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LEGITIMACY

An Analysis of Three Hungarian–Western European Collaborations

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DRAWING ON A LONGITUDINAL *comparative analysis of three Hungarian–Western European partnerships, it is argued that insight into the different assumptions foreigners often bring to their cooperative arrangements can be gained by framing such contacts as clashes in systems of legitimacy. Focusing on which partners' actions are viewed as desirable or appropriate in their respective social settings helps to illuminate the role of social support in maintaining behavior, as well as the ways assumptions are sustained and changed. These ideas are illustrated by differences between the Hungarian managers and their Western European partners in their approaches to managing authorities, and by an analysis of how Hungarian managers and government officials have maintained their familiar modes of operating despite the change from communism to capitalism.*

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CROSS-NATIONAL COLLABORATIONS are notoriously difficult for participants. Why are some successful, when others of apparently equal promise prove more costly than expected? Even previous cross-national experience does not guarantee success, as the Walt Disney Company discovered with its EuroDisney project. Here, we propose that insight into the difficulties posed by cross-national collaborations can be gained by attention to questions of legitimacy. This chapter presents a grounded theory of the role of legitimacy in collaborations based on a comparative analysis of three Hungarian–Western collaborations.

Heretofore, the problems of conflicting assumptions in cross-national collaborations have been addressed in two ways. One approach is purely descriptive (Townsend, Dow, and Markham 1990). The other approach takes a psychological perspective. For example, Hofstede's (1980) widely cited work summarized the differences among employees in various countries along several dimensions representing differences in values. Similar approaches emphasizing individuals' values and expectations have been taken by other prominent researchers (such as Adler 1991; Erez and Earley 1993), with Tallman and Shenkar (1994) focusing on the equally individualistic decision-making styles. As useful as these approaches have been, we suggest that further insights may be gained by framing cross-national collaborations as potential clashes in the legitimacies established and maintained in different societies. A legitimacy-based perspective would allow us to account for phenomena that descriptive and psychological approaches do not address: the role of social support in maintaining particular perspectives, and the ways in which assumptions are sustained and change over time (Zucker 1991). The concept of legitimacy allows us to bring the "social" back into the study of what, perforce, are contacts among members of different social systems.

Concern with the role of legitimacy in social organization has a long history. It was a central focus of Weber's (1947) pioneering work, and it has received substantial empirical and theoretical attention among comparative institutional theorists (Zucker 1987) and theorists of managerial behavior (Pfeffer 1981), among others. Yet despite three decades of research on legitimacy in disparate management and organizational subfields (recently reviewed by Suchman 1995), the concept of legitimacy has not been prominent in the study of cross-national organizational behavior.

To define the term: actions or practices of organizational actors vary in their legitimacy—in the extent to which they are judged desirable or appropriate within a socially constructed system. First and foremost, legitimacy is fundamentally social; actions judged proper by one audience may be seen as less legitimate by another. Therefore, we would expect that cross-national collaborations, because they involve participants from different social settings, run the risk of clashing with different socially constructed systems of legitimacy. Based on a comparative analysis of a sample of Hungarian–Western European collaborations, we discovered patterns of behavior we felt could best be explained as reflections of the production and maintenance of legitimation under the highly uncertain circumstances of the transition from communism.

Comparative Analysis

Comparative analysis is the term Glaser and Strauss (1967) used to describe the systematic study of comparisons in order to discover a grounded theory of the phenomenon of interest. Theories grounded in data help to forestall the opportunistic use of theories with dubious fit and working capacity. Of course, the data used to develop the theory cannot be used to test it but are used, instead, to establish and illustrate it. This process involves generating a conceptual category from the data and then seeking to establish the generalizability of the category by trying to see if it also applies in other settings.

Study Design

In 1989 the authors began a longitudinal research project to study the then-expected transformation of Hungarian organizational practices and organizational behavior as the political and economic changes shifted these organizations from a largely command economy to a market economy. The study began with four state-owned and two private entrepreneurial companies. However, the two entrepreneurial companies dropped out after changing ownership, and one of the state-owned companies had no foreign collaborations by early 1996 and so is not usable for this analysis. This leaves three state-owned companies with foreign collaborations, with summary statistics provided in Table 12.1.

By the end of 1989, both authors knew the relevant literatures and had direct experience in American and Hungarian organizations. Based on these experiences, we could articulate the differences between practices in the two settings, and we expected the Hungarians to change their practices in response to the forecasted changes of incentives in their expected market economy. We were aware, too, that Hungarian organizational practices and assumptions were deep-seated, and that the changes in

Enterprise	*Location*	*Customers in 1989*	*Ownership in 1989*	*Form of Collaboration*
Elevator company	Capital city	Elevator sales to domestic local authorities and companies, and maintenance service purchased by building owners	State-owned (intent to form joint venture signed in 1989)	1990: Joint venture, 75 percent West European partner + 25 percent original state-owned enterprise
Advertising agency	Capital city	Advertising and media buying for industrial and consumer products companies in domestic market	Small component of a large combine	1990: Alliance agreement with West European agency 1992–1993: Alliance partner attempted to purchase; when failed, ended alliance and founded wholly owned agency
Porcelain manufacturer	Remote village	80 percent of sales through state-owned domestic retail shops; 20 percent export sales	State- and local-authority ownership	1993: Series of contracts to serve as production facility for West European company

Table 12.1. Enterprises with Foreign Collaborations.

incentives still depended on future modifications in government policies. We expected Hungarians' organizational behavior to change, but we did not know enough about how such historically unprecedented societywide changes might unfold to limit ourselves to hypothesis testing. An approach based on the development of a data-driven understanding of the phenomenon was the only option likely to produce an accurate understanding of the changes. Therefore, we selected a sample of organizations that was both small enough to allow us to do the in-depth data collection necessary to understand the complex dynamics of changes in organizational behavior, and also to represent the widest possible range of location, ownership, products, and services salient in 1989.

Sampling Plan

The first sampling dimension is location. This was important in these communist economies because infrastructure and services get poorer with increasing distance from the capital city. Those in or near the capital city had access to phone and fax lines, international transit facilities, the best universities, a skilled labor market, and inexpensive business training provided by foreigners (see Table 12.1 for how these organizations differed on the sampling dimensions). We also expected the products or services provided by the state-owned companies to have an important influence on the necessity and ability to change. First, we avoided those enterprises likely to keep their monopoly advantages longer—what in the West would be public utilities, as well as the national railroad, oil and gas company, and health care and educational organizations. Also, services in communist countries were much less developed than in capitalist ones, and with services' low capital needs and thus low barriers to the entry of competitors, they were expected to experience the most immediate and severe pressures to change. Therefore, this sample includes one service, one enterprise that both manufactured and serviced its products, and a manufacturer. Finally, as transformation commenced, we expected different forms of ownership to facilitate or impede change: privately owned companies should have the most flexibility. Among the state-owned companies, those in the large industrial combines or trusts characteristic of command economies have little local control over their fate; those with local ownership (via local authority) are subject to more local politicking, as the company was also a source of jobs and other local services (Antal 1995); and ministry-owned companies are best able to act independently due to their greater anonymity. Finally, we wanted to be able to contrast those organizations with foreign involvement with wholly Hungariancontrolled companies, so a factor in the selection of the elevator company was its new agreement to form a joint venture with a Western elevator company in the following year (1990).

Data collection in the sampled companies consisted of questionnaires distributed to employees annually, two rounds of in-depth interviews of a sample of employees in 1990 and 1991, in-depth interviews with company executives (and, when available, key board members, bankers, foreign partners and ministerial officials) two to three times annually, and the collection of archival material such as privatization plans, financial records, and newspaper accounts of the sampled companies. Only the interviews with executives and officials and the archival material are used in the present report. Approximately 90 percent of the interviews with executives and officials were conducted at the research site by both authors in Hungarian (with the second author translating); the remaining interviews were conducted by either author alone in either Hungarian (second author) or English (first author). Detailed notes were recorded at each interview; immediately afterward the interviewers discussed the interview at length, and the first author drafted an approximation of it in English for review by the second author. In each organization we had a primary contact who was interviewed each time, with the addition of other executives and contacts dependent on their availability. Over the six years to date, the primary contacts in most organizations have changed; for example, the initial primary contact for the porcelain manufacturer was the managing director, but when he was fired by his governing board in June 1990, the economics deputy director (equivalent to a chief financial officer) took responsibility for the research project. Although other aspects of these organizations' changes have been reported previously (Branyiczki, Bakacsi, and Pearce 1992; Pearce and Branyiczki 1993; Pearce, Branyiczki, and Bakacsi 1994; Pearce, Branyiczki, and Bigley 1996), the present study focuses on these companies' collaborations with their foreign partners. It can be considered an exploratory set of three embedded case studies of legitimation in cross-national collaborations (Yin 1994). However, before describing these collaborations, a brief description of the salient features of the environment facing Hungarian enterprises in 1989 is necessary.

Semiregulated Market Socialism

Hungary entered into a series of economic reforms beginning in 1968 (Lauter 1971), creating an economic structure that has been called market socialism or, more formally, "semi-regulated market-socialism" (Kornai

1992). The pace of experimentation and change—political and economic—accelerated in the 1980s, what is commonly known as the period of "reform communism." However, as Kornai (1986, 1990; Kornai and Matits 1984) notes, despite reforms designed to provide managing directors of Hungarian state-owned enterprises with simulated market incentives, these organizations did not face market incentives in practice. Nevertheless, by the elections in the spring of 1990 (in which the communist party lost its control of government), the Hungarian economy had a substantial private sector of small entrepreneurial companies. In Hungary, perhaps to a greater extent than in other communist countries, economic (and to a large extent, political) changes have been evolutionary rather than revolutionary. Finally, for this discussion, we need to distinguish between company executives and those in the government ministries or (before 1990) those holding purely communist party offices: the former will be referred to as executives, the latter as officials.

The Collaborations

Beginning in 1985, the Hungarian government provided incentives favoring foreign joint venture arrangements. Further, as part of the evolutionary economic change in October 1988 it became possible for state-owned (and private) companies to become joint stock and limited liability companies. In this way, all or part of a state-owned company could be sold. A few companies, such as the elevator company in our study, were able to combine the various government programs to form joint ventures that were, in effect, a legal transformation or "spontaneous privatization" (for more on Hungarian spontaneous privatizations, see Branyiczki, Bakacsi and Pearce 1992).

The First Mover Advantage: The Elevator Company's Successful Joint Venture

In 1988, the state-owned elevator company had become independent of its large industrial trust, but only by carrying a proportion of the trust's massive debt. To find a way out from under this debt burden, the managing director initiated talks with the three largest multinationals in its industry to discover their interest in forming a joint venture to which the actual business could be transferred, leaving the state-owned parent with a small corporate staff, the physical plant, and the debt. As the former chief financial officer said, "We initiated this joint venture because we knew that the heavily indebted company with its old organizational structure and overstaffing needed a foreign partner in its profile to bring in added quality. . . . We expected the foreign partner to bring in better technology, develop know-how and licenses, provide training, help to organize the marketing function, and to ease the situation with a cash injection."

Two of the multinationals submitted bids for the elevator company. The managing director then selected the winning foreign parent, based on its promise to maintain the full profile of the company (design, manufacturing, and service), rent the large production facility from the state-owned parent, and retain the state-owned parent's managing director as managing director of the new venture. Late in 1989, a letter of intent was signed to create a joint venture to be 75 percent owned by the Western European parent. Thus, the joint venture started without debts, could hire only those employees from the state-owned parent necessary for the business, and had a generous amount of cash because the Western parent's purchase price remained with the joint venture. The Hungarian managing director remained in control with foreign-parent employees detailed for limited periods to provide technical training and advice.

Through a sophisticated manipulation of Hungarian law, through Westerners' enthusiasm for breaking into the new markets of the East, and because the state owners were temporarily distracted by worries about their own fate in the unfolding revolution, the managing director was able to favorably position his company for the future. The timing was fortunate; in 1989, no state agencies were in place to control such privatizations, and its owner, the Ministry of Industry, did not oppose it because no state property was being sold. Late in 1989 and early in 1990, however, the media and Parliament voiced increasingly greater concerns that managers of state-owned enterprises had been privatizing the organizations for their own personal gain. During the election campaign, the calls grew louder for the government to introduce some controls to stop spontaneous privatizations. Thus, Hungary's State Property Agency (SPA) was created in the Spring of 1990, and all privatizations not yet finalized were frozen pending SPA evaluation. The sampled elevator company was one of the few enterprises to squeeze through the brief privatization opening of 1989.

The Curse of Being Profitable in a Politicized Environment: The Advertising Agency Fails to Be Acquired

In contrast, the advertising agency, as of early 1996, had not succeeded in its effort to be privatized. As there were few barriers to the entry of advertising firms, by 1989 there was an explosion of new agencies; the sampled state-owned agency, which had never had to compete for business, suddenly found itself in a hypercompetitive environment. In 1989 it was one business unit of a large state-owned combine that owned the capital's fairgrounds and produced domestic and international trade fairs. These fairgrounds are considered a unique national resource, one on which many other companies depend, hence the privatization of this company attracted considerable attention from the media and officials.

In August 1991 the agency's parent company was selected as one of twenty companies to participate in Hungary's First Privatization Program (FPP) of the State Property Agency. This the first large-scale attempt of the newly formed agency to accelerate the stalled privatization of state-owned companies. Several foreign agencies were interested in acquiring the advertising agency's parent. However, because its executives were seeking about US$500 million for refurbishing the fairgrounds, foreign investors lost interest. Further political complexities have arisen over the years as other entities (for example, the local municipality, which claims an interest in the fairgrounds) have become involved. The parent's legal form has been changed and its ownership has shifted to newly created governmental bodies, all accompanied by extensive media attention, emphasizing dark hints of corruption in attempts to explain the delays.

While its parent's executives were occupied with privatization and reorganization discussions, in late 1990 the advertising agency's executives signed a one-year alliance agreement with a multinational Western European advertising agency. Although the agency was distressed by new competition, at that time, it was still one of the largest agencies in the country, and so the Western European agency saw it as a strong potential partner. Initially, the agreement provided that neither party would seek other partners for one year and that the Western agency would subcontract with the Hungarian agency for any Hungarian advertising by its multinational consumer-products clients. Subsequently, the relationship was expanded to cover the training of Hungarian employees and assistance in restructuring the company. After one year, both parties thought this relationship was working well, so the Western European agency, with the collaboration of the advertising agency's executives, made a formal proposal to buy an interest in the advertising agency from the combine. Unfortunately, the combine's uncertain legal status, its highly politicized privatization, and its frequent changes in executive ranks meant that the advertising company's attempt to privatize simply was not a priority for the parent. After three years of waiting to acquire its Hungarian partner, the Western European agency put an end to the alliance and founded its own wholly owned agency in the capital city. This was unfortunate for the studied advertising agency, as it led to a loss of its multinational clients and several key executives and professionals.

Learning by Doing: The Porcelain Manufacturer as a Contract Production Facility

The porcelain manufacturer—a 200-year-old "national treasure"—was also included as one of the 20 enterprises in the State Property Agency's First Privatization Program. Its privatization looked potentially successful to the SPA, because the porcelain manufacturer had received several exploratory visits from foreign porcelain manufacturers during the second half of 1989 and the first half of 1990. The SPA assigned a foreign privatization consultant to the porcelain company to represent the SPA, transform the company into a shareholding company, and then find a privatization partner for it. Yet due to the company's continuing operating losses, its large inherited debt, and the government's requirement that any owner maintain the company's large workforce (in what is an isolated, economically depressed region), no foreign offers materialized. Early in 1992, during this waiting interval, the company's continued losses compelled the investment arm of a ministry (calling itself a bank) and a state-owned commercial bank to take ownership of the company in exchange for the company's debts. This procedure helped to clarify control of the company, but it was control of a neglected but widely loved national treasure with mounting operating losses draining the banks' own resources, with no savior in sight.

In September 1993, the fifth managing director since 1989 determined that because the company had a labor force that was substantially underpaid (even by the low Hungarian industry averages), it might be attractive as a production facility. He began contacting Western European and American porcelain companies with the hope of arranging for them to outsource some of their own production to the porcelain manufacturer. The executives of the porcelain company hoped such contracts would provide the operating profits the owners required, and would supply working models of a more effective, quality-sensitive working culture. By early 1996 they had completed successful contracts with American and Western European porcelain companies, with one of the Western European companies planning future contracts involving major expansions as well as a possible joint venture. These contracts helped produce an operating profit for 1995, the manufacturer's first since the communist era.

Differences in Managing Owners: Managerial Bargaining

There was a key difference in the practices and actions judged to be legitimate by these Hungarian executives and their foreign partners. Though there were many areas of shared legitimacy—for example, problem solving was a respected managerial action by all—we identified one difference that seemed to impair foreign-Hungarian managerial collaboration. This was the expected relationship between owners and the executives of their companies.

The command economy, at least in its late decaying stages in Hungary, involved very little executive receipt of commands or submission to authority, and rather more hard bargaining (Antal 1995; Kornai 1992; Kovács 1988). Bargaining was widely seen as the primary executive task in Hungary. Although the dependence of state-owned companies on the state was extensive under the old system (Kornai 1992; Kornai and Matits 1984), who had power over what was ambiguous most of the time (see Carroll, Goodstein, and Gyenes 1988). The changes of the transformation have, by and large, only made their situation even more ambiguous, and so the executives of these companies continued to bargain hard with others. Bargaining had always been legitimate, respected managerial behavior, and it arose from the structure of dependencies in semiregulated market socialism.

Who has the right to compel obedience from others? Power based on the acknowledged right of the power wielder to do so—legitimate power—has long been of interest to students of organization (such as Barnard 1938; Weber 1947). Yet, who has the legitimate right to set the direction and deploy the resources of organizations was and remains a deeply contested issue in Hungary. Classically, ownership of an organization confers power by means of the legitimacy granted to owners to dictate how their property should be used. If ownership did not imply such legitimacy, socialists would have had no interest in the state ownership of companies. Our own observations suggested that ownership legitimacy in Hungary is a deeply complex question, which, rather than clarifying authority relations, sets the stage for bargaining. Though the ownership legitimacy of small entrepreneurs who founded and control their companies is no different from that found in the West, the same legitimacy is not granted to officials or purchasers of state-owned companies. This weakening of ownership-control legitimacy occurred for two reasons. First, legitimate authority was dispersed among a great many bureaucratic entities, each jealously asserting its "rights" and thus weakening ownership control. Second, beginning in 1968, the reforms intended to foster more performance accountability acted to strengthen the hand of enterprise executives. Each of these is elaborated below.

When Everyone Is in Charge . . .

Control over Hungarian enterprises was dispersed and thus became dissipated. Using agency theory terms (Eisenhardt 1989), these managing directors have been agents with weak principals. Rather than monolithic control over these enterprises, because the party was everywhere numerous entities could claim its authority. Further dispersal occurred in the numerous governmental bodies responsible for different organizational permissions, credits, and constraints. In the late communist period in Hungary, every enterprise had to cope with many other entities that had legitimate authority over certain decisions, and this often resulted in contradictory directives. Thus, bargaining with all those on whom they were dependent became the primary task of managing directors. Kornai (1992: 487) summarized the situation faced by company executives: "The relation between firms and superior organizations is full of vague, accidentally or intentionally ambiguous rules, improvisation, exceptional cases, and personal connections that evade the official 'route.' Various authorities all have a say in a single firm at once, often working at cross purposes. A smart manager learns to maneuver among many superiors, playing them off against each other." Thus, in Hungary to be a smart (admirable, clever) manager is to play one superior off against another.

Thus, the managing director of the elevator company saw little risk in giving the Western European partner majority ownership because he did not see it as a complete loss of control. Not that he and others did not understand that the foreign owners would be able to dictate to them; rather, enterprise executives were used to being dictated to by so many that adding one more to the mix was not nearly as important as the cash and training the Western European partner brought. To the Hungarian audience, good owners would behave like the stern parents of a teenager: they might admonish and seek to control, but in the end they would want to see their children succeed and so would support them with (yet more) money and training.

The Company Is Me . . .

Hungary's market-socialist reforms further strengthened the bargaining positions of managing directors. There were recurrent attempts to make company managing directors responsible for the performance of their companies, to reward them for meeting profit targets, and to provide them with greater discretion in decision making (Kornai 1992). In practice, these reforms handed Hungarian managing directors several strong cards to play in their bargaining with officials. First, because the rules and constraints generated by the different components of the government and party were so complex and mutually contradictory, managing directors could argue that their organizations' performance problems were not their fault.

The bargaining position of Hungarian managing directors was strengthened further by government officials' need to monitor so many companies in such different industries that they could not provide detailed supervision of most of them. Managing directors (or their deputies) had the technical, operational, and industry knowledge. Although detailed accounting systems were intended to control companies, the usefulness of the figures was limited by the complexity of the pricing, subsidies, loans (for numerous different products and purposes) and the lack of clear market tests in the communist trading block (Kornai 1992). Thus, proactive managing directors would gain reputations as successful managers not by reporting large profits but by working these complex entities to extract resources for their organizations—as the elevator managing director had done.

What is more, officials had their own careers to nurture, and, as in any bureaucracy, these were advanced best by demonstrating success and avoiding embarrassment. Officials had no incentive to audit companies' "cooked books" carefully, as they too would benefit from good numbers. The accounts did not reflect reality anyway, and the reporting system was so convoluted at every level that discrepancies probably could never have been uncovered even by the most heroic auditor. Besides, managing directors often had their own good connections in the party and government, and bureaucratic careers in any society rarely are advanced by alienating the well placed. Although there were people who tried to do the right thing despite these incentives, such people generally would not pursue, or last long in, apparat careers. Managing directors, who were well aware of officials' motives, could threaten embarrassment (poor results, layoffs, social upheaval) if they did not get the resources they wanted. Thus, executives grew used to dealing with those with power over them by engaging in negotiation via threats, or what Pearce (1991) has called "blood under the door bargaining."

Finally, the market-simulating reforms begun in 1968 gave company executives a base from which to bargain. No longer was it enough to simply carry out directives as they would have done in a true command economy. Now they were expected to make their companies successful. Executives could use performance objectives to make claims and to mount arguments, an approach that would have been awkward for executives in a purely command economy. An assertive managing director often could gain an upper hand, and any self-respecting one would certainly try.

This managerial assumption about the appropriate way to cope with those in authority played itself out with unfortunate results in our elevator company. This is the only company in our sample in which the foreigners (with their different assumptions about ownership legitimacy) owned the company, thus it provides most starkly the setting in which Western and Hungarian assumptions about managing owners clash. The Western European firm bought its controlling interest in the elevator company at the company's financial peak, and several subsequent events conspired against it. Its new construction market shrank quite dramatically after 1990, because state-owned companies and municipalities no longer built large apartment blocks for their workers or residents and people rushed to take advantage of the private housing market by building houses for themselves. Thus, the market for residential elevators collapsed. Further, the service business faced new competitive pressures. Before 1990, the large state-owned buildings had simply, as a matter of course, contracted with the elevator company for elevator maintenance, but now individual municipalities and tenants' associations had real accounts and had to cover their own costs, so they became interested in purchasing the best maintenance service at the lowest price. The elevator company found that its heretofore stable maintenance business was being poached by small operators who could provide more responsive and economical service. This meant that the profitable, market-dominating elevator company acquired by its Western European parent in late 1989 had, by the end of 1991, developed large losses.

Yet from the Hungarian managing director's perspective, all these changes were the result of environmental forces beyond his control. Throughout 1992, he explained this to his owners. But the owners insisted that the manager, regardless of whether losses were ultimately his fault, implement a plan which would, under the new circumstances, produce profits (or at least staunch losses). The managing director, still operating according to conventional Hungarian executives' expectations, felt that an explanation to his bosses was all that was required: once he had informed his superiors (and if it wasn't his fault), he was done. Only after his superior at the parent had tried for many months to solicit a plan of action from the managing director did the superior finally give up, fire the managing director (and a few other top executives), and bring in Westerners with Hungarian language skills to attempt to turn the company around.

There can be no doubt that the fatal blindness of the elevator company's managing director arose at least in part from his learning to view himself as a successful executive who had earned his autonomy. Had he not, after all, been able to negotiate a very successful privatization, in which he had been able to play two Western firms off each other, and thus increase the amount of money invested in the company? While most other Hungarian managing directors had failed to secure privatization for their companies, this managing director not only had wrested free of the apparat but had been able to choose which rich Westerner would be allowed to pour resources into "his" company. In his Hungarian social context, he was well known for this success; he was the very model of the successful "transition manager." His social environment supported and enforced, on a day-to-day basis, his assumptions about the correct way to manage authorities. Thus he was understandably slow to understand that the requirements of the new owners were quite different from those of the apparat.

We sought to test the generalizability of this idea in the other two sampled companies. But only in the elevator company did the foreign partner gain the legitimate right to direct the company by owning a majority share. The foreign partners in the other two companies were in an alliance and a production contract; thus, from their own perspectives, these Western European partners had very limited legitimate right to dictate to the Hungarian managers, so they did not do so. This is not to say that they did not forcefully assert themselves. But these foreign partners assumed that they would influence the Hungarians via persuasion, by providing useful knowledge, and by threatening to take away their resources if they did not get what they wanted. These were all approaches the Hungarian managers found to be normal, legitimate, and appropriate. The working environment under European communism was harsh (Haraszti 1977; Voslensky 1984) and became even more so in the transition (Pearce 1991; Pearce and Čakrt 1994), and so demands and threats by the foreign partners were seen as normal, even respected, behavior by the Hungarian executives. This is reflected in the following dialogue with the creative director of the advertising agency:

DIRECTOR: Now we [the Western partner and the agency] have gotten to know each other and we have real problems. They sent us accounts from [a major international consumer products company that wishes to sell its products in Hungary]. We had prepared a presentation for [this company] and they were very unhappy. We received a fax from [Western partner's head office] saying [the managing director] WILL be in here for a day-long meeting this Thursday . . . They were very honest and a little bit rude. They said we were confused. 'Media should not be talking about that. The managing director spoke too long. Market research didn't know what it was talking about. The conference room must be changed. You must have Western equipment. The creative people should not be handling products, the account handlers should do that.' And on and on. When the managing director returned she reported all of this to the departments.

INTERVIEWER: Weren't you upset at this rudeness? They aren't your bosses.

DIRECTOR: Yes . . . but they send us the accounts and they do not want to ruin their own reputations with these accounts. We need them. . . . In many things they are right and we need to be trained; everyone is happy to have the training. But in others they don't understand that we cannot produce the information they are used to. For example, in media planning in the West you just call up the television station and ask for the rates and viewer demographics for certain shows. Our television stations don't provide this information, nothing. They don't understand the East European situation.

Similarly, the porcelain manufacturers' contracts with their foreign partners contain punitively high penalty clauses—perhaps an insulting display of distrust in some settings, but viewed as prudent and appropriate by the Hungarian porcelain executives. Thus, in the alliance and contracting collaborations, the Western Europeans and Hungarians understood one another very well, despite the substantial differences in their national cultures and business experiences. In our judgment, this is because these alliance and contract forms of collaboration happen to draw on compatible expectations about the appropriate ways to exercise influence in Hungary, whereas the ownership form did not.

Reconstructing Legitimate Patterns

Meyer and Rowan (1991) suggested that building and sustaining socially constructed legitimacy of action is particularly important when uncertainty is high. Participants engaged in innovative ventures or operating in rapidly transforming environments might be expected to be especially concerned with drawing on actions already established as legitimate by their social set, possibly even to the point where such actions look counterproductive to neutral outsiders. Thus, the greater the uncertainty surrounding a cross-national collaboration, whether from the unfamiliarity of the participants with one another or from the uncertainty of the local business environment, the more likely it is that participants will cleave to their familiar, socially derived notions of what is correct and proper.

The scholarly literature indicates that legitimacy is much easier to maintain than it is to gain or repair (Ashforth and Gibbs 1990; Zucker 1987). Thus, when confronted with the massive change in the system of legitimacy involved in the transformation from communism to capitalism, we would expect participants to seek to maintain their familiar system rather than to construct legitimacy anew. The transformations facing Hungarian managers are unprecedented in the uncertainty they produce. Hungarian managers had grown used to managing change, but only change involving "reforms" that shifted the bargaining partners and perhaps added more complexity and dependencies. While they universally complained about interference, they did understand it. Legitimacy scholars would expect them, therefore, to take active steps to reconstruct the revolutionary change of the collapse of communism into the more familiar pattern of "another reform." We did observe that our sampled state-owned company executives and officials collaborated to maintain that which they understand well. This has been done by fostering a thicket of programs and rules that only an insider could navigate.

In the reform period, Hungarian state-owned companies sold goods and received revenue in return. Some state-owned companies had certain obligations to deliver particular products at government-set prices; however, these were not so much commands as they were markets made captive by currency and other government controls (Kornai 1990). By the late 1980s, state-owned companies were free to add other lines of business, and the government often encouraged certain activities through loans and other incentives. Alas, despite reforms intended to make Hungarian organizations more responsive to customers, fully 70 percent of a company's income came from governmental redistribution decisions (Kornai 1986, 1990; Kornai and Matits 1984) rather than from sales. *Redistribution* is the label given to government appropriation of an organization's revenue (from taxes and complicated methods such as currency reserve requirements) which it then redistributed back to companies. Such distributions to companies came in many forms, with labels that mimicked market mechanisms: investment loans (that could be forgiven behind closed doors at a later date), revolving credit accounts, hard currency permissions for favored exports, and the like. Thus, bargaining sessions with officials were more important to a company's cash flow than any customer (Kornai 1986, 1990).

We observed that the two studied companies that did not succeed in achieving privatization found themselves in much the same situation as they had always known, despite over six years in a market economy. First, their privatizations did not succeed because they were passed among different officials and handed to newly created governmental entities, each reviewing and sometimes altering their demands. The work life of executives in these two enterprises was and continues to be dominated by convoluted negotiations with the complex array of officials and processes that have scared away several potential Western acquirers of each company.

Thus, the managing directors of state-owned companies remain consumed in high-level bargaining and still spend their days dashing off to an official meeting in the capital city, only now they are no longer bargaining solely over redistribution payments but over bankruptcies and privatization plans. Bargaining is what executives are used to doing, it is what they are good at, and transition government policies have made it an activity with higher payoffs than those gained by developing markets and improving product quality. It is not that all executives and officials have consciously manipulated the transition to maintain the old system. More commonly, their routine ways of interacting with one another recreate their familiar environment out of the materials available from the transition.

Further, these two companies continue to receive various governmental subsidies, and no one ever expects the porcelain manufacturer to make interest payments on its large debt (owed to its state-entity owner, which sees no advantage in foreclosing on itself). Although markets are more important to these companies than they were in the reform period, sales remain less important to both of these companies' continued survival than do the bargains struck with various governmental entities. The names of these governmental entities have changed—now they are called the privatization agency or investment bank—but the game remains the same. That this advertising agency and porcelain manufacturer—which were loss-making, nonviable market actors in 1989 and remain so in early 1996—still operate in a putative market economy suggests that Hungary's transition has not been the smooth change in incentives once expected in the conversion from communism to capitalism. These state-owned companies still depend on officials for needed resources and permissions, and officials have discovered that the never-ending privatization process gives them a role similar to the one they played under semiregulated market socialism; these patterns of action are normal, expected, and still pay off for the participants.

Certainly, the Western European partners did not have either the language or connections needed for this kind of bargaining, and more important they did not see it as respectable managerial behavior. Expatriate social gatherings in Hungary are dominated by anecdotes denigrating these processes. In Hungary, therefore, we find that foreigners from the developed capitalist countries prefer to replicate their own familiar social setting by establishing wholly owned new enterprises, hiring younger (more malleable) Hungarians and providing extensive socialization via training in organizational development. Further, those Western partners who find themselves in joint ventures usually seek to rid themselves of the complications of partnership with a state-owned partner by buying out such a partner's interest as soon as possible (as the elevator's foreign joint venture parent did in 1995).

Ironically, even these parallel state and private sectors are nothing new in Hungary, which long has had state and private sectors that operate according to different rules (Stark 1989). However, the revolutionary change of the past few years may be that the private secondary sector, which previously lacked the respectability of the large state-owned enterprises, has now become the prestigious domain. It is possible that this shift in the perceived legitimacy of private companies may be a salient factor in the burgeoning growth of this sector.

Understanding the Role of Legitimacy in Cross-National Collaborations

Analyzing cross-national relationships as questions of legitimacy brings a new perspective to cross-national interactions. First, a focus on legitimacy helps account for the persistence of actions despite shifts in incentives and learning by participants. The different parties carry their own social environments into the collaborative interaction, and managerial interaction, rather than being a private matter between them, is performed before implicit audiences that will judge the rightness of what transpires. In these Hungarian–Western European collaborations, expectations about how good owners behave was an arena of deep difference, whereas harsh threats and demands by powerful people on whom the enterprise depends were seen as legitimate actions by all audiences. When the local managers did not follow the suggestions of their foreign partners, it was not that they did not understand or had not learned what a market economy required, it was that they judged their local audience to be more important. For example, the Hungarian advertising agency retained its media buying and signmaking components, even though it knew that these were not properly a part of an advertising agency in a market economy, because executives believed that layoff announcements would signal financial distress to their Hungarian clients. Maintaining social status in the eyes of one's relevant referent group is a very powerful motivator, sustaining actions despite economic incentives to the contrary. Adaptation that may make sense to the individuals seeking to collaborate may be resisted if it will cause either of them to lose legitimacy in the eyes of their fellow nationals. Conversely, some changes do not violate existing systems of legitimacy and so may be easily accommodated. A focus on the differences in systems of legitimacy can help provide insight into which foreign practices may be more stoutly resisted.

Further, our observations provide the first documentation of how participants react to the uncertainty of changes in institutional practices. Although legitimacy scholars have argued that the greater the uncertainty, the more likely the participants are to cling to socially constructed anchors of legitimate action, previous work focused on static situations that differed in uncertainty (such as education versus commerce). In these organizations we observed that, despite frequent complaints about interfering officials, the executives continued to collaborate in the reproduction of the old complex bureaucratic environment of reform communism. By acting in ways they found comfortable and appropriate, they sustained a system of official interference and bargaining they claimed to despise. This self-defeating behavior could not easily be explained by analyzing economic incentives or describing the participants' values; it requires an understanding of how certain social patterns become institutionalized and then sustained as an anchor of predictability in an environment fraught with uncertainty.

Finally, this comparative analysis suggests that the study of the role of legitimacy and related social forces in cross-national collaborations merits increased research attention. As an exploratory theory-generating study, this work provides no systematic test of these ideas. Although the subject of legitimacy presents barriers to systematic hypothesis testing, these are not insurmountable. Future research might profitably test these ideas regarding the role of legitimacy by using them to forecast the degree of difficulty involved in prospective collaborations. To return to the introductory example, if researchers had assessed the differences in the legitimacy of such actions as self-effacing customer service and corporate control of employees in both Japan and France, they might have been able to better anticipate some of the problems encountered with the EuroDisney project.

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