



Business Establishments Processes in Eritrea – Success and Failure Factors

By

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Abstract: This article addresses the issue of establishing a new business venture in Eritrea, since the country's independence in 1991. By making a literature review, a survey study, a focus group discussion and interview with those who attempted to establish a business entity in the market it will describe the historical development of the establishment processes. The establishment process is discussed by keeping a strict focus on the main actors that operate in Eritrea, the activities being conducted by those actors and the resources available and how they are being utilized and exchanged in the Eritrean market. In the description focus is put on the critical events that occurred, the main problems that cropped up and the main opportunities in the course of the establishment process. Mainly, the article endeavors to make a judgment of whether the establishment attempts have been a success or a failure and thereafter it will draw lessons of the main reasons for success and failure. Finally, in view of its findings it will conclude by making

managerial, research and policy implications. Conclusively, the main obstacle for business establishment is found out to be the hostile attitude of the government towards the private sector. The second main obstacle is the state owned command economy network of relationships which is the main hinder for firms in the private sector to build a successful position in the market. The third main obstacle is the inexistence of a market economy network of relationships that can provide firms in the private sector with the resources that they need to perform their operations. The overall obstacle of the private sector in Eritrea is the government's entrepreneurial and economic vision myopia. The only opportunity is the promise of the government to have created conducive business atmosphere which never existed and materialized in reality.

Introduction

Several studies of establishment processes conducted until the 1990s focused on developed countries and the developing countries markets were not given due attention. Some of the studies that focused on developed economies were Hammarkvist *et al.* (1982); Mattsson (1983); Johanson and Mattsson (1985); Lee (1991); Nazeem and Bolte (1992); Axelsson and Johanson (1992) and Kinch (1992). The main conclusions drawn from those studies were that, there exist tightly structured networks in developed countries. Consequently, establishment was defined as developing a position in already existing networks. In those markets as a firm already can have a position in the existing networks; establishments can be done by consolidating further the already existing position. When getting established in the markets of developed countries, the two most important problems that a firm has to solve in order to be successful in its position building are the contents of the bid and the establishment form.

The lack of focus in developing countries (economies) was said to have created a knowledge vacuum, as much was known about establishments in developed countries as briefly discussed above. Not only that much less was known about developing countries, but there lacked knowledge about the market structures, how they function and how they can determine establishment of firms in less developed countries in general. To fill this knowledge vacuum, Abraha (1994) studied the establishment processes of Swedish companies in Kenya. The main conclusions drawn from this study were that a well structured network of industrial relationships, industrial competence and industrial tradition do not exist in the Kenyan market. The other conclusion drawn was that, to succeed in its establishments attempt, a firm has to build a focal relationship with an actor that maintains a dominant market position with the help of the government's market policies. Moreover, as adequate industrial relationships don't exist in the market, if the developed focal relationship is going to function properly, the establishing firm has to

build a network of supporting relationships. Moreover, it was also concluded that in order to build a well functioning network of supporting relationships and if the network is going to function properly once it is developed, the firm must be able to deal with government relationships properly in advance.

Based on the research implications of Abraha (1994), Abraha and Hyder (1997 & 2000) conducted a further study of establishment processes in Kenya and Tanzania and confirmed Abraha's findings and arrived at some other interesting conclusions. Some of the findings were that developing countries in general, display different cultural, social, economic and political constraints that can influence the process of establishment. Until those and other relevant differences are properly recognized, understood and dealt with appropriately, it is difficult for the Swedish firms to deal with customers and other significant actors' relationships properly which are some of the major features of firms establishments in developing countries. Accordingly, when a supplier from the developed world interacts with a client or another partner from the developing markets, those differences create a big gap and misunderstanding among them making their relationship complicated, difficult and time consuming to handle. The partners differ in their understanding and application of the different economic and marketing concepts, which can further complicate the establishment process, which is mainly composed of relationships building and relationships management. Recognizing and aiming to bridge the above mentioned gaps among actors with their home base in different countries from different levels of development and different economic systems and consequently to facilitate the establishment process, Ghauri and Holstius (1996) have developed a matching model.

Another study of Swedish firms' establishments by Abraha and Mukhtar (2002)¹ was conducted in other branches in Kenya than those which were examined by Abraha (1994) also following his research implications. It was also found out that establishments in those branches were also significantly different from those conducted in other branches earlier. Accordingly, in order to increase their market share and to build a strong position in the local market, international firms entering the Kenyan market have to develop

¹ The empirical evidence used in writing this article was collected by Abraha during his field work in Kenya in 1988 and 1992 to collect information for his doctoral dissertation. The data was further up-to-dated by collecting information through telephone interview in the year 2000 and 2001.

flexible financial packages for their customers. As the markets on those branches were very limited, the regionalization of product developments and marketing strategies were recommended in order to achieve economies of scale in production and marketing, which in combination would enable the establishing firms to build and strengthen their competitive edge and position development. Illegal importation, corruption and importation delays were also observed to be some of the bottlenecks that the establishing firms encountered and which they should deal with appropriately. Inspired by the different kinds of results that were observed by examining Swedish firms' establishments in different countries' markets that existed in different levels of developments, Abraha and Kaynak (2002) studied Swedish firms' establishments in an emerging transition economy of Poland. Their empirical findings illustrated that the main problem that the establishing firms' have to deal with was to convert the planned economy network into a market economy network and to use the transitional economy network as a stepping stone in the transitional period. The other main conclusion of this study was that the state-owned enterprises were holding strong positions, and the success of foreign firms establishments depended very much on the relationships that they could build-up with the dominant firms holding a strong position in the local Polish market with the support they were getting from the Polish authorities during the socialist (communist) era. The establishment process in Poland was also affected by another environmental factor and that is the hierarchical organizational structure that created efficiency hinder. To deal with this problem the Swedish firms developed a flat organizational structure for their operations in the local Polish market.

In another related study, depending on their adoption of market economy since the downfall of the Berlin wall, Hyder and Abraha (2003) classified Eastern and Central European (ECE) countries into three groups. These are the fast adapters, the medium adapters and the slow adapter countries. Poland belonged to the fast adapter countries and the Baltic States and Croatia belonged to the medium adapter countries. In the above referred article it is observed that establishment process in a fast adapter country Poland differs remarkably from that in the developed and developing economies. Observing and arguing that the market structures, environmental conditions and the level of adoption of market economy in medium adapter countries differs from that in the fast adapter

countries, and as these factors have a major impact on establishment process Abraha et al. (2006) examined Scandinavian companies establishments in two medium adapting countries, i.e., Estonia and Croatia. In the case of establishment in Estonia the establishing firm enjoyed host and home countries authorities' support which really facilitated the establishment process. However, in the case of establishment in Croatia, as the establishing firm didn't enjoy such a support, establishment efforts were time and resources consuming. Moreover, the process of establishment was deterred and complicated by difficulties in reaching customers, lack of mutual orientation and commitment among various actors and of course by bureaucratic impediments. The varying nature of results obtained regarding establishments in different countries and different market environments have further created an interest to Abraha and Zineldin to study Swedish companies' establishments in Mexico. Abraha and Zineldin (2005) examined Scania and Volvo's entry modes and market relationships in Mexico. One of the major observations done in this study was that, to develop a strong position in the Mexican market direct relationship with the customers is a pre-requisite. Tightly structured and well developed industrial networks also do exist in Mexico although it is a developing country. Moreover, government relationships are also found out to be as important as customer relationships. One environmental factor that affected the Swedish firms' establishments is the culture of the old cabs concept. This factor has to be dealt with properly if the Swedish companies are going to be successful in building-up a strong position in the Trucks sector in Mexico. The so far presented studies in different countries and the results achieved have created an interest on Abraha to study establishment processes in Eritrea. Moreover, there are significant differences among how the market functions and what the state promises as how to manage the economy. It is those and other related differences that are considered as the main motives behind examining establishments in Eritrea as the differences can create several factors which can have an impact on the establishment process of firms. The other reason for studying establishments in Eritrea is that the government claims to be committed to the development of the private sector and further claims that it has created conducive atmosphere for the private sector development. It therefore criticizes the business community for being incapable to utilize this atmosphere and to prosper and flourish. It

even has the audacity to declare that there is no meaningful private sector or business community in Eritrea. Those vague and contradictory views and claims presented above have created an interest on the author to study establishment processes in Eritrea in order to identify the success and failure factors, which can help us to determine (judge) whether the government is really committed to the development of the private sector or not. In the next section, the general Eritrean business environment is discussed to be followed by the theoretical frame of reference.

The General Eritrean Business Environment

According to (Miovic, 1994), Eritrea is strategically located in the northeastern part of Africa, neighboring with the Sudan to the west and north, Ethiopia to the south, Djibouti at the extreme southeastern tip and the Red Sea on its east coast. According to the same source, Eritrea is said to have been a country of qualified people well experienced in international trade, commerce and entrepreneurship. Even as early as the 1930s, in Eritrea there were about 730 firms producing industrial products and services and there were about 2,200 companies active in international merchandising. This shows that the country was an active participant in international trade as early as the 1940s. The same source as the above contends that, before the second world-war, European firms were the main suppliers of industrial products to the East African countries. Following the eruption of the second world-war European firms could not continue to supply markets in the East African countries, and the Eritrean industries were capable of replacing the Europeans to supply those markets.

However, starting in the 1950s the economy deteriorated continuously, and following the Ethiopian military regime's command economy policy in combination with the civil war almost brought the Eritrean economy to a halt. In 1991, i.e. during liberation, the country inherited firms that were semi-operational, infrastructure that was nearly totally worn out by the war with an average level of maintenance, an agricultural sector that couldn't meet the country's needs satisfactorily and inadequate health and educational facilities.

“Following, the liberation of Eritrea in May, 1991, the Government launched a major program to rehabilitate the economy and society. This effort is being supported by the World Bank and other donors with contributions towards the Government's Recovery and Rehabilitation Program, aimed at providing foreign exchange to import essential inputs to jump-start the economy. The Government has made substantial progress with their rehabilitation effort. Major sources of growth during

1991/1992 were the increase in agricultural output by 10%; the expansion of industrial sector by nearly 7 percent and the increase in trade and transport by more than 8%.”.....=//=. Eritrea has also made progress in eliminating many restrictive policies of the past, and moving towards a market-based economy, open to external trade, and creating a strong role for the private sector”.

Eritrea Options and Strategies for Growth, Country Operations Division Eastern Africa Department Africa Region, 1994, Vol 1. P-p (1-18), Report No. 12930-ER.

The Eritrean government’s policy to promote private sector-led growth is based in the entrepreneurial tradition that existed in the country for a long period of time. (International Bank for Reconstruction and Development, Final Report, December, 2002). Even though, the Eritrean government has claimed that it is committed to a market-based economy, in practice the authorities are increasingly applying and reliant on centrally planned economic management (Library Congress – Federal Research Division, 2005). The fact that the Eritrean authorities have in different occasions declared that they are following the market economy model, whereas in reality they are implementing a militarist command economy model is also confirmed in Abraha (2004). The authorities promise one thing and do exactly the opposite is also clearly documented in the following source. Claiming that it is committed to privatization and a market economy, the Eritrean government has made priorities of development and economic recovery <http://www.traveldocs.com/er/economy.htm>). In contrast to what they claim, the ruling PFDJ party and the government play active and significant roles in the economy. According to the same source an arbitrary and complex set of regulatory requirements that discourage investment from both local and foreign investors is in place. Nine years after independence, the Conflict Prevention and Reconstruction Unit Report, described the conditions of labor in Eritrea after the border war with Ethiopia as follows: “Eritrea is facing a critical labor shortage, partly the result of the recent conflict. Mobilization has drained white collar and skilled workers, resulting in high female participation rates, rising wages and declining employment. High unit costs are affecting private sector competitiveness and export potential. Swift implementation of the demobilization program coupled with appropriate training is urgently needed.”

Conflict Prevention and Reconstruction Unit, Social Development Department, Dec.2002, p. 1, n.7.

In the same report the government of Eritrea is believed to see the private sector as one of the main forces to promote export expansion, as the main agent of growth that will enable to give a real push to accelerate the economy and that can eventually lead to long-term

growth. From the very beginning, the Government claimed to have considered the private-sector as the main driving force to economic growth and took steps to foster its growth as clearly indicated in this report. Accordingly, due to the impact of military mobilization, manufacturing employment has been declining and wages are rising sharply. Consequently, labor has become a severe constraint on the competitiveness of the manufacturing sector in Eritrea. The shortage of labor has a negative impact on the ability of firms to grow and compete in the regional as well as in the international markets. According to the above source, the rough indicator of competitiveness, unit labor costs, shows that relative to other parts of the world the Eritrean labor is very expensive. This clearly illustrates that, immediate and effective demobilization is very essential and that together with appropriate re-training program of former soldiers should be at the top of the policy agenda. Comparatively speaking, it is the firms in the private sector that are facing acute and critical shortage of labor if we compare them with the state-owned and run firms. Relatively speaking, the state-owned firms are in a much better position to recruit and maintain manpower from both the private and the public sector.

Services were equivalent to 62.4% of the gross domestic product in 2003 (Library Congress – Federal Research Division, 2005). The largest or a main portion of the services sector are financial services and are mainly produced by four Eritrean banks and one insurance corporation in which the government and the ruling party own the majority of the shares. The four banks and the insurance corporation are the Commercial Bank of Eritrea (CBE), the Housing and Commerce Bank of Eritrea, the Agricultural and Industrial Bank of Eritrea, the National Bank of Eritrea, the Eritrean Investment and development Bank and the National Insurance Corporation.

So far we have briefly presented a general picture as to how the general Eritrean business environment is structured and functions as presented in the literature. The Eritrean business environment as discussed in the preceding section differs considerably, from the various countries markets discussed in the introductory section. One of the main differences is that the Eritrean government has in practice a hostile attitude towards the development of the private sector in contrast to what it claims to be. Moreover, there is an excessive and incompetent self serving government intervention in the economic life of

the country as demonstrated in Abraha (2004). On top of that, the government is the main and monopolist actor in the Eritrean market that utilizes its political power and the various resources it owns to dominate the market. Finally, as concluded by Abraha (2004), the Eritrean government has built up a militarist command economy network of relationships which facilitates its own firms operations. This militarist market and economic network of relationships exists and operates both in the domestic market and abroad. The PFDJ owned economic institutions as well as several public institutions, which the governments calls “private firms” are the only and most significant actors in the above mentioned network. It is this network that this PFDJ owned firms capitalize on to build a monopolistic or at least a dominant position in the Eritrean market. In other words the PFDJ owned economic institutions are established, managed, owned and financed by the resources acquired in the militarist command economy network in order to have a monopolistic position in the market. Moreover, this network functions as the main obstacle or hinder for firms in the private sector to conduct their operations and to build a strong position in the market. This is in contrast to what the state claims to be committed to the private sector-growth led economy. However, in practice it does the opposite and creates critical bottlenecks which really impede the growth of the private sector. Hereafter, the theoretical frame of reference will be presented to be followed by the information about establishments in Eritrea collected through personal interviews.

Theoretical Frame of Reference

Several researchers in various disciplines such as Barnes (1972); Mitchell (1973); Burt (1976); Cook and Emerson (1984) and Katz and Shapiro (1985) have applied the network terminologies and concepts for a long period of time. However, the need of developing networks and exchange relationships with various actors in the process of building up and defending a market position that can determine the success of firms establishments in foreign markets is not given due attention in the works of those researchers.

In order to be able to identify market needs, to mobilize resources in order to produce the goods and services required and to make them available in the right place, to the right customer, in the right time firms have to be interconnected in an exchange of

relationships with various actors in the market. Such an approach can help firms to cement their relationships with customers and to develop a competitive position which is difficult for competitors to excel. Therefore, in such a market situation some of the most important questions to understand and handle for possible success are how the network looks like, how it functions, who are the most significant actors operating in it, what are the most critical resources and who possesses them, which are the essential activities performed and by whom. What are the most significant issues to be dealt with for successful establishment is also another crucial issue to be understood and managed properly in this approach. The theory of marketing in industrial markets which is specifically called “the network approach” and mainly developed by Hägg and Johanson (1982); Hammarkvist et al. (1982); Johansson and Mattsoon (1988); and Håkansson (1987) is the approach that can help us to understand this market mechanism. The concept of establishment process is defined in this approach as follows:

“To get established in a new market, that is new to it, the firm has to build relationships that is new to it and to its counterparts. Sometimes this is done by breaking old, existing relationships, and sometimes, by adding a relationship to already existing ones. Initiatives can be taken by both the seller and the buyer. A supplier can become established in a network that is new to it because a buying firm takes an initiative.”
(Johanson and Mattsson, 1987, p.36)

The discussion of the network approach and the definition of the establishment process presented above demonstrate that the application of the establishment process model developed by Abraha (1994) from the theory of marketing in industrial markets is an appropriate tool to be applied in the current work. We will therefore present the establishment process model briefly hereafter.

The Establishment Process Model²

The direct investment theory and the network approach of foreign market development and establishments were the two different approaches taken into consideration, discussed and compared before developing a model of establishment process in (Abraha, 1994). Developed on the basis of the theory of internationalization, the direct

² This section is adapted from the earlier work on the establishment processes conducted by Abraha (1994). This model was applied with some developments and adaptations in different country environments by Abraha and Hyder (1997, 2000), Abraha and Mukhtar (2002), Abraha and Kaynak (2002) and Abraha and Zineldin (2005).

investment theory (e.g. Vernon, 1966; Kindleberger, 1969; Hymer, 1976; Dunning, 1980; Doz, 1986; Porter, 1986; Hennart, 1982) supposes that establishment process in foreign markets is carried out by implementing the strategic plans laid down by management. The implementation of the plan is the sole purpose of the single firm, according to the investment theory. To ascertain success, the establishment process of the firm has to be planned in advance and the elements of the plan have to be adhered strictly and implemented carefully. The fact that the cooperation with other firms is totally neglected in the direct investment theory as it implied that the whole establishment process is a full responsibility of the top management of the firm is also confirmed by (Abraha and Mukhtar; 2002). The establishment process of a firm according to this theory is believed to be dictated by the strategic vision set by the management of the firm not by market realities and developments and how firms handle the reality in the market.

In contrast to what is claimed in the direct investment theory, the network approach provides a totally different picture of the market structure and how it functions. As discussed and addressed in Johansson et al (1994), the network approach puts focus on the number and types of business relationships built-up with the other firms in the market and with the other actors that are active in the development of those relationships. In this approach, establishment processes is defined in more or less the same way by stating that if one considers the market as a network, establishment means that the establishing firm obtains a unique position in a network which is new for the firm and its counterparts (Hammarkvist et. al, 1982)³. Accordingly, establishment process can take place when a firm enters a new geographic area and also when a firm using new or existing products' develops relationships with new customer groups. The establishment process model applied in this work is developed from the theory of marketing in industrial markets developed by Hägg and Johansson (1982), Johansson and Mattsson (1988), and Håkansson (1989), and which is usually called "the network approach". The approach and its main components are discussed and presented in detail

³ This definition of establishment process is also quoted in Abraha (1989), "The Establishment Processes of Swedish Firms in Kenya – A Model of Case studies" and it is also adopted in Abraha and Kaynak (2002), "Foreign Market Entry in a Transitional Environment: The Case of Swedish Firms in Poland."

in Johansson and Mattsson (1984, 1987), Håkansson and Johansson (1979, 1987), Johanson (1989), Mattsson (1983) and Eslsäcker (1984).⁴ Various studies of business network relationships and international business connections developments are carried out both in the domestic and international market by (Forsgren and Johanson, 1992; Håkansson and Shnehota, 1995; Blankenburg, 1996) applying the network approach as a frame of reference. Cook and Emerson (1978 & 1984); Burt (1982) and Granovetter (1985) developed and discussed the concepts of social networks. In those works, Industrial networks are viewed as sets of connected exchange relationships among actors who control industrial resources and activities in those works. Both industrial networks and social networks are very much related, however the industrial network refers to the exchanges of various resources and the activities performed in the exchange process, whereas the social network refers to actors and their social relationships. The main difference being that, the network approach mainly addresses the exchange of various resources where social relations are an integral part of industrial networks.

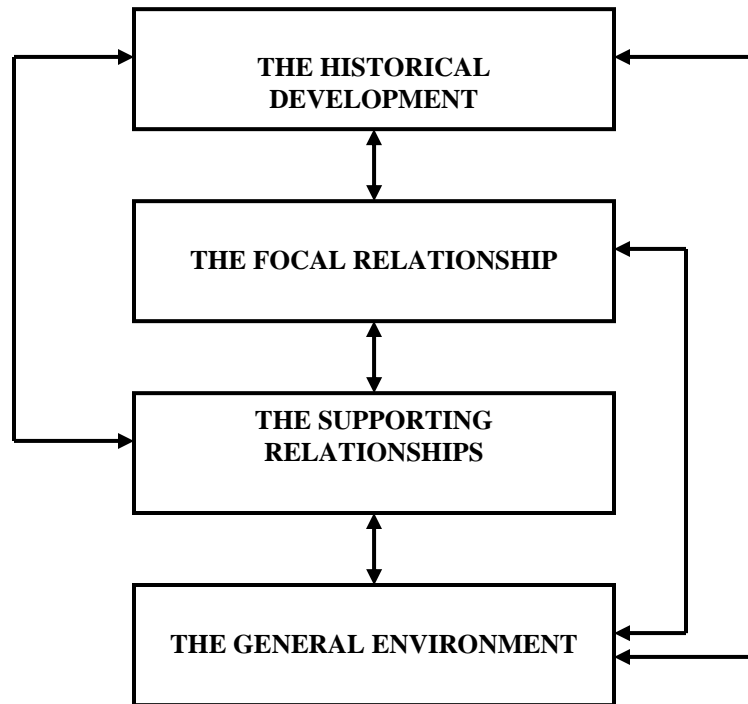
The model of establishment process developed on the basis of the industrial network approach briefly discussed above is applied as a conceptual framework in this work. After reviewing the literature that deals with establishment process, Abraha (1994) found out that most research on establishment process focused on developed countries and the developing country markets have received much less attention. It meant that, understanding of establishment processes within the context of developing countries remains an issue for future research. To bridge the gap, Abraha (1994) examined Swedish firms' establishments in Kenya by applying the above referred model⁵. This research resulted in Abraha's doctoral dissertation titled "Establishment Processes in an Underdeveloped Country: The Case of Swedish Firms in Kenya."⁶ As it is clearly illustrated in **the model (see Figure 1)**, below establishment process in developing countries is observed to take place in four stages, as developed and applied in Abraha (1994).

⁴ This section is adopted from Abraha (1994), "Establishment Processes in an Underdeveloped Country – The Case of Swedish Firms in Kenya."

⁵ This model was developed by Abraha (1994) on the basis of the network approach and applied in his doctoral dissertation.

⁶ This section is adopted from Abraha and Kaynak (2002) , "Foreign Market Entry in a Transitional Environment: The Case of Swedish Firms in Poland:"

FIGURE 1. The Establishment Process Model



The four phases (variables) are (1) the historical development of the establishment process, (2) the identification and the discussion of the focal relationship (s), (3) the various supporting relationships developed by the establishing firm, to enable the focal relationship (s) to function properly, and (4) the general or the macro-environment. Abraha (1994) conclusively recommended that such a study should also be directed towards other countries that differ from Kenya in some of the variables considered in his study. The studies conducted on the basis of this recommendation and the conclusions arrived are discussed in detail in the introductory section. Considering the conclusions and recommendations of Abraha (1994) and the other related studies' varying and different and significant findings by conducting studies of establishment process in different countries markets, **the specific aim of this article is to examine how establishment processes in developing countries and specifically in the Eritrean market looks like.**

Methodology

A focus group composed of six respondents have participated in the discussion that is used as a method of collecting information about the historical development of the establishment processes of the six firms presented hereunder. The six respondents prefer to remain anonymous and they will be referred as R1, R2, R3, R4, R5 and R6 hereafter. To safeguard the safety of the respondents, the names of the companies, their products, their date of establishments, their location of operations and all other indicative information will not be disclosed. Instead of presenting the companies one after the other, i.e. separately all the information gathered will be consolidated and be presented in a combined form.

The respondents were asked to read the written report and to make corrections if any misunderstanding has occurred. After reading the written report, the respondents have made some minor comments and the final version is prepared on the basis of their comments. The method applied for choosing the six firms is convenience sampling. The respondents in the six firms were not chosen by the author, however the author didn't have any other choice rather than to accept those who were willing to provide him with the necessary information. About ten people working in the six firms that the author has contacted to provide him with information have refused to do so.

Information regarding how the Eritrean government runs the economy is provided by three Eritrean experts. The fourth expert contacted refused to be interviewed and made a very brief comment on the information provided by the three experts⁷.

The Empirical Findings of the Establishment Processes

The Initiation Phase

The licensing processes to start operating in Eritrea was described to be time consuming by R1, R3, R4 and R5, moderate by R6 and efficient by R2. The process is either easy or difficult or moderate depending on in which sector of the economy, the applicant wants to operate. If the sector in which the firm applied to conduct its operations is in

⁷ His comment is the last sentence in presenting the empirical findings in this study.

the priority list of the government, the licensing process is not only time consuming, but the license might not be granted at all. Even if the license is granted, the firm might be paralysed to conduct its operations by certain critical obstacles created by the state, so that it will operate at a loss and to finally close down its business after a certain period of time. In other words, the government red tape is the main stumbling block for the firms to obtain a license and to conduct their operations once the license is granted.

According to R3 and R5 one typical and tricky method is applied by the government to limit or discourage Eritreans in the Diaspora to establish business firms in the sectors which are in its priority list. Although, this information was provided by R3 and R5, it was also confirmed by the other four respondents although they didn't encounter it directly in their business. The process goes like this. A certain individual or a group of people submit an application to obtain a license for operating a certain business in the market. Upon the receipt of the application, the applicant is instructed by the authorities to make a feasibility study of his business concept (ideas), to select a site for his business and to deposit a certain amount of money in the Eritrean banks. Here is a very tricky method (motive) to be underlined or noted. The applicant must deposit a certain amount of capital in the local currency Nakfa, however he has to prove to the concerned authority that he had bought the local currency by selling his hard currency in the official market, i.e. in the Eritrean banks. If the application is rejected it is very difficult to convert the money to hard currency. Even if the applicant manages to convert it to hard currency, he losses a considerable amount of money as the exchange rate changes to his disadvantage. Therefore, it is not only that one can't conduct the planned business; however he has almost lost his capital as he can use his money only in the domestic market. As indicated above if he can buy hard currency he has lost a considerable portion of his capital due to the continuous depreciation of the local currency and the fluctuation of the exchange rate.

Once the authorities have received the feasibility study conducted by the applicant(s) and the deposit of the required capital, they can come with certain delaying tactics to start the business. Firstly, the applicant can be told that the business activity that he wants to conduct is one of the priorities of the government and it will not be allowed for

private business men to operate in this sector of the market. Secondly, there is also another method applied to discourage the applicant(s) and that is to tell him (them) to look for another site as the site is already selected by the government for other national purposes. Thirdly, the concerned authority most likely with clear and strict instructions from the bosses at the top delays the processing of the application for a long period of time to discourage the applicant. Those delaying and discouraging tactics are really time and resources consuming processes which make people really desperate. Due to those and other similar obstacles several Eritreans in the diaspora gave up their business plans (missions) and withdrew their applications understanding the government's hostile attitude towards the establishment and development of the private sector. One of the two respondents' applications was rejected and the other applicant got his license approved after waiting for a long period of time. Even the individual whose license was approved conducted his business for a short period of time and he was finally compelled to quit due to the various government red tape that he encountered in his operations. A reasonable amount of license fee was paid depending on the purpose of the business and the types of products and services to be produced.

The Implementation Phase

According to four respondents, in contrast to what the government claims to be and promises to the business community, there is a strong government intervention in the market in general. Respondent 1 narrates that his main problem was to get the raw materials necessary to produce his final product, the shortage of labour and the lack of financial resources especially the hard currency to import the necessary raw materials. The respondent lacked hard currency to import directly, at the same time as his business volume was very limited it would have been better for him to buy from local sources, although the sources of the raw materials were very much limited in the local market. If the government had allowed for the private sector to flourish and prosper, there could have existed enough suppliers of the required raw materials in the local Eritrean market.

The case of Respondent 3 was also of a different nature. The respondent had enough financial resources and with the approval of the concerned Ministry could make the necessary goods available to sell in the market. The bottleneck for his business was that, he couldn't compete with the PFDJ owned economic institutions. This is because the state-owned economic institutions enjoyed an advantage of the economics of scale in purchasing as they could buy in voluminous quantities in order to satisfy the needs of their dominant position in the market. They also enjoyed economies of scale in transportation, storage, marketing and distribution. Consequently, they could sell their products at much lower prices than the firms in the private sector, which was a real competitive disadvantage to respondent three. This disadvantage crippled his operations in the market and his market share declined continuously. This was the case in a very small portion of the market which was competitive otherwise the main and major portion of the market was dominated and monopolized by the state-owned economic institutions as they were operating as importers, decision makers, market regulators, producers, distributors and consumers. It is the militarist command economy network of market relationships which enabled the PFDJ owned economic institutions to build strong relationships among themselves which was not only difficult, but also completely impossible for firms from the private sector to penetrate and to deal with. This was a two-edged sword for firms in the private sector. One is that they can't penetrate the existing network which is built by the state to the benefit of its own companies, so that they will be able to build, maintain and strengthen their market position. Moreover, firms from the private sector couldn't build a market economy network of relationships as most of those that existed stopped to operate and as new ones were discouraged to start. The government policies and practical intervention on the economic life of the country are the main hinders for the building up and development of the market economy network of relationships. This clearly demonstrates that the state is not committed to the development of the market economy and the private sector, in contrast to what it claims to be in different occasions. The socialist oriented market network which was the legacy of Ethiopian colonialism in Eritrea was also partially systematically destroyed under the pretext of the privatization program developed by the government, however which was never materialized. A certain portion of the socialist

oriented market network which was deemed to be appropriate and viable was inherited, adapted and incorporated into the militarist command economy network created by the PFDJ regime.

One of the respondents encountered the following problem in his operations. As a supplier of a certain service he competed with several other companies in which very clear selection criteria were set. However, in the supplier selection process the criteria were totally ignored and an arbitrary procedure which was even difficult for the decision makers to explain and justify was applied. Not only it was unfair but the selection criteria factors were not fully evaluated and even before the process was finished, the deal was given to another competitor. As a contender the respondent was not even informed officially that a decision was made. The decision maker is a government body composed of several individuals, which are accused of receiving kick-backs under the table from the so called winner. Even if there were no kick-backs paid, this really shows that what really matters is your personal or social connection that determines, not how competent you are and what you offer to the buyer of the service i.e., how favourable your offer is to the customer. This clearly demonstrates that it is not a matter of being qualified or competent, but your contacts with the decision makers and how much financial benefits that you can offer to the decision maker that really matters. In such a situation it is difficult to think of an efficient and effective service which can lead to customer satisfaction. High quality services are very essential in the optimization of resources and providing a satisfactory service and product to the users of your products. Not only providing high quality services, but such an unfair method of supplier selection will also hinder the development of competent and qualified service providers. In other words, such an unfair method of supplier selection hinders the process of developing a competitive market. In the absence of fair competition, competent and qualified service providers it is difficult to think of effectiveness and efficiency which are some of the main pre-requisites to develop a competitive market, to develop competitive firms both in the domestic and international market, to economic growth, development, prosperity and social justice.

The General Environment

In this first part, the general environment as described by the first six people (R1-R6) interviewed will be briefly discussed. Especially, since the beginning of the border war with Ethiopia Respondent 3 faced an acute shortage of labour. It is not only respondent 3, however all firms that were granted to operate a private business faced an acute shortage of labour since the beginning of the border war. This is because during the war almost all the available working force was recruited in the army. Here is another perplexed paradox created by the state. The government owned institutions didn't face an equally acute shortage of labour as they were allowed to maintain most of the labour force they had if necessary and they could even recruit manpower from the national service directly and even from the private sector indirectly via the national service. This shows that the shortage of labour created during the border war didn't affect the state owned institutions to the same extent as it did affect firms in the private sector. To the contrary the border war created an opportunity to the state and its economic institutions to recruit whatever manpower they needed in the name of the border war and national development programme. Not only that, but it was also observed that the government supplied labour to the private sector from those recruited in the national service. If one compares what the people in the national service are paid with what the state earns by selling their labour to the private sector, it can definitely be stated that this was also one of the other main sources of income for the government.

According to all respondents, most of the governmental institutions are inefficient, bureaucratic and time consuming to deal with. On the first place when you approach a certain government official you are given an appointment for a specific date without any specific time. If you then approach the person in charge on the date of the appointment, after waiting for a long period of time, he will tell you that he is in a hurry and he can leave you without giving you any specific date and specific time for another appointment. This time and resources consuming nature of dealing with the various authorities' relationships is one of the main obstacles or constraints for firms operating in the private sector.

Another unnoticed or unidentified problem of the Eritrean economy is the contribution of diaspora Eritreans in different forms. Some of the contributions are compulsory and some are indirectly or more or less compulsory. These contributions are some of the main sources of finance of the PFDJ as a party and the economic institutions it owns. The more the contributions, the stronger the PFDJ party financially and the stronger the PFDJ financially the more it monopolizes the market with its serious negative impacts in the structure and mode of operations of the market in particular and the development of the economy in general.

The Economic Plan and the Budget Problems

Three highly qualified Eritreans and internationally recognized economic development experts, have this to say as to how the government is running the economy of the country. All the information provided by the three experts is shaded and presented hereafter. **In Eritrea since national independence there doesn't exist a national economic plan. By corollary, there is no nationally consolidated budget. As a result, every ministry operates on project basis. Any particular ministry presents its own project to the Ministry of Finance. The Ministry of Finance in turn forwards the project to the macro policy at the office of the president. The macro policy office forwards the project to the president for his consideration. Thereafter, the final decision of the president is the plan. This clearly demonstrates that there is no coordination of plans between the various ministries. And in most cases, the ministries work at cross purposes with contradictory objectives, which eventually result in massive losses of manpower, material and financial resources. According to the three highly qualified and internationally recognized economic development Eritrean experts, there are two ways of making national plans as presented hereunder.**

1. **Every ministry in the country can develop its sector plans across the country. The sum-total of the sector plans becomes a national plan and the national plan should be presented as a proposal to the national assembly for approval. If approved it becomes a national plan. The plan could incorporate short term plans which can cover a period of 1-**

3 years, or medium-term plans which cover 4-6 years or long term plans which can cover up till 10-15 years, depending on the size of the economy. The other way is:

2. All regions develop their own regional plans and present their plan as a proposal to their respective regional assemblies. Once the plans are approved by the regional assemblies, the plans are presented to the central government which in turn presents them to the national assembly. If approved by the national parliament, the sum of all regional plans becomes the consolidated national plan. When the national plan is approved at the same time a national budget has to be proposed to the parliament for approval. Once it is approved it goes back to the executive organ of the government. And the executive organ pushes it down to the minister of finance, where every sector-ministry plans and budget is publicly declared. Every sector-ministry-regional administration is responsible for implementing the plans that are publicly declared. The Ministry of Finance is responsible to provide the resources to every ministry –regional administration in accordance with the respective budget-approved by the national parliament.

The three experts strived to convince the Eritrean authorities to make a political choice as to which of the two alternatives presented above should be followed in preparing the national plan and the national budget. However, the authorities seemed to be incapable of making a political choice according to the three experts. The experts further stated that, this is one of the fundamental points or issues where the authorities failed to prove as political leaders. The first attempt being a failure, one of the three experts continued his efforts and tried to convince a certain minister for the need of a workable and effective national plan. The minister responded by saying that, there is no need for such a plan in Eritrea. Finally, the expert left the minister with disappointment.

The three experts summarized the above briefly presented picture as to how the Eritrean economy is managed as follows, because the government has failed in economic perspectives and vision, as a sub-structure of the society, by corollary it has also failed in the political super-structure. In other wards, the government couldn't institute political organizations that go in harmony with the economic and social-sub structure. The failure of the economic vision in Eritrean leadership has of course consequences in the area of

politics. In other words, the government has no short range, neither medium nor long term national economic plans. One can therefore say that the government is running the economy of the country like a private shop, i.e. a one man shop which makes bookkeeping balance at the end of every day. It is within this environment that one hopes against hope to develop a meaningful private sector in Eritrea.

After reading the transcribed interview above, the fourth expert who refused to be interviewed concluded the discussion by making the follow statement: In this environment, no private sector in his right mind would decide to take economic risks and invest to do business in Eritrea.

Analysis

The empirical evidence presented from the various sources in this article clearly demonstrates that, how the government manages the economy of the country in practice is contrary to what it claims to be doing and to what it promises. To some extent theoretically and completely in practice it is proved to maintain a hostile attitude towards the development of the private sector. Not only the government has hostilities towards the private sector, but it has totally made the nominal ministries non-operational as it is clearly demonstrated in how it mismanages the mismanaged economy, specifically in the issues of the national plan and the national budget. In the absence of an efficient and properly functioning public sector, it is impossible to create an atmosphere conducive for the proper functioning, success and growth of the private sector.

The opportunities of making business in Eritrea are valid only until one starts to operate, i.e. empty promises, but once one starts to operate one has to deal with a myriad of obstacles and constraints on a daily basis. As underlined in the establishment process model, the probability of developing a focal customer relationship(s) is almost equal to nil for firms operating in the private sector. This is because most of the potential focal or critical customers are part and parcel of the militarist command economy network of relationships that is the typical characteristic of the Eritrean market. Because of the

government red-tape and the competitive disadvantage of private firms highlighted in the various parts of this article, it is absolutely impossible to penetrate the state owned network of relationships and build a market position in it for a privately owned firm.

Although it is very rare and in case if a firm finds a customer operating outside the above referred and state owned, managed and strictly controlled command economy network of relationships, it is very difficult for the firm and its counterparts to build and manage a network of supporting relationships for various reasons. Firstly, the PFDJ owned economic institutions can out-compete the private firm and start to supply the customer at an offer which is impossible for the firm in the private sector to afford. Secondly, even if it is not out-competed by the PFDJ owned economic institutions, the firm in the private sector can in the long run face several problems. This can be most of the problems that it might face in dealing with the various bureaucratic governmental institutions. Thirdly, as most of the resources that firms utilize in their operations are under the strict control and ownership of the state, in the absence of those resources it would be very difficult for the firm to perform its operations and to make the goods and services needed available in the right time, in the right form and in the right place for the right customer. In sum, it is impossible and informally prohibited to build and manage a market network of relationships as it would create a competitive disadvantage for the state as a main economic actor and the various economic institutions it owns.

The socialist oriented network of market relationships which is the legacy of Ethiopian colonialism had to be converted into a market economy network of relationships in order to create a favourable economic and business environment for the private sector, as we have observed in the Eastern and Central European (ECE) countries. This was not allowed by the state and that is also a missed opportunity for the development of the private sector. Instead of converting the socialist oriented network to a market economy network, the government has destroyed it in two different forms. Part of it was dismantled under the pretext of the fake government launched privatization program. This is true because the most private sector hostile government can not launch an honest, successful and meaningful privatization program. This part is almost non-existent at present. The remaining part which the state considered to be useful was inherited,

modified and incorporated into the militarist command economy network which is the archenemy of the private sector. Because this militarist command economy network is the main obstacle for the private sector and the main opportunity for the state owned firms, the author calls the PFDJ Central Office specifically and the state owned economic institutions (enterprises), the parasites of the Eritrean economy and the Eritrean people. This is supported by the fact that the PFDJ Central Office and its economic institutions failure to build symbiotic and harmonious relationships with the Eritrean people.

The general business environment which is the fourth variable in the model also creates obstacles for the licensing, drainage of resources and operations of the firms in the private sector. The specific obstacles are the time and resources consuming nature of the licensing process, the various government red tapes in various forms, and the shortage of human capital, the shortage of the financial and material resources.

Conclusions

It is very much more of obstacles, i.e. failure factors rather than opportunities, i.e. success factors for the establishment of a private firm in the Eritrean market. One of the main constraints is the absence of the government's commitment to market economy and the development of the private sector. The other constraint which is very much linked to this lack of commitment to market economy is the existence of the command economy network of relationships, which is really difficult and almost impossible for firms in the private sector to penetrate and develop a market position in it. The main reason which makes it difficult for firms from the private sector to penetrate this network is that there is a very strong interdependence among the state owned enterprises which are active in this network. The main advantage of the state owned economic institutions is that they have a secured supply of resources in order to produce or to make available whatever products are needed in the local market and they have a secured market for their products. This is what the firms in the private sector lack and it is one of the main constraints for their operations and success in the market.

Another main obstacle for firms in the private sector is that due to the government policies and the ownership and management of the various resources in the market, it is very difficult to build a market economy network of relationships which is governed by the rules of the market through the interaction of the various market forces (firms) that are active in it.

The socialist oriented network of economic relationships couldn't be converted to a market economy network of relationships and as a result it couldn't be utilized by the firms in the private sector.

One opportunity for running a private company in Eritrea is the promise of the government which doesn't function in practice. The government claims to have built a business atmosphere which is conducive for the private sector however this is automatically converted to a hostile environment once one obtains a license and starts to conduct business. Another unreliable opportunity is to work in the form of a JV with the government. This is also a risky strategy as the JV can be dissolved at any time to make the firm fully owned by the state.

Several management implications can be drawn from this article. First, a firm should develop a long term market orientation. The short term should be considered as an investment period and returns can be expected in the medium and long range. Second, a firm should attempt to identify a niche in the market and to position itself as a supplier or distributor in the identified niche. Third, management can be successful if it identifies a unique service or product which can not be easily imitated by competitors. Fourth, the identification and development of unique products and services should also be done on a continuous basis as it can enable the firm to build and defend a strong market position.

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