays represent important research spheres in library and information sciences, and this directly relates to the management and planning of the work of a library. Library economics belongs to a sphere of econometrics and deals with the analysis of library statistics. The purpose of library statistics is to gather, process and analyse data and to present reliable overviews in order to evaluate the economic situation that libraries find themselves in. Planning also includes financial planning, and cost effectiveness and income-expenses analysis. In order to make optimal decisions to improve the work of libraries, it is important to constantly gather statistical information about these strategic actions and to conduct such analyses regularly. Thus, making it possible to decide about the allocation of a library's resources and the effective use of the services it provides.

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It is due to these factors, and the fact that the author of the current article was working at the NLE at the time of writing, that the author finds becoming better acquainted with the economics of a large library relevant, necessary and also of personal interest.

The aim of this article is to analyze the principles of the allocation of resources, the financial management and the economic activities of the National Library of Estonia (henceforth NLE) within the Estonian public administration system as a legal body in public law.

As far as the author knows, this is the first time an analysis spanning 10 years like this has been carried out. So far, only short-term statistical data has been examined as part of different comparative analyses of Estonian research libraries (Nuut, 2001; Puura, 2007).

The current analysis concentrates on the following tasks:

- to obtain an overview of the theoretical positions of financial management in libraries;
- to analyse the principles for compiling the NLE budget within the Estonian public administration system;
- to analyse the general development of the NLE over the last ten years;
- to handle the dynamics of expenses in the NLE budget from 1996 to 2006;
- to analyse changes in income in the economic activities of the NLE from 1998 to 2006.

Financial Management of Public Sector Organizations

Ideas from the area of business management and the principles of organizational management successfully introduce notions of quality, performance management, benchmarking and so on to practices in public sector organizations and organizations based on public-law. These new methods and principles of organizational management are necessary because of the greater demands being placed on public sector services. At the same time, the limited resources in the management of such organizations must also be considered, and this forces these organisations to search for solutions in order to satisfy the needs of clients and financers in the best way (Puura, 2007). For example, promoting competition between organizations, raising finances independent of the state budget and so on are among just some of the new management techniques being adopted in public sector organizations.

Organizational management theorists are divided in two schools when comparing public and business sector organizations, one group finds that these organizations are incomparable objects, and the other group finds that the size of the organization, its tasks and branch of activity are more important than its legal status. There are some specific factors – such as the absence of market mechanisms, the “production” of products and services that can’t be measured in market prices, the emphasis of abstract values like honesty, justice, loyalty and so on – that need to be considered when applying management techniques from business organizations in public sector organizations (Aru, 2001).

The management of economic results in the public sector (including the domain of economic calculations) originates from the idea of New Public Management – or applying the management principles of the private sector to public sector organizations.

The focus of planning and control (accountancy) in the public sector converge at the following points (Böhret, 1993):

- tactical and strategic plan,
- results planning and budget
- hierarchical planning and accountancy
- results standards
- accountancy results
- audit results
- costs evaluation and costs/income/efficacy research.

Reform endeavours in the public sector are targeted at making savings or improving work performance; often broad organizational changes accompany this, such as decentralization or reforms of financial management, inculcating public sector values among employees resulting in greater price awareness, stronger concentration on services or a greater desire to take responsibility for results. Better management of the public sector is vitally important to achieve economy, effectiveness and expertness in the short- and long-term perspective. The potential to activate better management practices definitely exist in almost every public sector organization. Cutting costs can have a great influence on the organization and its management – it exposes weaknesses and deficits that can be hidden in better economic conditions. Traditional public sector values emphasise primarily stability, predictability, constancy and certainty (Metcalfe and Richards, 1993).

Reliable financial management is a budgeting principle, and according to the principles of economy, effectiveness and efficiency, it forms the basis of public sector institutions. This means that concrete purposes and planned results are achieved (effectiveness) at the lowest price with the available resources (economy), assuring the best relationship between resources used and results achieved (efficiency).

Management levels in a reliable financial management process are related to planning and controlling activities as in any public sector organization. They include:

- the strategic management level – the purposes of the organization and their adjustment, the acquisition and use of the resources necessary for achieving goals, monitoring the entire organization

- the tactical management level – fulfilling strategic decisions based on financial analysis, using activity reports for monitoring (income, costs) and summarized data from different activities

- the operational management level – decisions on the level of detailed transactions and everyday activities, monitoring single activities

Efficiency means using limited resources in a best way for the purposes of the organization. The economic definition of effectiveness compares costs and income, or in other words, compares the use of resources and the results achieved. Using the criteria of effectiveness in the public sector is much more complicated than in an organization whose main orientation is to earn a profit. Using the criteria of economic effectiveness above all depends on the comprehensibility and quantifiability of the purpose of the organization. It is rarely possible to formulate such purposes in the public sector, and accidental and systematic mistakes occur when measuring them. The existence of such purposes is not enough on its own, they also have to be presented in the form of activities that simplify the measurement of services results (Tõnnisson, 1998).

Problems in the Financial Management of Libraries

The management of one public sector organization, such as a library, has been described as something enormously specific and complicated. In fact, business management ideas, organizational management techniques and contemporary methods of analysis have also been applied to libraries. The measurement of the results of the work of a public sector organization, such as a library, with the help of statistical economic indicators – analysing costs and income – is one of the most certain ways to ensure the efficacy of the library.

Beside performance indicators libraries have started to apply the balanced scorecard, Data Development Analysis (DEA), and new methods of pricing like Activity Based Costing (ABC) and Time-Divided Activity Based Costing (TDABC).

The dependence on local government and state finances and the increasing costs of publications, electronic databases and so on, have recently influenced the library and information sector both positively and negatively – new markets and target groups have been discovered little by little, new services with additional value have been sought and new management tactics have been applied. An understanding now exists that bookkeepers are not the only professionals related to the financial processes of libraries and the information sector (Roberts, 2003). Working in a net-centric information environment demands complex finances, management and technical skills. Managers have to manage the acquisition of licences, the observance of the costs of internet services, and auditing at the organizational, departmental and personal level. Distinguishing between the costs of systems and the costs of services characterize libraries and information institutions. Managers have to be able to justify the expenses of concrete items and their entire range of services more than ever before (Corrall, 2000).

Table 1: Financial Management Studies in libraries in the US, UK and Germany (Roberts, 2003).

	Pre-1968	1968-1984	1985-1997	Total
Cost Studies	21	178	61	260
Broader Financial Management Studies	9	111	105	225
Total	**30**	**289**	**166**	**485**

In the 1960s, specialist papers about forecasting costs, economic calculations, accountancy and other related activities in the libraries started to appear. The statistics about studies that have been published in the United States, Great Britain and Germany are summarised in Table 1. The number of studies published increased abruptly after 1967 and up till 1984 as can be seen in the table. Broader studies of financial management (planning, budgeting, financial studies generally) continued to the same extent. The figures in the table do not pretend to be absolute because a large number of these studies are only for the internal use of the library, but they still prove to be of great interest because finances are more and more important in relation to everything going on in the library (Roberts, 2003).

The Europe-wide library economics project, LibEcon, an international research study into library economics (Millennium Study 2000 - Library Economics in Europe) started in 1998 and lasted a total of 6 years. There were over 30 countries in the project, and the NLE participated as a partner from Estonia. Statistical data was gathered and analyzed for the period 1991–1998 about national, university and public libraries. The purpose of the project was to harmonise methods for gathering and analyzing library statistics among participating countries, to make the analysis of activity results more effective, to ensure the application of these methods and the use of indicators for benchmarking, to prepare proposals for modernising international standards, to regulate the methods for analysing library statistics and the presentation of these analyses and to create databases and electronic data exchanges. It also aimed to develop cooperation with museums and archives and to apply the LibEcon economics model to analyse their statistics. Survey reports from the project offer useful information for working out the politics and developmental plans for libraries, and likewise information for evaluating and auditing the performance of the work of libraries.

Since the second half of the 1980s, it has been increasingly important to acquire financial knowledge in addition to the specialized skills necessary for librarians and information specialists. The managers of libraries and information institutions have understood the importance of economic aspects in their managerial decisions – the principles and skills necessary for forecasting expenses that support the effective management and administration of libraries and information services have until now been the weakest domain in the management of the activities of libraries and information services (Kingma, 1996 ; McKay, 2003).

Research has been conducted by the department of information sciences at Tallinn University into the skills necessary for information and library employees. In the study, the employees of Tallinn University Academic library and master students in information sciences were surveyed and unfortunately, the following were among 10 skills identified as unnecessary: knowledge of statistical analysis and statistical software; composing the budget and related financial management skills; strategic planning; public relations, marketing and project management skills. Why these competencies are so unnecessary among librarians and students will be investigated in future studies (Virkus, 2007).

A comprehensive basic knowledge of the administration and analysis of financial data as well as an understanding of library concepts are necessary for future information professionals. They need to be able to distinguish between receipts and payments and income and expenditure. For example, the manager of an information service has to be able to talk to finance people while using professional library terms and later present the same story to their colleagues and clients in ordinary language (Corrall, 2000).

Recent trends in the information business have included an understanding of (McKay, 2003):

* limited financial resources;
* the need to move towards cost centre-based management of financial resources;
* their responsibility for financial decisions in the public arena and inside the organization;
* the need to ensure that money spent on the development and improvement of services is "well spent";
* the need for an increasing emphasis on the development and establishment of performance indicators for library work and services;
* the increasing need to make inter-rather than intra-Organizational comparisons;
* the need to move from purchasing the ownership of information to purchasing access to information (e.g. different databases etc.).

The budgeting process in the library has been made more complicated and difficult, and now also includes elements of strategic planning. The whole process has been developed from the simple use of line-item budgets, based purely on previous experience and expenditure, to a much more formal planning process (MacKay, 2003). Two well-known methods of systematising information and making optimal choices are the use of cost effectiveness and analyses of income and expenditure.

The purpose of evaluations according to cost-effectiveness is to find the best result for each monetary unit spent or to find the measure that provides the greatest result per invested monetary unit. The results achieved are divided according to expenditure in order to find the proportion of cost-effectiveness, and the results are gained per one monetary unit, or expenditures are divided by the results of example figures and the costs resulting are gained per single unit (Aru, 2001). Statistical indicators enable us to measure the financial resources of the library, the employees and also the time spent on one or another job. It is useful to analyse the allocation of resources in the library and use them effectively according to the following indicators: the average cost per publication, the average cost per employee, the average workforce cost, the average cost per visit, the average cost per reader (reader cost) and the average cost per service (e.g. cost of lending) (Nuut, 2001).

In libraries, the basis for this kind of analysis is the ISO 11620: 2008 *Information and documentation standard – Library performance indicators,* which forms the basic document for measuring and evaluating the results of the work of a library. This document functions as a guide for planning the activities and managing the work processes in libraries all over the world.

The methodology for analysing and the definition of the resulting indicators of the work of a library are described in this document.

The main task of the resulting indicators is to make it possible to monitor the management effectively and to offer support information in the dialogue between the management of the library and its patrons (ISO 11620, 2008).

Unfortunately, this standard does not take into consideration the activities of national libraries and the special need for measuring cost-effectiveness. National libraries have different roles all over the world – some in addition also fulfil the tasks of the parliamentary library (e.g. in Estonia and Lithuania), and some, the functions of a university library (e.g. in Finland and Denmark). Each national library has tasks that other libraries do not have – the maintenance of cultural heritage, compiling a national bibliography, participating in the work of international organizations, operating as a cultural centre etc.

Therefore, the Committee of the International Standards Organization (ISO), Information and Documentation sub committee has formulated a technical report *ISO/NP TR 28118 Information and documentation – Performance indicators for national libraries* (ISO/NP TR 28118, 2008). This report was formulated on the basis of extensive and exhaustive analysis. In 2001, a test questionnaire was administered (e.g. *state-of-the-art* questionnaire with closed and open questions) to 41 European national libraries in order to determine previous problems and bottlenecks in the evaluation of the results of activities in national libraries. A more detailed questionnaire followed this in 2002, and 21 libraries responded (Ambrožič, 2003).

The questions in these studies explored a wide spectrum, including the strategic development plan, mission, vision, tasks, existence and fulfilment of purposes, responsibilities and domain complements of national libraries, financial resources and connections between finances and effectiveness indicators, the analyses of income and expenditure and frequency of the evaluation of cost indicators etc. The results showed that the analyses of finances and costs are carried out regularly in some libraries. Thirty-eight percent of libraries get their income directly from the state, 38% through a ministry and their own funds, 10 % from the state, their own funds and sponsors, 5% only from a ministry and 5% from the state and different funds. The rest did not answer this question. Financing did not depend on any evaluation of effectiveness indicators for 81% of national libraries. The results of the research show that the financing of national libraries has been relatively stable and has not forced the management of the library to adopt a more serious attitude towards the evaluation of the results of the library's activities (Ambrožič, 2003).

The analysis of income-expenditure enables us to get a clear overview of concrete expenditures and income for the library (Aru, 2001).

The calculation of income-expenditure in libraries is carried out according to the *EVS-ISO 2789:2007 International library statistics* standard, which is the basis for national statistics. Libraries primarily use statistics for strategic planning, as legal evidence when applying for funds, to help with financial decision-making, for observing the results of their own work, for making comparisons with other organizations, for informing national and local organizations etc. (EVS - ISO 2789, 2007).

In terms of library economics, the *ISO 9230:2007 Information and documentation – Determination of price indexes for print and electronic media purchased by libraries* standard offers the methodology necessary for determining the price index of library collections, and this enables libraries in addition to evaluating their collections and instruments, to also orient themselves better, for example, in regard to negotiations with booksellers and publishers (ISO 9230, 2007). The long-term budget of the library or the forecasting of expenditures concerning complementary costs depends on this.

The Status of the National Library of Estonia and Financing in the Estonian Public Sector

This section of the article presents an overview of the positive and negative aspects of the legal status of the NLE in public law and its financial activities.

The National Library of Estonia carries out the tasks of a public and parliamentary library, and a special library for the humanities and social sciences according to the National Library of Estonia Act. The National Library of Estonia is an information, science and cultural institution established on the basis of the National Library of Estonia Act, and its main objective is to support the development of the Estonian Republic and each person by cooperating with other information and library organizations in collecting, preserving and making accessible information resources (Statute of the National Library of Estonia, 2006).

In developed countries (foremost Anglo-American countries), the economic activities of universities, libraries, theatres, healthcare centres and so on are handled as the activities of non-profit organizations. Until recently, this term has not existed in Estonian legislation (Haldma, 2005), and its introduction is related to the library reform that has been conducted since Estonia regained its independence. Along with public libraries being placed under the responsibility of the local government, the local people as the direct users of library services were also given the right to make decisions regarding the library. Therefore, the massive dissolution of libraries (as happened, for example, in Latvia) was avoided. University libraries were taken from state ownership and made the responsibility of public law universities, which was the only solution for supporting the specific needs of the teaching and scientific work of the universities (Ottenson, 2008). Now they have the status of research libraries.

The activities of the NLE are financed from the state budget, their own earned income and other financial resources. The NLE budget is a top-down budget, but there are also some characteristics common to a bottom-up budget method. The budget is formed on the basis of the budget strategy and developmental plan of the Ministry of Culture. At the macro level, it uses results-based budgeting characterized by applying the principles of results-based management. A perennial budget strategy and the results of the previous budget period form the basis for this approach. The main assumption for the success of results-based budgeting is a strong connection between the results desired by society and the outcomes of public sector organizations (e.g. services) on the one hand, and on the other, the connection between accounting and budgeting (Handbook of Financial Management: 1 and 2, 2001-2007).

The legislation that regulates the library's activities and financing resources has the greatest impact on the autonomy of the library. The plurality of financing sources and the freedom to use these finances determine the financial autonomy of the organization. The library has more right to make decisions and to coordinate its activities if it has different financing sources.

The status of the NLE in public law as a legal body gives it more freedom to act, but also causes many problems; for example, there is considerable pressure from the National Audit Office of Estonia to increase the percentage of earned income in the library's total budget.

Legal bodies in public law could be referred to as being in the "sphere in-between" – they are in neither the state nor the private sector – they fulfil important tasks for the state and for society, but they have to be quite independent from the power of the state because of the uniqueness of their tasks. Universities are of public law *par excellence*. For example, the status of the NLE as a legal body in public law is somewhat more emblematic and is an inevitable outcome of the prestige of being a national representative institution. The status of legal body tends to be awarded to large institutions, and therefore their foundation based on the initiatives of citizenship is impractical and also improbable. Beyond this, legal bodies operate on the basis of a special law and usually they have been given a new status, but they were established during the Soviet period (Herkel, 2001).

The highest management authority in legal bodies in public law is the council. There is only the sum of an institution's allowance in the budget of the ministry. Therefore, officials of the ministry may have a number of questions. What do they do with this money? Is it possible to economize? Why do they need such independence? The ministries do not always understand that such legal bodies are not subdivisions of the ministry, but cooperation partners. There has been much confusion and tension in forming the budget. Until recently, the status of legal body has not been regulated at the state level in regard to when the special status of these institutions is acknowledged, when private protection rules are applied and what the role of the academic or parliamentary councils is in presenting budget applications (Herkel, 2001).

In countries that are good examples for Estonia, an open society has been built up on the basis of such legal bodies. There is a need to specify all the rules and to acknowledge the principles of legal bodies better in Estonia (Herkel, 2001).

The Development Tendencies of the National Library of Estonia 1996–2006

To obtain a theoretical background for the empirical analysis of income-expenses at the NLE from 1996 to 2006 and an overview of the dynamics of the budget – the financial economic activities and the strategic management of the NLE – the author of the current article elaborated upon the annual reports and action plans of the NLE as well as the economic annual reports and strategic development plans for the NLE.

First, the NLE's strategic development plan for the period to 2000 was compiled in 1996 and foresaw concrete action plans and finance projects for each year. Concerning the development of services, the expansion of priced services was important according to the principle that information has a price and this price has to be paid. No payment is taken for using the publications on site, delivering general information and providing supportive consultations. Self-financing was applied in the publishing policy of the library, so that every publication has to have finances from the budget or sponsors or income gained from sales. Concerning the budget deficit, it was important to find additional resources, for example, by offering conference services for different institutions and finding external financing from funds and sponsors. Concerning financial management, an economical regime was necessary as was the need to observe spending priorities (Strategic development plan for the years 1996-2000, 1997).

The most important task in any year was to work out and implement the principles of a personnel policy originating from the principle of less personnel and the political division of labour, and also from the principles of results-based management with the expansion of rights and responsibilities to lower levels of management (Strategic development plan for the years 1996-2000, 1997).

In 1996, the summer vacation was given collectively to employees in order to save administrative costs – 300 000 Estonian kroons were saved.

The action plans for 1997 and 1998 viewed observations about spending priorities concerning the financial management and the acquisition of additional money from funds and other sources. It was decided to turn more attention to in-service training for the library's employees and to start applying the principles of managing a service enterprise, which means concentrating on the consumers of the services and their needs. Studies in library economics were planned, in which options for project work in the library were analyzed. Observing processes, gathering expert opinions and questioning specialists were the methods used (Action plan 1998, 1997).

The synthesis of the 1998 report and the 1999 plan was innovative among annual reports at the NLE. It did not concentrate so much on detailed descriptions of what was done and will be done, but on analysing work processes (Annual report of NLE 1998…, 1999).

From 1999, the NLE as a legal body did not have an opportunity to defend a budget in parallel with the Ministry of Culture or the Ministry of Finance as has been the case in previous years (Annual report of NLE 1999…, 2000).

The budget for 2000 was designed conservatively and did not cover the expenses from the tasks enacted by law, and did not ensure the strategic development of the library. The activities of the library were only successful in those spheres that did not demand large financial investments (Annual report of NLE 2000…, 2001).

The NLE development plan for the period to 2010, confirmed in 2001, is a strategic document that helps work out annual action plans and formulate development tasks. Its status as a legal body and the determination of its role in the Estonian public administration system, working out the clearly formulated transparency of the activities and finances of such public sector organizations, were brought out as critical success factors and main risks (Development plan of NLE for the years 2002-2010, 2001).

The NLE had a plan to invest approximately 16 million Estonian kroons to improve the conditions for storage and preservation in 2001. Priority number one was to assure the preservation of the national publications. An application for a loan of five million kroons was submitted to the government, and the plan was to use these funds to improve the conditions for conserving and restoring national publications that had been ruined by mould and other problems. This situation had become urgent by the poor quality of the restoring and conserving techniques, which could not ensure the necessary conditions for preservation. The loan funds would also cover improvements to the lighting and the purchase of additional shelves (Annual report of NLE 2001…, 2002).

The means for financing in the period 1999–2003 did not ensure the strategic development of the library according to the increasing demand for new information services. The administration of the building was becoming more complicated because of the obsolescence of the building, the depreciation of the technical network and the growth of budget items. Top specialists left and the competitiveness of the library in the labour market diminished because the average income earned remained lower than other scientific libraries. The opportunities to increase the capacity of the library's real activities diminished because of the rising prices. The level of the main services of the library is only retained because of the increasing income from economic activities and the stability of the special-purpose financing (Annual reports and action plans of NLE from 1999–2003).

Accession to the European Union and NATO were the most important events in 2004 for the National Library of Estonia and for Estonia in general because it opened new perspectives by creating opportunities to participate in different projects financed by the European Union. Focus on analysing the financial management and the application of results, internal controls and fostering a disciplined approach to the budget were given special consideration. A new budget system was formulated (Annual report of NLE 2004…, 2005).

The budget for the NLE in 2005 was intensive, but the development of its main processes improved regarding growth in the appropriation of the state budget, stable income from economic activities, growth of targeted financing and the general condition of the library. It was important to build up training facilities for users, so that additional resources could be gathered to cover the expenses of the library, for example, by renting out rooms, organizing paid vocational training etc (Annual report of NLE 2005…, 2006).

The acceptance of changes to the NLE Act was another important event concerning the development of the library. The library's main task as described in the Act is scientific and development work in addition to gathering objects of national cultural value, preserving them and making them and other information assets accessible. This change created the opportunity for the NLE to acquire the status of a centre for scientific and development work, and this satisfied the prerequisites for better financing of development activities. The 2006 budget for the NLE enabled it to increase the income of its employees, especially in positions that demanded a higher education. There were also changes to the condition of the building, which improved the working environment for visitors to the library considerably. Certain guarantees were required in order to continue the renovation work, for example, about how certain funds were going to be invested. It was possible to realise the plans for 2006 mainly due to a better analysis of the budget, income from the library's stable economic activities and having successfully joining EU projects (Annual report of NLE 2006…, 2007).

Analysis of the Main Costs of the National Library of Estonia 1996–2006

As the first, theoretical part of the current article already attested, measuring the results of the work of the library via analyses of statistical economic indicators – income and expenses – is one way to ensure the effective work of the library. Statistical data from economic indicators is used by the NLE for strategic planning, to support applications for funds and for making decisions. Statistics are inherently retrospective and thus only provide information after the occurrence of events. Nevertheless, future plans should be based on solid statistical foundations (EVS-ISO 2789:2007, pp. 22-23).

There has been proportional growth in labour costs according to the changes to the main costs of the NLE, except in 2000 when the costs remained stable compared to 1999, and there was a small downtrend in 2003 according to the data in figure 1.

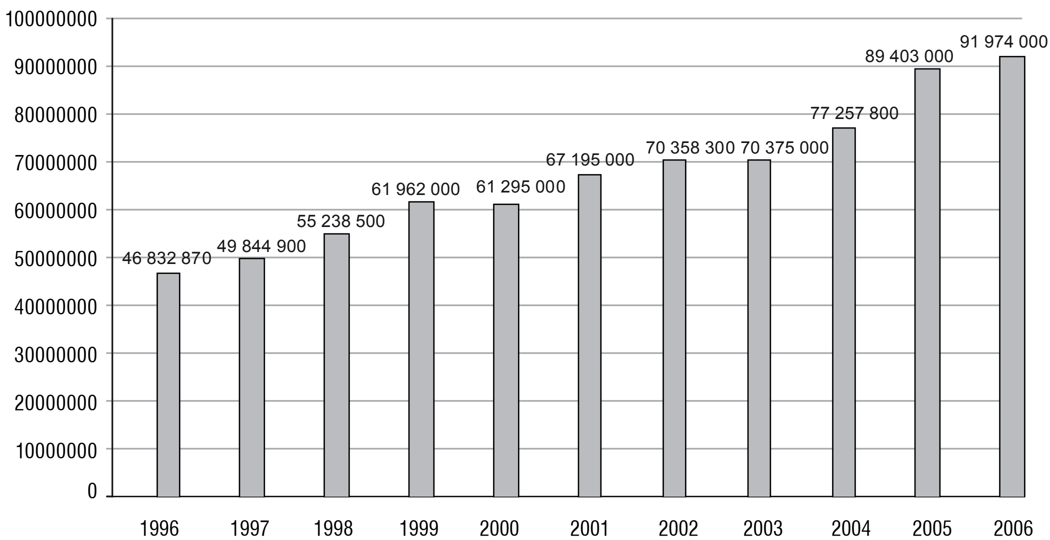

Figure 1: The Dynamics of the Budget of the NLE from 1996 to 2006 (in thousands of kroons)

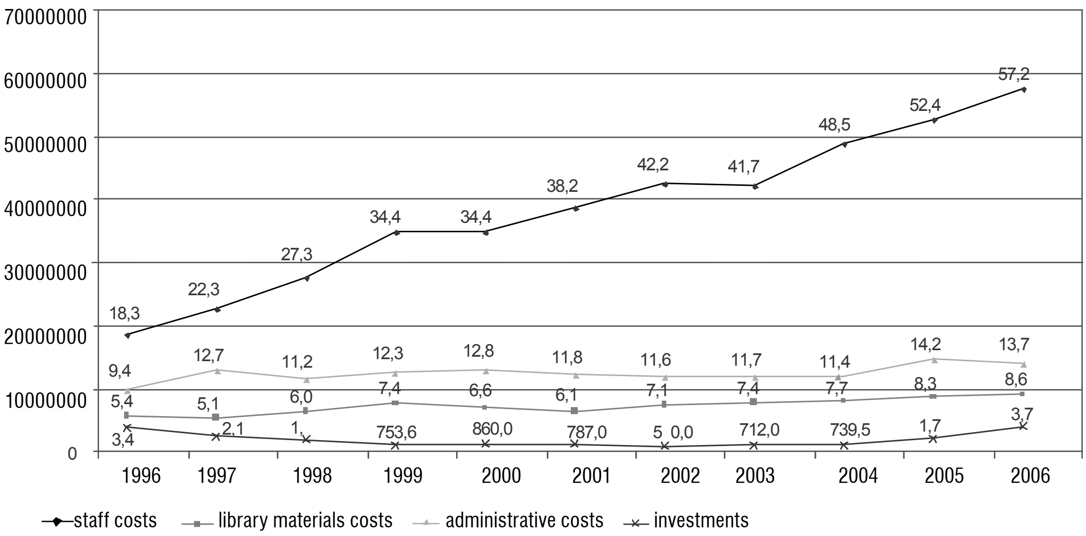

Figure 2: The Dynamics of Regular Expenses at the NLE from 1996 to 2006 (in thousands of kroons)

The trend for the costs of space is relatively stable from 1996 to 2004. Heating and electricity costs increased in 2005–2006. The growth in the trend for completion costs is relatively constant, with small changes until 2002, when growth can be noticed again. The trend line for investments also starts growing from 2005 – many reading rooms were overhauled, and the building and technical systems were renovated (Figure 2).

The largest part of the library's budget consists of staff costs (with FICA) throughout this period – 41% or 19 140 000 Estonian kroons in 1996 and 61% or 56 548 200 Estonian kroons in 2006 (Table 2 and Figure 2).

The relative importance of staff costs for the NLE as a research library is considerable, and this largely stems from the need for higher specialist skills compared to school libraries. The number of employees at the NLE has decreased – there were a total of 525 employees, including 469 librarians and 56 other workers in 1998, and by the end of 2006 there were 433 employees, including 351 librarians.

Calculations of staffing costs per employee cannot be used to provide an average salary, because many other additional costs concerning personnel development are added, for example, those employees hired on the basis of special contracts (gardeners, employees related to certain projects).

Administrative costs form another large expense item, which comprises management costs related to immovables and rooms – 9.78 million or 20% in 1996, 13.646 million or 15% of the budget in 2006 (Table 2).

The relative importance of the cost of library materials in the budget is not an adequate indicator for deciding whether the cost of the materi-

Table 2: Regular Expenses at the NLE (percentage of the budget) from 1996 to 2006

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Staffing costs	41%	50%	53%	55%	56%	58%	61%	59%	63%	59%	61%
Administrative costs	20%	26%	20%	17%	21%	20%	17%	17%	15%	16%	15%
Library materials costs	12%	10%	11%	12%	11%	10%	10%	11%	10%	9%	9%

als is great or small. These amounts in the budget are different in different years and they depend on different factors. It is important that the percentage of the budget used to cover the cost of library materials is bound by an average limit, below which it is not permitted to plan to cover materials costs from the budget. In addition, the content of the collections and their correspondence with the demands of information consumers should be analyzed and first of all the growth of the quality of the collections planned *(Nuut, 2001*). The relatively low percentage of the material costs at the NLE is common to almost all European national libraries (for example in Ireland 10.4%, in Lithuania 7%, in Latvia 14.1%, in Poland 4.3%, in Sweden 4.1%, in Finland 6.4%, in Denmark 11.3%) (Nuut, 2001).

The main role of the NLE is the comprehensive acquisition of national literature, and therefore a large amount of the documents acquired come in as legal deposit copies at no charge to the library. Legal deposit copies are necessary concerning how little they actually cost to produce because it supports the procurement of Estonian literature and makes it easier for the library to purchase foreign scientific literature (Nuut, 2001). In addition, cooperation agreements with different embassies offer good opportunities for the procurement of collections from Nordic countries, France, Germany and other countries.

The absence of unified financial reports aggravates the application of the method of financial analysis in libraries. It is difficult to match the standards of accountancy and the standards of the work of the library, which is the basis for such analysis and comparison of activities with libraries all over the world. It was hard to accurately determine the financial value of cost articles in previous years. The indicators presented are much more reliable and easier to analyse because the calculation of expenses is now done according to the ISO *2789 international library statistics* standard.

The transparency of the financial analysis aggravates the changes in inflation at different times – the growth of inflation according to data from the Bank of Estonia was 23.1% in 1996, 11.2% in 1997, 8.2% in 1998, 3.3% in 1999, 4% in 2000, 5.8% in 2001, 3.6% in 2002, 1.3% in 2003 (e.g. in European Union it was 2%), 3% in 2004, 4.1% in 2005 and 4.4% in 2006 (Annual indicators of the Estonian economy, 2008).

The Analysis of Income from the Economic Activities of NLE 1996–2006

Economic pressure and the decision of the Estonian Republic to decrease expenditure in the state budget in 2008 made it necessary to seek options for improving the functioning of public organizations, including libraries. Therefore, the income earned from economic activities is becoming increasingly important for the NLE because an important part of the costs of maintenance and other activities are covered in this way – currently repairs and covering the growth of administrative costs.

The position of marketing manager was created in 1999, and the selling strategy and costs policy improved as a result of this. The tasks of marketing and public relations at the NLE involve contributing to a seamless quality customer service via delivering information. The purpose was to change the transparency of the work of the library, and to achieve a situation where employees and different client groups are informed about what is going on at the library and what is offered (Annual report of NLE 1999…, 2000).

The greatest gains from activities at the NLE in recent years have been through the following services: *conference services, leasing and renting* rooms to other institutions (these income articles formed 69% of all incomes from economic activities in 2006), *publishing, bookbinding, restoration and duplication.*

The sale of the journal “Library” has proven profitable. There are 6 issues per year and the number of copies printed every year has remained 800–1000 copies per issue. The journal is partly self-financed – for example, the printing costs are paid by a donation from the

Ministry of Culture, the salaries of employees are partly paid from sales and partly from a grant from the Estonian Cultural Endowment Fund. *Information services* have been given on the basis of contracts to different constitutional institutions and state institutions. *Training services* began to be offered at the NLE when the training room and special computer class were completed in 2006. This service wasn't offered before because the necessary facilities did not exist. There were some small courses, but these were presented among *other services*. The part played by exhibition services was marginal (emphasis was placed on NLE exhibitions). Year by year new exhibition spaces were added and income increased. The income article other services currently includes transportation services, guided tours in the library, photographic services, the rent of visitor rooms etc. (Figure 3).

Income from the NLE's own activities as a percentage of total income has tended to remain between 9–10% over the last ten years. Strong competition on the conference services market and the limited parking around the library lim-

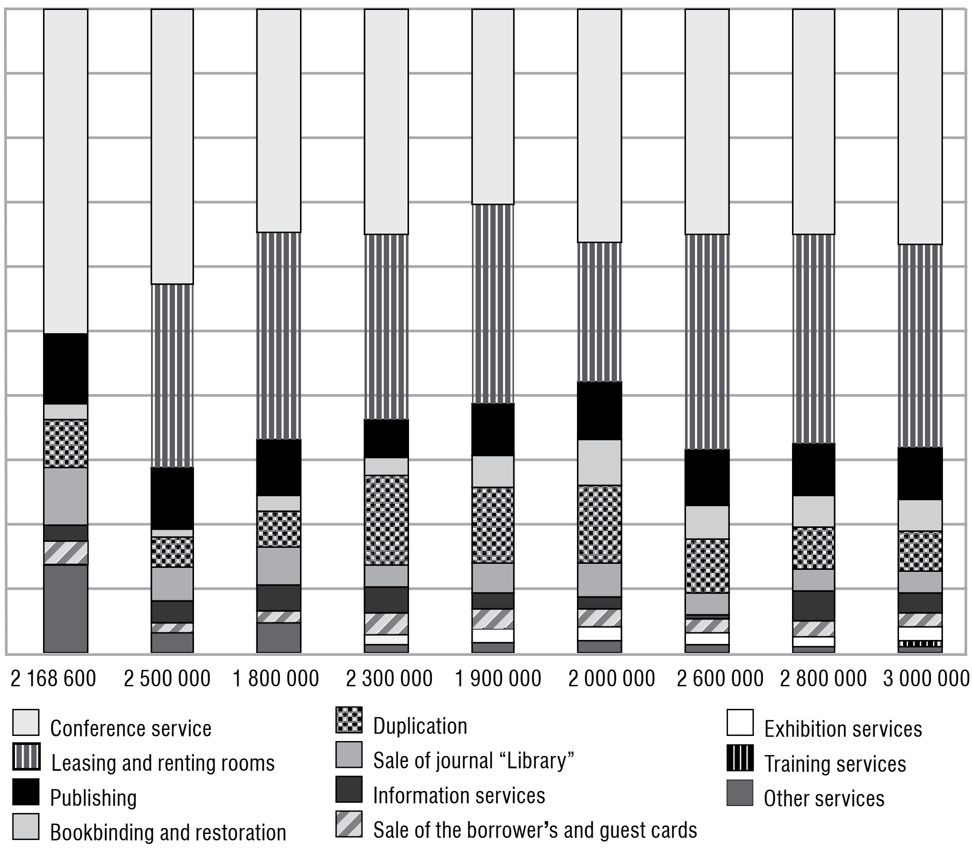

Figure 3: Main Sources of Income at the NLE from 1998 to 2006 (in thousands of kroons)

Table 3: Distribution of Income from NLE's Economic Activities from 1998 to 2006

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Staffing costs	84%	84%	85%	84%	84%	84%	85%	85%	85%	84%	85%
Administrative costs	9%	9%	8%	10%	11%	10%	10%	11%	11%	11%	10%
Library materials costs	7%	7%	7%	6%	5%	6%	5%	4%	4%	5%	5%

ited the sale of NLE services, and more information services are available for free on the web. Income from publishing activities has been relatively modest over the years because more publications are published electronically.

In addition to the finances from the state budget and income from its own activities, the NLE has special purpose financing from the State Chancellery of the Republic of Estonia, European Commission, Ministry of Culture, Cultural Endowment of Estonia and the Nordic Council of Ministers' Office. The proportion of self-financing was 6–7% in 1996–1999 and this has been decreased to 4–5 %.

The role of the finance manager is increasingly valued in the library. It would be ideal if the finance manager at the library could also acquire an understanding of information and library sciences or vice versa. The top managers at the NLE need a partner to work with them in strategic planning and the management of their primary activities (planning and analysing). Strategic management should involve a collective decision-making process. The economic environment surrounding libraries has changed and will change even more. Finance managers have become key people in regard to change management and in the process of relating the results and the strategy (*chief metrics officers*) and overall results-based management. The role of traditional finance managers has changed – finance managers who can ensure the sustainable development of the enterprise and make well-founded forecasts are more valued (Rabi, 2005).

Summary

The NLE has a responsible role before the state and the nation of Estonia as well as the international cultural public. This role includes preserving cultural memory, heritage and Estonian literature; running the centre of national bibliography and the parliamentary library; providing an information resource for the Parliament of Estonia and other institutions on the basis of law; and providing a training centre for the development of library sciences and a cultural centre. This responsibility necessitates a diversely educated and highly qualified team of employees, collections and electronic databases that correspond to the demands of the library's target groups, contemporary information technology, comfortable reading rooms etc. These are what help libraries work at a contemporary level.

The successful work of the library requires better planning of all resources, and this requires an increased understanding of financial management and planning for the employees of libraries and the information sector. Developed countries already understood this in the 1980s, when new discussions about the field of library economics were published. However, the research done in 2003 among European national libraries showed that the need for comprehensive financial analyses and competencies was not only given a lower estimate in Estonia. National libraries are used to obtaining their main support from state or local governments. Although libraries are not enterprises that earn a profit, there is still a need to find additional resources for activities and development by raising funds and participating in international projects.

The NLE has always sought possibilities to increase its own finances. The range of services provided on the basis of a fee has been enlarged. The proportion of funds from the NLE's own activities in the total budget has increased. An important part of the costs of running the building and the library's activities is covered by income from these activities and services. Therefore, a complete analysis of the NLE's own incomes is needed: which services should be offered and at what price (taking into account competing institutions), the cost of rent should correspond to the demands of the market, opportunities for developing new services and so on. All this assumes the drafting of a map of possible services offered in the organization.

Although the summative proportion of the special purpose finances has remained at the same level, there has been a decrease in the percentage of the change. The NLE has joined many international projects after Estonia entered the European Union. This has not improved the financial condition of the institution all that much. Currently, the NLE is participating in 2 projects financed by the European Commission where the NLE's own rate of participation is 50%. The use of support funds is impeded because of the high cost of participating.

While analyzing the financing of the NLE on an annual basis, we may conclude that Estonia's flagship library is under financed. Despite repeated efforts to increase expenses, in the period 2000–2006 mainly only grants for employment costs have increased and this has been the result of employment agreements between the government and TALO, and which the institution must cover at the expense of other items. Employees were laid off in order to maintain the level of wages in 2009 because of this. The maintenance of the collections, budgeting for the building and rooms and the proportion of other important expenses has decreased in the budget, in spite of price rises, and this has become a real obstacle in achieving the strategic purposes of the library. In the context of price increases that started in 2007, it is crucial to increase support for the NLE from the state budget. Leaving the managing costs at the same level forces the library to cut the costs of its main activities and put the sustainability of the entire organisation in danger .

This study refers to the need to specify the legal basis of legal bodies in public law in order to contribute to the growth of the effectiveness of the activities of public institutions, including the NLE, to make the financial basis stronger and to enable organizationally and economically important decisions.

The library needs to work out and apply a system of organizational indicators for its further activities to provide a more concrete strategic direction for the activities of the institution and enable a better evaluation of what has been achieved. The importance of the finance manager at the library cannot be underestimated.

The task of the finance manager is to foresee future trends, but also to analyze retrospectively, and to concentrate on strategic questions and value creation and on the wider picture of organizational development.

Obviously it is good that libraries and information institutions have the opportunity to compare themselves with similar institutions elsewhere in the world. Unfortunately, in the limited capacity of this article, it was not possible to conduct a closer study to compare financial management and analysis in other national libraries in Nordic and Baltic countries or across the EU, which would without doubt provide a more complete picture of development tendencies in European national libraries.

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